Tolley®CPD

April 2016

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Budget 2016

Personal tax and NIC (Lecture P946 – 10.23 minutes)

Personal allowances & tax rates

The personal allowance and higher rate threshold for 2017/18 were announced in the 2016 Budget:

	2016/17	2017/18
Personal allowance	£11,000	£11,500
Higher rate threshold	£43,000	£45,000
Basic rate	20%	20%
Higher rate	40%	40%
Additional rate threshold	£150,000	£150,000
Additional rate	45%	45%
Threshold for personal allowance withdrawal	£100,000	£100,000

Termination payments

The Red Book indicates that the tax treatment of termination payment is often subject to abuse. The rules will be tightened up to ensure that the £30,000 exemption only applies in specific circumstances. There will also be a change from April 2018 introducing employer NIC on the excess over £30,000 that is subject to income tax.

Salary sacrifice arrangements

It is well known that HMRC is not happy with a number of salary sacrifice arrangements. This subject will be looked at again with a view to limiting tax exemptions in return for salary sacrifice. However, pension payments, childcare and health related benefits such as the cycle to work scheme will not be affected by this review.

Contracting in the public sector

Public sector organisations will be required to deal with the tax and NIC consequences of IR35 on the contractors that they engage from April 2017. The Red Book states that public sector bodies will be required to determine whether IR35 rules apply and, if they do, to ensure that the correct tax and NIC are paid – presumably by deducting this from the payments made to the intermediary.

This responsibility will be placed on the recruitment agency if the contractor is engaged through one. There are also further promises to simplify the rulers.

Renewals allowance / replacement allowance

As announced in July 2015, Finance Bill 2016 will include measures to abolish the renewals allowance for landlords of fully furnished let property and to provide tax relief on replacement furniture for all residential landlords, effectively reversing the changes brought through three years ago. The new relief is available for expenditure on the replacement of domestic items such as furniture, furnishings, appliances (including white goods) and kitchenware in a let dwelling house. The deduction will be for expenditure incurred on or after 1 April 2016 for corporation tax payers and 6 April 2016 for income tax payers on an item that is substantially the same as the item being replaced, plus any costs incurred in disposing of, or less any proceeds received for, the item being replaced

Class 2 NIC

Although previously much trailed and announced, this budget seems to include a final announcement that Class 2 NIC will be abolished from April 2018. Class 4 will be restructured to allow the self employed to acquire pension rights through class 4 contributions. There is no detail on this issue at present, but it is highly likely to lead to an increase in Class 4 contributions.

Micro-enterprise allowance

To simplify tax for the smallest start up businesses, those with self employed income or property income of no more than £1,000 will be exempt from tax on that income. If their income exceeds this amount, they will be permitted just to deduct the £1,000 allowance rather than calculating their net profit or loss from the activity.

OTS review of Class 1 NIC

The Red Book announces that the OTS will now be requested to undertake research into moving employee NIC on to an annual, cumulative and aggregated basis and employer NIC on to a payroll basis. The terms of reference will be published shortly.

Company cars

The Red Book has confirmed that previous announcements and policy with regard to company car tax will continue, but that the lower end of the table may be reformed to enable focus of incentives on ultra-low emission cars from 2021.

There will be further increases in the benefits charged on cars without an emissions rating to align them with the new higher car benefit charges

As announced in the Autumn statement, the 3% supplement for diesel cars will remain for a further five years; it was due to be abolished in April 2016.

Benefit in kind on vans

The van benefit charge standard benefit amount will increase in April 2017, based on CPI inflation as at September 2016.

Electric vans are being brought within the charge to tax, starting from April 2015 when 20% of the standard van benefit will be charged as a benefit in kind. This was due to rise to 40% of the charge from April 2016, but the increase has been deferred so that the charge remains 20% of the standard amount (£3,150) until 5 April 2018, when the rises will recommence, bringing the charge to 100% in April 2022.

Payrolling benefits

The new arrangements for voluntary payrolling of benefits in kind will apply from 6 April 2016. However, there are some benefits that for technical reasons cannot be included in payrolling arrangements. Finance Bill will make the necessary amendments to the law to allow benefits provided by credit tokens or non-cash vouchers to be taxed through payrolling arrangements.

Calculating benefits in kind

The legislation regarding the calculation of the taxable amount in respect of certain benefits in kind is to be amended to make sure that where tax law provides a specific formula for the calculation of a taxable amount, this cannot be displaced by providing certain benefits based on "fair value" – that is the basis of provision is the same as for third parties.

Disguised remuneration schemes

When steps were last taken to attack disguised remuneration, loans which were already in place at the start date were excluded from the regime provided they remained outstanding and no changes were made to them. The Red Book announces more steps to attack new disguised remuneration schemes that have emerged since the last changes, with an indication that loans still outstanding at 5 April 2019 will be liable to tax at that point if they have not already been subject to tax. Draft legislation is already available and the changes will come through in both Finance Acts 2016 and 2017.

Sporting testimonials

As previously announced, there are changes to the taxation of sporting testimonials for employed sports persons. In broad terms the income tax taxable, but there will be a £100,000 (increased from the proposed £50,000) exemption against income from non-contractual or non-customary. The legislation will apply to income arising on or after 6 April 2017, in respect of grants of testimonials on or after 25 November 2015.

Simple assessment

HMRC will have the power to assess the tax due by an individual without that person completing a tax return where it has sufficient information to make that assessment. The taxpayer will have 60 days to object. The power will come into force with effect from Royal Assent to the Finance Bill.

ISA limit

The ISA limit will rise from £15,400 to £20,000 from 6 April 2017.

Lifetime ISA

The lifetime ISA will be launched in April 2017, and will be available to savers aged under 40. Savers will be permitted to save £4,000 per annum, and a Government contribution of £1,000 will be made into the accounts of those who save the maximum, providing a 25% tax incentive, or more accurately a 20% tax relief at source on savings. Help to buy ISAs can be transferred this into the new lifetime ISA.

The funds will be available at any time to savers who use the savings to buy their first home, and also at age 60 with the Government bonus if it is to be used to fund retirement. There will be provisions allowing savers to use the balance in the account for other major life events, but the Government bonus may be restricted to the purchase of the first home and to use in retirement.

There are further documents available explaining both the practical and technical aspects of this financial product.

Help to save

Low income families will receive a Government incentive to help them save regularly. The schemes will run for two years and savers can receive a 50% bonus on up to £50 per month saved through this period, with the option of rolling over for a further two years, bringing the total saved to £2,400 with an additional bonus of £1,200. The amount saved can be used for any purpose.

Personal savings allowance

The allowance announced last year will be legislated for in the Finance Bill 2016. The draft clauses released in December 2015 have been amended to clarify certain elements of the new allowance, including the interaction with the savings starting rate.

Reduced lifetime allowance

As previously announced, the pensions lifetime allowance will reduce to £1 million on 6 April 2016. The Budget Resolutions put in place both a Fixed Protection 2016 measure and a personal protection 2016 measure, in the same way as for previous changes of this sort.

Pensions – serious ill health lump sums

There will be changes in the Finance Bill to change the taxation of serious ill health lump sums paid out by pensions schemes. For members aged 75 and over, this reduces the tax charge from 45% to the recipients' marginal rate of tax.

Trivial commutation payments

There are a number of technical changes to pension taxation, none of which have very wide impact; however, this change will be useful for scheme administrators. It will allow a defined contribution pension already in payment to be commuted to a trivial lump sum within the existing tax-free rules.

Capital taxes (Lecture P947 -7.31 Minutes)

Capital gains tax rates

The rates of CGT will reduce from 6 April 2016 to 10% for basic rate taxpayers and 20% for higher and additional rate taxpayers. However, the existing rates of 18% and 28% will continue to apply to property sales and carried interest. There are no changes to PPR on the disposer's main home.

Entrepreneur's relief – investors in unquoted shares

A new type of entrepreneurs' relief has been introduced from March 2016 for newly issued shares in unquoted trading companies that are issued on or after 17 March 2016. The shares must be held for at least 3 years before disposal (staring from 6 April 2016), but this change will limit the tax on disposal to 10% on a separate limit of up to £10 million of lifetime gains.

Entrepreneurs' relief – amending previous changes

Changes made in 2014 and 2015 have had some unintended consequences. HMRC has worked with ICAEW and CIOT to identify these and amend the legislation. Where goodwill is sold to a close company in which the disposer has less than 5% of the shares or votes, entrepreneurs' relief will be available on the disposal; this change is backdated to 3 December 2014.

Where there is an associated disposal, the availability of relief was restricted where the disposer did not sell at least 5% of his ownership in the business. This can defeat a family sale of the business, though connected party relationships, so the is also amended ab initio – from 18 March 2015.

A further change will amend the definition of a trading company or group to include the activities of a joint venture company to the extent owned by the group, partially reversing a change brought forward on 18 March 2015.

Employee shareholders

The exempt amount of gains for individuals with employee shareholder status (ESS) will be restricted to £100,000 for arrangements entered into on or after 17 March 2016. ESS is acquired by those employees who forgo some employment rights in return for being able to acquire employee shares.

Company liquidations – income treatment

It is proposed that from 6 April 2016 distributions made by a company on a winding up will be taxed as income where the conditions of a targeted anti avoidance rule are met. These include a condition triggering income treatment if the recipient or a connected person is involved with a similar business in the two years after the liquidation, and the transaction is undertaken for tax avoidance motives. Responses to the consultation on this have yet to be published.

IHT – residential enhancement

The announcement in 2015 of an extra slice of nil rate band for IHT applying to the family home is to be extended where the home has been sold and its value is represented by other assets in the estate. Legislation to achieve this will be included in the Finance Bill 2016.

Additional rates of SDLT

The new 3% additional rate of SDLT will apply from 1 April 2016, and was expected to apply to second homes and buy to let investments by individuals. It has now been announced that the extra charge will also apply to major investors and companies, so that the higher rates will apply on all purchases of residential property other than an individual's main home. The 3% will not apply to properties within the ATED regime, which are subject to 15% SDLT in any event.

New SDLT slice system for commercial property

Following the restructure of SDLT for residential property, Government has now announced a reform of the SDLT charge on business property. The current "slab" system will be replaced by a "slice" system, similar to that now applying to residential property. The rates will be as follows:

Property cost / value	% charge	SDLT on slice
£0 - £150,000	0%	£0
£150,001 - £250,000	2%	£2,000
£250,001 +	5%	N/A

The break-even price is £1.05 million so all purchasers of properties below this value will pay less SDLT as a result of this change. The changes take effect from 17 March 2016.

There will also be a new leasehold rental charge rate of 2% for leasehold rent transactions worth more than £5 million NPV. These transactions are already taxed on a slice basis.

ATED regime – widening the reliefs

Three new categories of property will be exempted from the ATED and related CGT and SDLT regimes from 1 April 2016. These are property:

1. owned as part of an equity release arrangement
2. occupied by certain members of staff, and
3. acquired for demolition or to be converted into non-residential property.

VAT (Lecture P947 – 7.31 minutes)

VAT Registration

From 1 April 2016 the following thresholds will apply:

- the VAT registration threshold will be £83,000; and
- the VAT deregistration threshold will be £81,000.

Overseas Businesses Selling Goods in the UK

With effect from Royal Assent, Finance Act 2016 will give HMRC enhanced powers in respect of businesses established outside the EU who make supplies in the UK via online marketplaces.

HMRC will be able to direct that:

- a VAT representative of such a business must be established in the UK;
- a VAT representative of such a business must be appointed from a specified date;
- such a business must provide security instead of or in addition to appointing a representative.

In the event that the overseas business does not comply with a direction, HMRC will be able (after a period during which the online marketplace may take action to secure the compliance of the overseas business, or to remove it from the marketplace) to hold the online marketplace jointly and severally liable for the VAT due from future sales of the overseas business.

New Criteria for VAT Refunds to Museums and Galleries

With effect from 16 March 2016, the VAT refund scheme for museums and galleries is to be extended to any museum or gallery that:

- is open to the general public for at least 30 hours per week, without exception;
- offers free entry, without prior appointment;
- holds collections in a purpose-built building; and
- displays details of free entry and opening hours on the museum website.

Museums and galleries must apply to the relevant body and must support their application with a strategic business case.

Power to make VAT Refunds to Named Bodies

Government departments are permitted to obtain refunds of VAT which they incur in relation to non-business activities. However, this does not extend to Non-Departmental Public Bodies and similar arm's-length bodies.

With effect from Royal Assent to Finance Act 2016, new legislation will provide that the Treasury may, by order, name any such bodies as 'specified bodies', with the result that they will be able to recover the VAT which they incur on goods or services which relate to non-business activities.

The aim of the measure is to prevent VAT from being a disincentive to cost-sharing arrangements between such bodies. (Such arrangements currently give rise to irrecoverable VAT.)

Any hope of a windfall for a specified body will, however, be short-lived; since the body will be government-funded, the extent of its funding will be adjusted downwards to take account of the VAT which will be recoverable.

Isle of Man Charities and VAT reliefs

For a charity to qualify for the VAT reliefs set out in VATA 1994, it must meet the conditions set out in FA 2010, Sch 6, one of which is that the charity must fall under the jurisdiction of the High Court, the Court of Session, or the High Court of Northern Ireland.

With effect from Royal Assent, Finance Act 2016 will amend Finance Act 2010, Sch 6 to include a reference to the High Court of the Isle of Man to make it clear that charities subject to that court's jurisdiction will qualify for the UK VAT reliefs.

Corporation and Business Tax (Lecture B946 – 11.56 minutes)

Corporation tax rates

The main rate of corporation tax will reduce still further as a result of the Budget announcement. The rates will be as follows for the rest of the life of this government:

Financial year commencing 1 April	Main CT rate
2016	20%
2017	19%
2018	19%
2019	18%
2020	17%

Corporation tax losses

This announcement forms part of the modernisation of corporation tax still further. It is worth noting that the Chancellor referred to corporation tax as "one of the most distortive and unproductive taxes there is" which refers back to the Mirlees review in 2010 which suggested the abolition of corporation tax.

Extending the use of carried forward losses

For losses incurred on or after 1 April 2017, companies will be permitted free use of carried forward losses against any type of income and brought forward losses will also be available for group relief. Losses arising before that date will continue to have restricted offset.

Restricting the use of carried forward losses

However, there will also be a restriction on the use of carried forward losses so that companies can only offset losses against 50% of their taxable profits. The restriction will apply to profits in excess of £5 million, so smaller companies will not be affected by the restriction. There is already a restriction on loss offset by banks, and this will be reduced to 25% in respect of pre 2015 losses.

High-geared companies – interest deductions

The Red Book also announces a restriction on the deduction of interest by companies, which will be capped by reference to UK taxable profits. In principle the deduction will be limited to 30% of UK taxable income, but will apply at net interest expense in excess of £2 million only to exclude smaller companies. There is no more detail on this and no planned start date at present.

Capital allowances on cars

The capital allowances regime has once again been the subject of announcements, reflecting policy around lower vehicle emissions. The following changes have been announced:

100% first year allowances on new low emission cars has been extended to April 2021 (it was due to expire in 2018); the emissions attracting 100% FYA's will be 50g/km and below from April 2018.

The emissions for main rate capital allowances on cars will reduce to 110g/km for cars purchased from the same date (currently 130g/km).

Capital allowances in Enterprise zones

The existing regime for 100% first year allowances in a designated area within an Enterprise Zone has been slightly modified to allow the measure to apply for eight years after the zone has been designated.

Patent Box

The patent box legislation in the UK is widely regarded as too generous, and Finance Bill 2016 will include amendments to the regime to align its provisions with the internationally agreed provisions in relation to tax favoured intellectual property (OECD agreement November 2015). In particular, this will more closely relate patent box relief to the R & D activities carried on by the claimant company. The change will take effect from 1 July 2016.

R & D – SME scheme and state aid

SME's are restricted by state aid rules in the amount of R & D tax relief they can claim – only the SME scheme is regarded as state aid. However, where a claimant company also receives relief under the large company scheme the calculation become difficult from 1 April 2016 when the old large company scheme is replaced by the new "above the line" relief. The legislation will be amended to deal with this issue.

Loans to participators – tax under s 455 CTA 2010

The rate of tax on loans taken out on or after 6 April 2016 will rise from 25% to 32.5%. The tax is payable by the company, and is repaid if the loan is repaid. Obviously, planning will allow loans to be crystallised before that date to reduce the rate of tax chargeable.

Trading income

Where trading income is received in non-monetary form it is possible that it is not liable to tax – the rules are unclear. The Finance Bill will set this issue beyond doubt and ensure that non-monetary forms of consideration received through a trade will be included as taxable income.

Option for quarterly or more frequent payment

As part of the Making tax digital proposals, those businesses which are keeping digital records and updating HMRC quarterly will be permitted to opt for quarterly or more frequent tax payments if they prefer. This will commence in 2018 and will also extend to landlords.

Improving HMRC services

A further £71 million has been earmarked to provide improvements in HMRC services for smaller businesses, in addition to digital developments. This funding will provide:

- By 2017 a seven day week for the main helplines and online support
- A further 800 staff recruited to telephone help lines to cut waiting times. Further improvements to call handling is also on the cards.
- A dedicated phone line and online forum for new businesses providing help with getting started in business and the transition to digital services

Small business rates relief

The detailed scope of these changes are beyond the scope of this session, but in essence they will deliver a reduction in business rates for many smaller businesses. 100% rate relief will be available on rateable values up to £12,000, with tapered relief available up to £15,000. However, there is an interesting development in that the intention to combine business rates with the HMRC digital tax account for businesses has been announced as a longer term plan (for 2020). There may also be a business rates allowance in the future which would allow businesses to spread their relief across more than one local authority area.

Apprenticeship levy

The levy was announced in 2015 and commences in 2017. It will cost 0.5% of the gross payroll of each employer, with an allowance of £15,000 meaning that many smaller businesses will not have to pay the levy. The levy will be available to the employer to spend on apprentice training but if not used will become available to other businesses.

Budget 2016 has announced that from April 2017 employers in England will receive a 10% top up on the funding in their digital levy account which will be available to spend on apprenticeship training.

National Minimum Wage

The main rate of National Minimum Wage will increase to £6.95 per hour from 1 October 2016. There are similar increases in the youth rates. There is no news of the expected rate of National Living Wage from 1 April 2017, apart from confirmation that the rate is on course to reach £9.00 per hour from April 2020.

Business tax roadmap

A new version of the business tax roadmap is to be published shortly. In particular, the road map will:

- cut tax rates to drive growth and support small businesses
- modernise the business tax system in line with international best practice
- ensure a level playing field, with large multinationals paying their fair share of tax

Tax transparency

The Finance Bill will include provisions requiring major companies to publish their tax strategy as it related to UK taxation. There will also be measures to deal with large companies that repeatedly engage in aggressive tax planning or which do not engage with HMRC in an open and collaborative way.

OTS review of corporation tax computations

The Red Book includes a statement that the OTS is to review the options for simplifying corporation tax computations, for which the terms of reference will be published shortly.

New Enterprise zones

Budget 2016 announced the following new or enhanced enterprise zones:

- A MarineHub Enterprise zone in Cornwall;
- Brierley Hill, Dudley
- Loughborough
- Leicester, and
- Extending the Sheffield City Region zone.

Sugar levy

The sugar levy will be imposed on soft drinks production companies at one of two rates from April 2019. The lower rate will apply to drinks with a sugar content of no more than 5 grams per 100ml, the higher rate at drinks containing more sugar than this. Fruit juice and milk based drinks will be exempt. The revenue will be used to fund extra-curricular activity, and in particular sport in schools.

Personal Tax

Too late to code out - Deadline for paying tax through PAYE

Summary – The Tribunal confirmed that the taxpayer had submitted his tax return too late for coding out the underpayment

The taxpayer submitted his 2013/14 tax return online in January 2015 and wished to have the tax due collected through his PAYE. But he did not realise that, for this to happen, he should have submitted the return by 30 December 2014. Eventually, he paid the tax on 24 March but HMRC imposed a late payment surcharge against which the taxpayer appealed.

Decision:

The First-tier Tribunal said the taxpayer's argument that his online statement showed nothing to pay did not constitute reasonable excuse. First, he looked on the day before he filed the return and, second, the website made it clear that tax could not be collected through the taxpayer's code after the 30 December deadline. It was the taxpayer's responsibility to ensure that returns and payments were made on time.

The taxpayer's appeal was dismissed.

Comments – Although HMRC have an arbitrary date for the submission of the tax return for coding out which seems unfair there needs to be a deadline so that practically HMRC can carry out coding exercises. It has been signposted historically and is spelt out on the website so the Tribunal made a fair decision

P Christovic v HMRC TC4854

Was a payment on behalf of a director 'earnings'?

Summary - The First-tier Tribunal (FTT) found that a payment of £75,000 by NEP to HSBC was a payment of Mr Willey's pecuniary liability and therefore should be taxed as earnings.

SA Utilities Ltd (SA) was a company which engaged in the same type of business as North East Pipelines Ltd (NEP). In 2007, Mr Willey and Mr Powell had hoped to expand SA and for that required further funding. Mr Willey and Mr Powell signed a Deed of Guarantee on a joint and several basis in favour of HSBC in respect of the indebtedness of SA. At the same time, the bank required Mr Willey to enter into a second mortgage on his home. HSBC then sought and obtained a second mortgage on a flat which Mr Willey owned. In early 2008 SA went into administration. Mr Willey decided that he wished to continue his business but without Mr Powell. Accordingly, NEP was incorporated and by October 2008 Mr Willey owned the one and only share in NEP and he was the sole director.

When SA failed it owed at least £250,000 to HSBC. Mr Willey was able to negotiate an exit route whereby the mortgages on his two properties were released and he was also released from the guarantee for a total consideration of £75,000.

The appellants contended that the £75,000 paid by NEP was a payment which was not paid by reason of Mr Willey's employment. It was made by reason of the company raising new finance. Similarly the £75,000 payment was not 'earnings' under the NICs legislation. Accordingly, NEP was not liable to pay Class 1 NIC on that amount.
HMRC contended that the payment of £75,000 made by NEP was a payment of Mr Willey's pecuniary liability and should be treated as earnings. The payment was made to satisfy Mr Willey's personal debt. The payment was 'money's worth' as it was of direct monetary value to Mr Willey. While the appellants claimed that the payment provided no benefit or earnings to Mr Willey, HMRC did not accept this because as a result of the payment made by NEP, two mortgages on Mr Willey's personal properties had been settled.

Decision:

The FTT held that the question was whether or not the £75,000 was a reward for services and arose from Mr Willey's employment. It was not disputed that the £75,000 was not 'salary, wages or fee'. The issue was whether or not Mr Willey derived 'profit … or incidental benefit of any kind … if it is money's worth' 'in relation to an employment'. The FTT found that he did. The £75,000 added an unquantified value to his two properties which he later sold. Furthermore it removed him from the prospect of a claim of some £250,000 or more and all of the possible legal costs associated therewith. He was only able to arrange the payment because he was the sole director of a successful company.

The FTT found that the payment only happened because Mr Willey was an employee of, but more pertinently, the sole director of NEP. What he did was as an employee. Mr Willey arranged the payment which was for his benefit. The payment was for 'money's worth'. Consequently both appeals were dismissed.

Comments - On the particular facts this case led the FTT to decide that the payment was only made because, for entirely personal reasons, Mr Willey needed to settle with HSBC. NEP only made the payments because he was the only director and he could ensure that it was made. The case demonstrates the wide definition of earnings which extends beyond 'salary, wages or fee' to deriving 'profit … or incidental benefit of any kind … if it is money's worth'.

Willey & Anor v HMRC TC4913

Tax liability of the restricted shares given as bonuses

Summary – the Supreme Court has found that two similar share schemes designed to avoid income tax and NICs on the payment of bonuses to bankers failed.

Two appeals, *UBS AG v CRC* and *DB Group Services v CRC*, covering similar issues were heard recently in the Supreme Court.

Both taxpayers were investment banks that had entered into arrangements to provide bonuses to employees. The aim was to avoid income tax and National Insurance on the payments.

In the first scheme, a Jersey-registered company, ESIP Ltd, was incorporated, from which UBS awarded restricted shares to its employees. The bank said these were restricted securities within s423 ITEPA 2003 and therefore exempt from income tax under s 425(2). UBS did not control ESIP. DB had a similar arrangement with its off shore company, Dark Blue Investments Ltd.

Conditions were attached to the shares making them subject to forfeiture if a contingency occurred, so as to qualify for the exemption. In the UBS case, the contingency was a specified rise in the FTSE 100 within the next three weeks. The contingency was unlikely to occur, and it was also hedged against so that the employees would lose out slightly, but not significantly, if it did. In the DB case, the contingency was the employee being dismissed for misconduct or voluntarily resigning within the next six weeks. The shares were then redeemable by the employees for cash.

HMRC said the shares were not restricted and the bonuses should be subject to tax. The First-tier Tribunal dismissed the appeals of UBS and DB in separate hearings. The Upper Tribunal heard the cases together and allowed UBS's appeal. The Court of Appeal dismissed HMRC's appeal in the UBS case, but allowed DB's.

HMRC appealed in both cases.

Decision:

In the Supreme Court, Lord Reed agreed with the Upper Tribunal and Court of Appeal that the *Ramsay* principle did not apply. HMRC had argued that the shares were vehicles for passing cash bonuses to employees without paying income tax and National Insurance. Although genuine, they functioned only as a cash delivery mechanism. Acknowledging that the schemes had no purpose other than tax avoidance, Lord Reed said the employees did, though, receive shares as opposed to cash. Further, the realisable value of the shares depended on the performance of the assets in which the companies' funds were invested. The amount of cash for which the shares might be redeemed was neither fixed nor ascertainable when the shares were acquired.

Lord Reed said the condition for UBS employees was completely arbitrary and had no business rationale. Further, its economic effect was nullified by the hedging arrangements, except to an insignificant and pre-determined extent. As a result, the shares were not restricted securities within s 423. The condition in the DB case operated for a short period, during which the possibility that it might be triggered lay largely within the control of the employee who would be adversely affected. It had no business purpose, and also fell outside s 423.

On the basis that the exemption did not apply, Lord Reed held that the bonuses should be taxed as shares rather than cash. The value of the shares had to be assessed as at the date of their acquisition. However, he disagreed with HMRC that the conditions attached to the shares should be disregarded, saying they had the effect of reducing their value to a small extent and should be taken into account.

HMRC's appeals were allowed.

Comments - Andrew Watters, director and tax expert at Thomas Eggar (recently merged with Irwin Mitchell LLP), said: 'Apart from the significant tax consequences for UBS , DB, and other users of similar schemes, this judgment has wider consequences. It provides authority for courts to interpret legislation by taking into account non-statutory considerations, for example whether there is a real world consequence other than tax avoidance.

'Since HMRC's view is that schemes by their very nature have an element of artifice, one can foresee some interesting litigation ahead. In the future, in deciding on the risk of whether a particular tax arrangement "works" from a legislative perspective, the prudent taxpayer may wish to consider the commercial versus tax avoidance driver. Such considerations may cover reputational as well as tax consequences.'

The financial secretary to the Treasury, David Gauke, described the decision as 'an important victory and confirmation from the UK's highest court that tax avoidance is simply unacceptable'.

UBS AG v CRC; DB Group Services (UK) Ltd v CRC, Supreme Court

Other benefit in kind changes (Lecture P949 – 12.06 minutes)

VW, eat your heart out!

In connection with the calculation of benefits in kind for company cars, clause 7 of the draft Finance Bill has the effect of retaining the 3% diesel supplement which was due to be abolished on 6 April 2016. As a result, S141 ITEPA 2003 will continue to apply for 2016/17 and subsequent tax years.

In his Autumn Statement on 25 November 2015, the Chancellor announced that the legislation dealing with this additional 3% would remain in place until the point at which new EU-wide testing procedures finally come into operation. These procedures aim to ensure that all diesel cars meet NO2 and other key air quality standards under strict real-life driving conditions.

It is anticipated that the 3% diesel supplement will not now be removed until 6 April 2021.

How trivial is your benefit?

As mentioned in the previous chapter, the OTS conducted in 2014 a detailed review of the administrative aspects of employee benefits and expenses. One of their recommendations was that there should be a statutory exemption for 'trivial' benefits in kind provided for members of staff. This, it was suggested, should replace what has hitherto been a concessionary practice, under which an employer has had to agree with HMRC that a benefit can be regarded as 'trivial' (and therefore liable to neither income tax nor NICs). Indeed, such benefits do not even have to be reported.

Clause 8 of the draft Finance Bill introduces a new S323A ITEPA 2003 with effect from 6 April 2016. This states that any benefit provided by, or on behalf of, an employer to an employee (or to a member of his family or household) will not be chargeable to income tax where four conditions are satisfied. There will also be a corresponding NIC exemption.

The four specified conditions are:

1. The benefit must not be cash/ cash voucher as defined in S75 ITEPA 2003 (S323A(3) ITEPA 2003).
2. The cost of providing the benefit must not exceed £50 per person (S323A(4) ITEPA 2003). If the benefit is provided to a number of persons such that it would be impracticable to calculate the cost of providing it to each one individually, a simple average cost mechanism can be used (S323A(5) and (6) ITEPA 2003).
3. The exemption will only be in point where the benefit is not provided as part of a salary sacrifice arrangement or any other contractual obligation (S323A(7) and (8) ITEPA 2003).
4. The benefit must not be provided in recognition of services performed by the employee in the course of his employment or in anticipation of such services (S323A(9) ITEPA 2003). In other words, the exemption only applies if the benefit is given for a non-work reason, for example, the birth of a child – it cannot be provided in recognition of a job well done or for anything else which is work-related.

There is no limit to the number of 'trivial' benefits which employees can receive in any one tax year.

However, if the employer is a close company and if the recipient is a director or office-holder of the company (or is a member of that person's family or household), there is an additional condition which has to be met. The cost of providing such benefits must not exceed an annual cap of £300 (S323A(10) ITEPA 2003). This figure is known as the 'available exempt amount' and further relevant details can be found in S323B ITEPA 2003.

HM Treasury have the power to amend Ss323A and 323B ITEPA 2003 by statutory instrument, should they so decide (S323C ITEPA 2003).

Contributed by Robert Jamieson

Capital Taxes

Trust dividend income after 5 April 2016 (Lecture P948 – 12.29 minutes)

Life interest trusts

The essential principle is that trustees pay basic rate income tax on trust income which is credited to the life tenant. In these circumstances, beneficiaries may:

(i) obtain a refund;

(ii) suffer no further tax; or

(iii) be liable at higher and additional rates

on their trust income. In the case of dividend income received by such trusts, the position to date has been that the tax credit covers the trustees' basic rate income tax liability.

With effect from 6 April 2016, life interest trustees will have to pay the dividend ordinary rate (7.5%) on all their dividend income. They are not entitled to the £5,000 dividend allowance – that benefit is only available to individuals (see new S13A ITA 2007).

However, because life interest trusts are transparent for income tax purposes, this means that the 7.5% dividend tax charge will be credited to the life tenant (who may therefore be entitled to a refund if the income falls within his £5,000 dividend nil rate band).

In order to avoid the problem of trustees having to pay income tax on their trust income which is then refunded to the beneficiary, it is of course possible for them to mandate dividends and other income directly to a life tenant, in which case the trustees will not need to submit a trust tax return following their agreement to this effect with HMRC (see Para TSEM3040 of the Trusts, Settlements and Estates Manual).

Discretionary and accumulation trusts

Discretionary and accumulation trusts are also unable to utilise the £5,000 dividend allowance and so these trusts will suffer tax at 38.1% on all their dividend income from 6 April 2016 onwards. This will be credited to the trust's tax pool and will be available to 'frank' any income distributions. These types of trust are *not* transparent and the trust distribution counts as an annual payment in the hands of a beneficiary.

Note, therefore, that the current disadvantages of channelling dividends through, say, a discretionary trust will remain:

(i) a beneficiary cannot take advantage of the £5,000 dividend allowance; and

(ii) in making the payment to the beneficiary, the trustees will have to deduct tax at the trust rate (45%) and so they are likely to end up having to pay HMRC an additional 6.9%.

The conclusion is that it will often be attractive to appoint an interest in possession to a beneficiary so that he will be able to benefit from the £5,000 dividend nil rate band. This arrangement should not trigger a CGT or an IHT charge.

Contributed by Robert Jamieson

Genuine mistake - Discovery assessment on executors

Summary - the FTT reduced a penalty to nil for failure to report taxable income.

The executors of the deceased taxpayer, who died on 15 October 2012, appealed against a penalty of £5,060.18 issued for failure to disclose income. This gave rise to an assessment to income tax due from the taxpayer issued on 15 April 2015 for £14,457.67.

The taxpayer's estate was worth about £1.5m at the time of his death. An inheritance tax return was filed in January 2013 and probate applied for in February 2013. The executors filed the taxpayer's self-assessment tax return for 2012/13 on 10 August 2013. The self-assessment return covered the period from 6 April 2012 to the date of death, but under-declared the income for that period.

On 26 September 2013, an executor wrote to HMRC sending a cheque for £15,332.92, which was then the outstanding tax due, and saying that they 'presumed this is in full and final settlement' because the executors were proceeding to finalise and distribute the estate. However, they failed to publish a notice in the *London Gazette* of their intention and give a deadline for any further claims. Exactly one year later HMRC raised a query on whether mistakes had been made in the 2012/13 return, issuing a discovery assessment under s29 TMA 1970.

HMRC issued a penalty under Sch 24 FA 2007 on the basis that the error was 'deliberate but not concealed', although the executors accepted that their conduct had been careless since the figures in the self-assessment tax return did not match those in the inheritance tax return filed earlier that year.

Decision:
As laymen, Cornwell-Kelly J said, 'the executors did not know, and could not be expected to have known, that an advertisement in the *London Gazette* of their intention to distribute the estate would have safeguarded their position'.

The executors agreed that the error had been 'careless' but it was not reckless or with intent to cause loss to HMRC. They accepted that the tax was lawfully due and that interest on it was no more than a commercial restitution to the Exchequer; however, they were concerned about the penalty, feeling that, the mistake had been genuine and unintentional, so the penalty should not have been levied.

Cornwall-Kelly J agreed, saying that, under Sch 24 Para 11 FA 2007, HMRC could have reduced the penalty 'because of special circumstances'. The executors' choice to risk the consequences of whatever shortcomings in their legal or accountancy knowledge, alongside HMRC's own admitted delays in dealing with the case (including poor customer service), warranted 'some consideration of special circumstances'. The judge added that had HMRC's delays not occurred, it 'might well have spared [the executors] the difficulty they are in now'. The taxpayers' appeal was allowed.

Comments - The FTT had pointed out that it had no jurisdiction to deal with matters of maladministration but it found that HMRC's delay was partly the reason for the appellants' difficulties and consequently reduced the penalty to nil.

Usher & Perkins, Executors of Terence J Guy (deceased) v HMRC TC4849

Purchase Of Own Shares and Entrepreneurs' Relief (Lecture B949 – 11.22 minutes)

Entrepreneurs' relief (ER) offers a capital gains tax (CGT) rate of 10% on aggregate net chargeable gains of up to £10 million. A claim for ER is available on a material disposal of business assets. This includes (for example) the disposal by an individual of shares or securities of a company (or an interest in them).

A disposal of shares will typically involve a sale (or possibly a gift) of the shares. However, the ER legislation (at TCGA 1992, s 169S(2)) provides that, for ER purposes, the disposal of an interest in shares also includes a disposal treated as made under TCGA 1992, s 122. This potentially brings (for example) capital payments on a company purchase of own shares (within CTA 2010, ss 1033-1043) within the scope of ER, if the relevant conditions are satisfied.

Company purchase of own shares

Tax law

When a company buys back its own shares from a shareholder, any payment in excess of the capital originally subscribed for the shares generally constitutes a distribution. Accordingly, for tax purposes the transaction would ordinarily fall to be treated as an income distribution (CTA 2010, s 1000(1)).

However, there is an exception from income treatment in the case of unquoted trading companies (s 1033). If certain conditions are satisfied (see ss 1034-1043), the transaction automatically falls outside income distribution treatment. The effect is that the vendor is treated as receiving a capital payment instead (unless the vendor is a share dealer, in which case the receipt is treated as trading income).

Company law

It is important to note (although unfortunately it is sometimes overlooked) that a purchase of own shares must comply with company law requirements (in *Companies Act 2006*) to be valid.

For example, in the case of an unquoted (or 'off market') company purchase of own shares, a contract is generally required to be approved in advance (*CA 2006, s 693*). However, a company may enter into a contract to purchase its own shares, on condition that the shareholders approve the contract terms by an ordinary resolution (*CA 2006, s 694(2)*) (Note: separate authority provisions apply (in *s 693A*) for an off-market purchase in relation to an employees' share scheme).

If the contract (or its terms) is not approved, the company may not purchase the relevant shares and the contract lapses. In other words, the company purchase of own shares is not completed until the above requirement is met.

Entrepreneurs' relief

A capital payment to an individual on a company purchase of own shares may be the subject of an ER claim where, throughout the period of one year ending with the date of disposal, the following requirements are satisfied (TCGA 1992, s 169I(6)):

> "(a) The company is the individual's personal company and is either a trading company or the holding company of a trading group; and
>
> (b) The individual is an officer or employee of the company or (if the company is a member of a trading group) of one or more companies which are members of the trading group."

The date of disposal for CGT purposes is when an unconditional contract for the purchase of own shares is made. If the contract is conditional, the time of disposal is when the condition is satisfied (TCGA 1992, s 28).

Interaction of tax and company law

If a shareholder intends claiming ER on a purchase of own shares that satisfies the conditions for capital gains treatment, it is important to ensure that the ER conditions are satisfied upon disposal, including in relation to the 'officer or employee' requirement.

In *Moore v Revenue & Customs* [2016] UKFTT 115 (TC), the taxpayer was a director who owned 3,000 out of 10,000 shares in a trading company, and was employed under a contract of employment. Following a dispute with the other director shareholders, it was agreed that the taxpayer would leave the business. At a general meeting of the company on 29 May 2009, it was resolved that the company would purchase 2,700 shares from the taxpayer. On the same day, the taxpayer signed a compromise agreement for the termination of his employment, and the company purchase of shares agreement. All Companies House papers concerning the taxpayer's resignation as a director were also signed on that day. However, those documents stated that the effective date of his resignation as a director was 28 February 2009.

The taxpayer declared the share disposal on his tax return and claimed ER. However, HMRC concluded that the taxpayer was not entitled to ER because he was not an officer or employee of the company throughout the period of one year ending with the disposal of his shares.

The taxpayer appealed. He accepted that he had ceased employment with the company and was no longer an office holder from 28 February 2009, but contended that the completion of the negotiations resulted in a binding contract for sale in February 2009, which was therefore the date of disposal for capital gains tax purposes.

Unfortunately for the taxpayer, the First-tier Tribunal noted that company law (in CA 2006, ss 693, 694) required a contract for a company own purchase of shares to be approved in advance by a special resolution. That resolution was not passed until 29 May 2009. Accordingly, the company was incapable of entering into a valid contract to purchase the shares until the resolution had been passed. Even if there had been a contract, it had to be conditional on approval by special resolution. The date of disposal under a conditional contract would (by virtue of TCGA 1992, s 28(2)) be the date on which the condition was satisfied, i.e. 29 May 2009. The taxpayer's appeal was dismissed.

Officer or employee

It should be noted that the 'officer or employee' requirement (in TCGA 1992, s 169I(6)) applies not only in the context of a company purchase of own shares, but in other circumstances as well, including on a sale of the company.

If the company has ceased trading (e.g. if it is being wound up), the conditions in s 169I(6) must be met throughout the period of one year ending with the date on which the company either ceased to be a trading company (without continuing to be becoming a member of the trading group) or ceased to be a member of a trading group (without continuing to be or becoming a trading company), and that date must be within three years of the date of disposal (s 169I(7)).

Contributed by Mark McLaughlin

Are deferred shares ordinary shares?

Summary - The First-tier Tribunal found that a holding of ordinary shares, that could only meet the 5% ownership test necessary to satisfy the 'personal company' condition in s169I(6) TCGA 1992 by ignoring the existence of deferred ordinary shares, did not qualify for entrepreneurs' relief.

Mr Castledine claimed entrepreneurs' relief on the disposal of ordinary shares. The issued share capital of the company included deferred shares. If those deferred shares were 'counted' as ordinary shares, Mr Castledine's holding represented 4.99% of the ordinary share capital, so that he did not qualify for entrepreneurs' relief (s169S TCGA 1992 and s989 ITA 2007).

Decision:

The FTT observed that the intention that the term 'ordinary shares' should be given a wide interpretation, as emphasised in s 989 by the words in parenthesis: '(however described)'. The tribunal added that the creation of the class of deferred shares had been commercial. They were a carefully devised means of protecting the company, in the case of share-incentivised employees leaving it and/or becoming its rivals. There was no reason why such a measure should be found to be at odds with the presumed intention of Parliament.

The FTT also rejected the arguments as to the 'absurdity' of such shares, with no rights to participate in the profits of the company and no voting rights. It noted that the ordinary shares were not any more likely than the deferred shares to receive a return, as they were swamped by the preference shares. Furthermore, as mentioned above, the deferred shares had been issued for commercial reasons and not as part of a tax avoidance scheme, so that this case should be distinguished from *Arrowtown* [2003] HKCFA 46. Finally, Parliament's definition of a person entitled to entrepreneurs' relief seemed to envisage someone who had 'a full bodied risk stake in the company' in the form of ordinary shares as opposed to preference shares.

Comments - As the deferred shares had been created for purely commercial reasons and with the intention of stripping them of economic value (whilst avoiding pitfalls associated with other mechanisms for achieving this when a member of the management team ceased to be an employee), it seems strange and ironic that they should still form part of the ordinary share capital for entrepreneurs' relief purposes.

A Castledine v HMRC TC4930

Capital gains tax due on conversion of QCBs and NQCBs

Summary – The Upper Tribunal found that the redemption of loan notes had triggered a charge to CGT.

The taxpayers were a married couple who held all the share capital in a limited company, BL. In August 2000, they sold BL to LH and received loan notes as consideration. The notes were repayable on 24 August 2004 or earlier and could be redeemed in US dollars, with the exchange rate to be the spot rate 20 days before repayment. It was agreed that these provisions prevented the notes being qualifying corporate bonds (QCBs) for the purposes of s117 TCGA 1992.

The couple received additional loan notes in 2001. A deed of variation removed the right to redemption in US dollars from the 2001 notes, as a result of which they became QCBs.

On 7 May 2003, the couple exchanged both sets of loan notes for two secured discounted loan notes which were QCBs. HMRC said the gains arising on the exchange were subject to capital gains tax. The taxpayers appealed to the First-tier Tribunal. It agreed with the couple that the disposals of the qualifying and non-qualifying corporate bonds should be treated as a single one and was not liable to capital gains tax. The Revenue appealed.

Decision:
The Upper Tribunal said that according to s 132 and s 116, each original single asset or single security should be treated as the subject of a conversion whenever that was provided for by s 132. The provisions could operate sensibly only if there was 'separate treatment of each asset that might otherwise have been the subject of a disposal or part disposal... on any form of reorganisation, conversion etc, the new holding might well be composed of two or more shares or securities'.

Disagreeing with the First-tier Tribunal, the Upper Tribunal judge said the conversion of the first set of loan notes into secured discounted loan notes was a conversion to which s 116(1) applied so that, on the redemption of the successor notes, the frozen gain was realised under s 116(10).

The redemption of the successor notes after the second set was converted into secured discounted loan notes triggered the gain at the point of the removal of the dollar redemption provision.

HMRC's appeal was allowed.

Comments - The Upper Tribunal found that the transaction to which s116 TCGA 1992 refers is the single conversion of securities referred to in s132 and cannot include more than one such conversion. It was not therefore possible to regard the original shares as comprising a mixture of QCBs and non-QCBS with the result that s116(1)(b) did not apply. If the FTT's approach in regarding the transaction to whichs116 applies as potentially comprising more than one conversion had been accepted then, as pointed out by the Upper Tribunal, the anomalous approach that allowed a 'frozen' gain to escape taxation would not only arise on a relatively unusual set of facts but could occur on any occasion when a taxpayer holding securities with a large latent gain converted a small amount to QCBs and then converted the mixed holding into other QCBs before redemption.

Hancock and Hancock v CRC, Upper Tribunal

CGT avoidance on the redemption of loan notes

Summary - The First-tier Tribunal found that the Ramsay principle prevented the artificial manipulation of the value of loan notes from reducing their market value and accordingly the marketed avoidance scheme used by the taxpayer failed. HMRC were entitled to make a discovery assessment because the disclosure in the tax return was insufficient.

The appeal concerned a 2004 tax avoidance scheme to reduce the CGT liability on the redemption of loan notes by using a deed of variation to convert them from non-qualifying corporate bonds (NQCBs) into qualifying corporate bonds (QCBs), and to artificially depress their value at the time of the conversion. The conversion had been effected by removing the ability to redeem the loan notes in US dollars; and their value had been depleted by introducing a three month long period during which the loan notes could be redeemed at a fraction of their value. The main substantive issue was whether the deed of variation had converted the loan notes from NQCBs to QCBs.

Decision:
Following the decision in *Blumenthal [2012] TC2174*, the FTT decided that the effect of the deed of variation and resolution signed by each loan note holder had been to 'delete' the foreign currency option (on the occurrence of a contingency), with the result that the loan notes no longer contained such a provision. They had therefore been converted into QCBs.

In terms of valuation, the FTT rejected HMRC's argument that, if viewed realistically, the conversion of the loan notes had been brought about solely by the deed of variation when it had become certain that the conversion would happen. Such an interpretation would create practical difficulties, for instance, where a deed of variation provided for a conversion 12 months later. The loan notes should therefore be valued at the date that the contingency had realised. However, as the market value of the loan notes had been artificially reduced, applying the *Ramsay* principle, the deed of variation had not reduced the value of the loan notes. This meant that a taxable capital gain had arisen on their redemption, which HMRC had been right to assess by way of discovery.

Finally, HMRC should not have been expected to be aware of the insufficiency of tax on the basis of the information included in the taxpayer's return. The disclosure was identical to the one made in *Blumenthal.* Agreeing with the decision, the FTT found that the information had been sufficient to alert an officer to the need to make enquiries but not to an actual insufficiency of tax.

Comments – The marketed tax avoidance scheme in which the taxpayer had participated had also previously been considered (and deemed ineffective) by the First-tier Tribunal in *Blumenthal* [2012] TC 2174. Note also that it is now likely that advance disclosure of such a scheme would be required under the Disclosure of Tax avoidance schemes (DOTAS) rules introduced in *Finance Act* 2004.

Executors of W Connell v HMRC TC4940

No PPRR

Summary - The First-tier Tribunal dismissed Mr Kothari's appeal against HMRC's refusal of his claim for private residence relief as occupation of a two bedroom flat in Mayfair lacked the necessary degree of permanence or continuity.

Mitesh Kothari had claimed private residence relief and lettings relief under ss222 and 223 TCGA 1992 in respect of a gain of circa. £1.384m arising on the disposal of a two bedroom flat in Mayfair. HMRC refused the claim on the basis that although the appellant had occupied the property for just over six months his occupation did not have the necessary degree of permanence for the property to be his principal private residence. Mr Kothari had bought the property in 2005 with a residential mortgage but had initially let the property and switched to a buy to let mortgage at a later date. Mr Kothari moved into the property on 19 January 2009 submitting that he did so with the intention of making the property a permanent home for himself and his family. An election that the property should be treated as his principal private residence was submitted to HMRC. Some time in February 2009, however, estate agents were engaged and the property was placed on the market for sale. An offer was received on 5 March 2009 and the property was sold in July 2009.

HMRC stated that they did not believe that the Mr Kothari's occupation of the property had the necessary degree of permanence to be his principal private residence and pointed to a number of factors which supported this contention.

Mr Kothari had occupied the flat for a very short period of time before placing it on the market;

- it was a two bedroom flat and he was moving to it from a four bedroom house despite having a wife and three young children;
- in a telephone call with HMRC in 2013, he had indicated that he had retained his former home temporarily whilst waiting to see if his family enjoyed living at the flat which indicated that no final decision to live there had been made at the time;
- he had not moved his furniture from his former home but instead had bought the previous tenant's furniture;
- no change had been made to his eldest child's schooling (although it was accepted the move had taken place part way through the school year); and
- neither his bank nor the DVLA were informed of the move.

Decision:

The FTT confirmed that, firstly, following the well known cases of Goodwin v Curtis (HMIT) and Levene v IR Commrs (1928), the appellant was required to demonstrate that his occupation of the property showed some degree of permanence or continuity, or some expectation of continuity.

The second question was, therefore, whether or not the evidence which had been presented was sufficient to demonstrate that the appellant's occupation did indeed possess the necessary qualities of permanence or continuity, or expectation of continuity. The FTT found that considering the submissions by both parties, it did not.

The appeal was dismissed.

Comments - Mr Kothari moved into a two bedroom flat in Mayfair from a four bedroom house, purportedly, with the intention of making it a permanent home for himself, his wife and three young children and electing that it should be treated as his principal residence. However, a month later the property was placed on the market for sale and the flat was sold within five months. With such a large gain at stake the taxpayer should have ensured beyond doubt that the facts. could support his claim

Kothari v HMRC TC4915

ATED relief declaration turns by 30 April 2016 (Lecture B950 – 17.23 minutes)

Introduction

The enveloped dwelling legislation was introduced from 1 April 2013 and is aimed at high value residential property being held by non-natural persons e.g. companies and mixed partnerships.

The following tax charges apply, all with the aim of stopping high-value UK residential property being held in corporates or mixed partnerships without good reason:

- **15% rate of SDLT on acquisition** costing at least £2m by non-natural persons whether UK resident or not. From 19 March 2014 this limit was reduced to £500,000.

  The additional 3% from April 2016 will not apply to the 15% ATED rate.
- **An annual charge** from 1 April 2013 on high value residential property (ATED)
- **The application of CGT** to gains from 6 April 2013 on such property by non-natural persons (whether non-resident or resident). For UK resident companies any gains relating to earlier periods are subject corporation tax and should be submitted as part of the CT 600.

High value but falling!

The value of a property is measured as at 1 April 2012 or acquisition if later. To fall within the regime:

- Initially the property had to be worth at least £2m at 1 April 2012 (or acquisition if later);
- From 1 April 2015 ATED applies for properties worth £1m at 1 April 2012 or later acquisition;
- From 1 April 2016 ATED applies for properties worth £500k at 1 April 2012 or later acquisition.

On 1 April 2017 the property valuations are going to be reset and where individual property prices are above £500k, they will be within the ATED regime.

Annual Tax on Enveloped Dwellings (ATED)

The amount of tax raised in 2013/14 was five times more than the government was expecting so they have raised the charges by over 50% for the year to 31 March 2016!

The charges for the year to 31 March 2016 are as follows:

	£
More than £2,000,000 but not more than £5,000,000	23,350
More than £5,000,000 but not more than £10,000,000	54,450
More than £10,000,000 but not more than £20,000,000	109,050
More than £20,000,000	218,200

For properties in the £1,000,000 to £2,000,000 band which came in from 1 April 2015, the annual charge is £7,000; the £500,000 band brought into charge from 1 April 2016 will be charged at £3,500.

The ATED chargeable period is linked to financial years, i.e. it runs from 1 April in one year to 31 March in the next.

Returns and payment are due within:

- 30 days of the start of the year; or
- 30 days of acquisition if later; or
- 90 days of build or conversion

The amounts due are pro rata depending on when properties are acquired or sold within the financial year.

Exemptions

There are a number of exemptions from ATED:

- charitable companies using the dwelling for charitable purposes
- public bodies
- bodies established for national purposes

HMRC ATED technical guidance provides the detail on exemptions.

If you meet the conditions for an exemption, you do not need to file a return.

ATED reliefs

There are numerous reliefs from ATED that must be claimed.

The most important reliefs relate to:

- property rental businesses
- property development businesses
- property traders
- farmhouses

Penalties arise for late submission of ATED returns – even if there is no ATED due. If you send in the ATED return late and claim a relief then there are still penalties for filing late returns.

On top of the late filing penalty there are penalties for late payment together with interest on the late payment of the ATED.

Property rentals relief

In order to claim the relief the claimant must be carrying on a qualifying property rental business which means meeting two conditions:

1. It must be a property rental business per PIM 1020; and
2. It must be carried on, on a commercial basis, with a view to a profit

Where a dwelling is not generating rents, the taxpayer may still be able to claim relief provided that they are realistically taking steps to rent out the property:

- Appointing a letting agent
- Redecoration
- Making substantial alterations
- Purchasing furniture

The steps being taken must ensure that the dwelling will generate rents without undue delay taking into account unavoidable events.

Where reasonable steps are not being taken then the property falls under the ATED regime and the ATED charge will be payable.

Permanently ceases to be let

Where a property permanently ceases to be let, ATED relief is still available where, without undue delay:

- The single-dwelling interest is to be sold
- The dwelling is to be demolished or converted

However non- qualifying individuals (s1122 CTA 2010 - connected person of a controlling shareholder) must not be permitted to occupy the dwelling in this vacant period.

Property developers

Property developers are relieved from ATED where they carry on a property development trade: buying, developing of redeveloping for resale, land and property.

This includes refurbishment of substantially the whole of a property prior to resale, extensive works on the property including extensions or demolition and rebuild.

Property traders

Property traders are relieved from ATED where the interest is held as the stock of the business and for the sole purpose of resale in the course of that property trading business. This includes the buying and selling of dwellings.

For the business to amount to a trade it must be carried on, on a commercial basis, with a view to a profit.

If a company buys a property in the expectation that in a few years time it will be able to sell that property for a higher price that may not be sufficient to make the activity amount to a trade.

This may be considered to be an investment activity for which relief is not provided.

Farmhouses

Farmhouses will qualify for relief if the farming trade is carried on on a commercial basis and with a view to a profit and the farmhouse:

- forms part of the farmed land; and
- is owned by the person carrying on the farming trade or be owned by a person who is connected to the person carrying on the farming trade
- is occupied by a farm worker for the purposes of the farming trade or by a former long-serving far worker or the surviving spouse/ civil partner of a former farm worker

The stabling of horses and care of those horses will not amount to farming.

The farmworker must have a substantial involvement in the day-to-day running of the trade or in the direction and control of the conduct of that trade.

This means working for an average of 20 hours per week doing tasks that are necessary for the operation of the trade such as ploughing, spraying, harvesting, milking, birthing etc.

Alternatively where the individual is responsible for the running of the farming trade they must spend a minimum of 20 hours a week making decisions to buy equipment or additional land, contract for services to be provided and also making decisions on when, where and how to sell, produce and stock.

The 20-hour test can be met by combining time spent working and managing.

To qualify as a 'former long-serving farm worker' if the individual would have qualified as a farm worker for a qualifying period of three or more years or for periods that together total three or more years within a five year period.

Relief Declaration Return

Prior to 2015/16, taxpayers were required to submit one return for each of the properties within the ATED system – even where relief was being claimed. Finance Act 2015 introduces a new type of ATED return called a relief declaration return (s 73, inserting new s 159A into FA 2013). For each type of relief being claimed, a separate relief declaration return must be filed in respect of one or more properties held for the chargeable period. A return will also needed in respect of any property that ceases to qualify for a relief and ATED becomes due.

As a reminder, the legislation lists the types of relief that may be claimed together.

Provision	**FA 2013**	**Type of relief**
Property rental business	Ss 133 or 134	1
Dwelling open to the public	S 137	2
Property developers	Ss 138 or 139	3
Property traders	S 141	4
Financial institutions	S 143	5
Dwelling occupied by employees of a trade	S 145	6
Farmhouses	S 148	7
Providers of social housing	S150	8

Having made the return, the declaration will also cover any further properties acquired in the year which are subject to the same relief, as the properties will not be specified in the relief declaration. This represents a considerable administrative saving for affected companies.

Where a return is late, any penalty chargeable is calculated by reference to a single relief declaration if this applies, rather than individual returns for each property.

The relief declaration return for the year to 31 March 2017 should be submitted by 30 April 2016.

Administration

Penalties for late filed employer's annual return – No reasonable excuse

Summary – The Tribunal dismissed the taxpayer's appeal holding there was no reasonable excuse

The taxpayer appealed against penalties totalling £1,200 imposed under s98A(2) & (3) TMA 1970 for the late filing of the employer's annual return for 2010/11. He had been trading as two separate businesses: one in partnership as the Malt Shovel Hotel, but also as a sole trader under a different PAYE reference.

He wrote to HMRC about the penalty appeal on 5 May 2015 stating that he had closed his businesses in May 2011, and that the address had changed for both. However, when the penalty notification was originally sent on 16 February 2012 the taxpayer wrote to HMRC on 19 March 2012 enclosing copies of letters, one for each business and both dated 16 June 2010, stating that they had ceased on 31 May 2010. In each case he confirmed that he would be making the final payments for the periods April to May 2010.

Decision:

The First-tier Tribunal found that, on the balance of probabilities, the businesses must have closed on 31 May 2010.

HMRC admitted it had received the letters dated 16 June 2010, but the taxpayer argued that, although he had received HMRC correspondence for his recently closed sole trader business at the new address, nothing was sent to him at that address for the Malt Shovel Hotel. Since HMRC records for the hotel showed it had had nine employees, a return was required. HMRC said a reminder was sent electronically on 6 August 2010 and the late filing penalty notices for £800 and £400 respectively were issued on 16 February 2012 and 28 May 2012.

The taxpayer said it was only when a debt collection agency pursued him in 2015 (by which time he had moved address again) that he became aware of a problem and he acted immediately.

The tribunal decided the taxpayer did not have a reasonable excuse for failing to file an employers' annual return for the Malt Shovel Hotel because, in the letter of 16 June 2010, he confirmed he had 'recently submitted the year end … to complete 2009/10'. This showed he was aware of the need to file the return, but none for the April to May 2010 period had been filed.

The appeal was dismissed and the penalty confirmed.

Comments – This demonstrated that the taxpayer knew of the need to file the returns but confusion over dates did not help the taxpayer's case. Consequently the appeal was dismissed and the penalty was confirmed.

John Wain for D Franklin and John Wain trading as The Malt Shovel Hotel v HMRC TC4856

Unsolicited returns

Summary - The FTT found that an enquiry into an unsolicited return was not valid.

Mr Revell was a professional footballer and his tax was accounted for through PAYE. In March 2011 HMRC identified an underpayment on Mr Revell's PAYE record for 2008–09. Although HMRC were aware of Mr Revell's address at the time in Brentwood (from a P45 issued in July 2010) they sent the underpayment calculation to an old address. Consequently Mr Revell never received it. In September 2012 HMRC issued a self-assessment return for 2008–09, but again they sent it to the Brentwood address. With no completed return, in February 2014 HMRC issued a determination under s28C TMA 1970') in relation to the underpayment of tax it argued was due for 2008–09. As the only way to supersede a determination was to submit a return, Mr Revell submitted a 2008–09 tax return in March 2011 which included a 'notional credit' resulting in the return showing that no tax was due for the year. HMRC purported to open an enquiry into the return under s9A TMA 1970 and following completion of that enquiry, issued a closure notice removing the notional credit thus increasing the tax due for the year to £16,519

Decision:

The FTT found that the request to deliver a return had not been served as it had been sent to the wrong address, HMRC having received a more up-to-date address in form P60.

HMRC observed that it received approximately 350,000 unsolicited returns a year and that its practice was to treat such returns as if they had been made in response to a notice to make a return. The FTT found, however, that there was no basis for the submission that by making an unsolicited return, the taxpayer has waived the requirement for a notice under s 8. The FTT added that the return filed by Mr Revell should be characterised as a notice of liability to income tax under s7 TMA 1970 rather than as a self-assessment return. This, in turn meant that the deadline to request a return had passed (s34 TMA 1970) and the only option for HMRC was to issue a discovery assessment, provided the conditions of s29 TMA 1970 were satisfied.

Comments - HMRC appear to have failed both the taxpayer and the wider UK population. In respect of the taxpayer the FTT noted that the taxpayer had well justified complaints about the manner in which his affairs had been handled. In respect of the UK population as a whole, because HMRC did not use the taxpayer's correct address and demonstrated a clear lack of rigour in getting to the bottom of what happened when they did not receive a completed tax return it appears that £16,519 of tax that should have been collected has not been collected. The FTT noted that there was no express right of appeal against a determination notice because it was assumed that the taxpayer's remedy is to displace the notice by filing a self-assessment return, which is what the taxpayer did in this case. But if the taxpayer chose not to take that course, but resisted enforcement of the determination notice, it appeared to the FTT that it would not have jurisdiction in respect of those enforcement proceedings. The FTT regarded that as being not particularly satisfactory. The FTT effectively found that HMRC's practice of treating unsolicited returns as if they had been filed under a notice was in breach of the legislation. This may mean that other taxpayers that have filed unsolicited returns should now challenge the validity of enquiries into those returns

A Revell v HMRC TC 4887

Judicial review claim stayed

Summary - The High Court stayed a claim for judicial review pending the appeal of British American *Tobacco (BAT) in the FTT.*

The claimants sought judicial review of the restitution interest tax provisions which are contained in Part 8C CTA 2010, as amended by F(No.2)A 2015. The issue was the appropriate forum.

Decision:

The High Court found that the FTT was the appropriate forum for the following reasons:

- The issue was already before the FTT in the British American Tobacco appeal.
- The grounds of appeal were identical to those in the *BAT* appeal
- The FTT allowing the appeal would have the same effect as the declaratory relief the claimants sought to obtain in the High Court.
- It would be more effective to test arguments against actual rather than hypothetical facts and the FTT was a specialist tax tribunal with the relevant background knowledge.
- The FTT would consider issues of legality, alongside any technical arguments.

Comments - The conclusion reached by the High Court was consistent with the decision in the High Court in the *Six Continents* case, in which the court had refused the claimants' application to amend pleadings to include a challenge to the lawfulness of the restitution interest tax provisions.

R (on the application of (1) Imperial Chemical Industries and (2) FCE Bank) v HM Treasury and HMRC [2016] EWHC 279

Deadline Dates

1 April 2016

- Due date for the payment of corporation tax liabilities for accounting periods ended 30 June 2015 for small and medium-sized companies not liable to pay by instalments.
- Change to emissions thresholds for business cars (zero rate ends).
- Application to defer Class 2 or 4 National Insurance for 2015/16 or claim exception for 2016/17 must be made by this date.
- Multiple contractors need to advise HMRC that they wish to be treated as a single contractor for 2016/17 by this date.

5 April 2016

- 2015/16 tax year ends.
- Ensure personal allowances, exemptions and tax bands are efficiently used by this date.
- Deadline to pay previously unpaid Class 3 NICs for 2009/10.

6 April 2016

- As it is the start of 2016/17 tax year, ensure that payroll and other systems are updated.
- Personal allowances increased to £11,000 for 2016/17
- CGT AEA increased to £11,100 for 2016/17.

7 April 2016

- Due date for VAT returns and payment for 28 February 2016 quarter (electronic payment).

14 April 2016

- Due date for the quarterly corporation tax instalment for large companies depending on accounting year end.
- Forms CT61 must be submitted and tax paid for the quarter ended 31 March 2016 by this date.

19 April 2016

- Due date of payment of PAYE, NIC, construction scheme industry and student loan liabilities for month ended 5 April 2016 if not paying electronically.
- File monthly construction industry scheme return by this date.
- Due date of payment of PAYE liability for quarter ended 5 April 2016 if average monthly liability is less than £1,500.

21 April 2016

- File online monthly EC sales list by this date.
- Submit supplementary Intrastat declarations for March 2016 by this date.

22 April 2016

- PAYE, NIC and student loan liabilities should have cleared HMRC's bank account by this date.

30 April 2016

- By this date Companies House should have received accounts of private companies with 31 July 2015 year end and public limited companies with 31 October 2015 year end.
- By this date HMRC should have received corporation tax self-assessment returns for companies with accounting periods ended 30 April 2015.
- By this date the ATED returns should be filed and paid.

HMRC News

HMRC's response to recent media coverage on Gift Aid donations.

Recent reports in the national media have suggested that HM Revenue and Customs (HMRC) has sought to restrict Gift Aid on donations which are accompanied by a message of support from a donor's family. This is absolutely not the case.

HMRC's position has always been that Gift Aid can be claimed when an individual donor, who pays tax in the UK, makes a donation, even if additional names are added in a supporting message. HMRC's advice on this issue appears to have been misinterpreted so we are going to ensure our guidance is as clear as possible.

Where gifts are made by groups of people, such as work collections or large groups of friends, Gift Aid is not due and should not be claimed.

It is a government priority to maximise Gift Aid on eligible donations, and £1.2bn of tax repayments were made to charities in the tax year 2014 to 2015 through Gift Aid.

HMRC will continue working closely with charity collection agents to help them improve their processes so that Gift Aid is not removed from eligible donations.

Top ten things to know about the new Tax-Free Childcare scheme.

Tax-Free Childcare will be available to around 2 million households to help with the cost of childcare, enabling more parents to go out to work, if they want to, to provide greater security for their families. Here's the top ten things to know about the scheme…

1. You'll be able to open an online account

You'll be able to open an online account, which you can pay into to cover the cost of childcare with a registered provider. This will be done through the government website, GOV.UK.

Tax-Free Childcare will be launched from early 2017. The scheme will be rolled out gradually to families, with parents of the youngest children able to apply first.

You'll be able to apply for all your children at the same time, when your youngest child becomes eligible. All eligible parents will be able to join the scheme by the end of 2017.

2. For every 80p you or someone else pays in, the government will top up an extra 20p

This is equivalent of the tax most people pay - 20% - which gives the scheme its name, 'tax-free'. The government will top up the account with 20% of childcare costs up to a total of £10,000 - the equivalent of up to £2,000 support per child per year (or £4,000 for disabled children).

3. The scheme will be available for children up to the age of 12

It will also be available for children with disabilities up to the age of 17, as their childcare costs can stay high throughout their teenage years.

4. To qualify, parents will have to be in work, and each earning around £115 a week and not more than £100,000 each per year

The scheme is designed to be flexible for parents if, for example, they want to get back to work after the birth of a child or work part-time.

5. Any eligible working family can use the Tax-Free Childcare scheme - it doesn't rely on employers offering it

Tax-Free Childcare doesn't rely on employers offering the scheme, unlike the current scheme Employer-Supported Childcare. Any working family can use Tax-Free Childcare, provided they meet the eligibility requirements.

6. The scheme will also be available for parents who are self-employed

Self-employed parents will be able to get support with childcare costs in Tax-Free Childcare, unlike the current scheme (Employer-Supported Childcare) which is not available to self-employed parents. To support newly self-employed parents, the government is introducing a 'start-up' period. During this, self-employed parents won't have to earn the minimum income level.

The scheme will also be available to parents on paid sick leave and paid and unpaid statutory maternity, paternity and adoption leave.

7. If you currently receive Employer-Supported Childcare then you can continue to do so

You do not have to switch to Tax-Free Childcare if you do not wish to. Employer-Supported Childcare will continue to run. The current scheme will remain open to new entrants until April 2018, and parents already registered by this date will be able to continue using it for as long as their employer offers it.

However, Tax-Free Childcare will be open to more than twice as many parents as Employer-Supported Childcare.

Employers' workplace nurseries won't be affected by the introduction of Tax-Free Childcare.

8. Parents and others can pay money into their childcare account as and when they like

This gives you the flexibility to pay in more in some months, and less at other times. This means you can build up a balance in your account to use at times when you need more childcare than usual, for example, over the summer holidays.

It's also not just the parents who can pay into the account - if grandparents, other family members or employers want to pay in, then they can.

9. The process will be as simple as possible for parents

The process will be light-touch and as easy as possible for you. For example, you'll re-confirm your circumstances every three months via a simple online process; and there will be a simple log-in service where parents can view accounts for all of their children at once.

10. You'll be able to withdraw money from the account if you want to

If your circumstances change or you no longer want to pay into the account, then you'll be able to withdraw the money you have built up. If you do, the government will withdraw its corresponding contribution.

More information will become available ahead of the scheme being introduced so parents making childcare decisions are able to consider all their options.

Business Taxation

Can share dealing be a trade for loss purposes? (Lecture B947 – 16.56 minutes)

In Ali v HMRC (2016), the First-Tier Tribunal ruled that an individual, who was regularly buying and selling quoted shares, can be classed as trading for loss relief purposes, even though his principal source of income came from an entirely different unincorporated business.

The taxpayer (A) ran a successful pharmacy, but he had also been dealing in large volumes of shares in publicly listed companies since the 1990s (funded by his pharmacy profits).

Initially, A had submitted his tax returns showing the details of his share activities on the CGT pages. However, from 2006/07 onwards, he had treated these activities as a separate self-employed trade. He set up a special office on the first floor of his business premises from where he conducted his share dealing (virtually on a full-time basis) and, as a result, he had to employ a locum to manage the pharmacy that was based on the ground floor.

A engaged in numerous share transactions over the course of a tax year (ranging from a low of 775 to a high of 2,320 trades covering the period in question). He would often buy and sell the same shares within a few hours of each other. He very seldom held shares for any length of time and, in consequence, the dividend income derived from these activities was minimal. Unfortunately, more often than not, A was unsuccessful at his share dealing, generating losses that varied from £61,216 to £273,614 over the tax years 2009/10 to 2012/13 (inclusive). Given that his pharmacy produced substantial profits (considerably in excess of £200,000 for most years), A sought to claim sideways loss relief under S64 ITA 2007 for these losses against his other income.

HMRC refused to allow A to set off his losses from share dealing against his income from the pharmacy business and imposed heavy penalties on him for submitting inaccurate tax returns. They argued that A's share activities represented what they called 'speculative investment' and that this should not be treated as trading. HMRC also questioned whether the activities were carried on 'commercially' for the purposes of S66 ITA 2007 in view of the fact that A had sustained losses for several consecutive years.

Similar cases have been fought in the courts on previous occasions. The outcomes for the taxpayers have varied, depending on the particular facts and also on the jurisdiction of the courts to overturn HMRC's interpretation of the facts. Some relevant examples are:

- Lewis Emanuel & Son Ltd v White (1965) – won;
- Salt v Chamberlain (1979) – lost; and
- Cooper v C&J Clark Ltd (1982) – won.

A appealed to the First-Tier Tribunal, claiming that his share dealing activities satisfied the well-known 'badges of trade'. The Tribunal accepted the taxpayer's arguments concerning four of the badges, namely:

1. the length of the period of ownership;
2. the frequency or number of similar transactions;
3. the way in which the transactions were carried out; and
4. motive.

All of these pointed firmly in favour of trading. The other two badges (the subject matter of the realisation and supplementary work on, or in connection with, the property realised) probably go in the opposite direction, but, on balance, the Tribunal concluded that A was indeed trading. His activities, they said, bore the classic hallmarks of trading, namely that, over an extended period of time, A bought assets with the intention of selling them on, in short order, at a profit. This criterion is the same as that used by HMRC when deciding whether taxpayers who buy and sell on eBay are 'trading' for income tax purposes.

However, the crucial factor seems to have been that A had a business plan, albeit an unwritten one. As the judge said:

'We find that the appellant did indeed have a deliberate and organised scheme of profit-making. We conclude that, on the facts as we have found them, the appellant was carrying on a trade in undertaking his share activities during the tax years in question.'

The Tribunal also decided that the trade was commercial as per both limbs of S66(2) ITA 2007. Transactions took place at market prices, the business plan was pursued with sufficient application and the taxpayer was genuinely trying to make profits. The way in which the share transactions were undertaken was the most important aspect. The fact that A was self-taught, probably overconfident and undertook considerable risk was dismissed as irrelevant. Sadly, he was still short of the skills needed to turn in a consistent profit.

Judgment was therefore given for the taxpayer who was allowed to set off his share dealing losses against his pharmacy profits. The penalties imposed on him by HMRC were cancelled.

Contributed by Robert Jamieson

Casual attitude - Was a trade carried out on a commercial basis?

Summary - The FTT decided that the taxpayer had not carried on a trade on a commercial basis.

The taxpayer claimed to have a car hire business and a trade in foreign exchange. He incurred losses from those activities and sought to set them against his other income. HMRC refused, saying he had not carried on a trade commercially (s66 ITA2007).

Decision:

The First-tier Tribunal accepted that the hiring of his car for one wedding in 2000 and its use as a prop by Pinewood Studios had constituted a trade. However, the car was stolen in 2001 and between that year and 2006 he did not carry on the activity. Further, the loss-making nature of his arrangement with Pinewood Studios and the absence of any other wedding business indicated that his trade was casual and had no commercial basis.

For the years 2006 to 2009, the taxpayer's car hire activities had been as an employee and he had therefore not been trading. From 2009 to 2012, neither car owned by the taxpayer had been available for hire because they had been undergoing repairs. Therefore no trade existed.

The tribunal added that the lack of business records or business plan, the lack of business insurance and his failure to give priority to repairing the vehicles, or to find different ones so that he could offer a car hire service, were evidence that, even if the taxpayer had been trading, he had not been doing so on commercially.

On the foreign exchange and commodities trade, the tribunal found that the taxpayer had undertaken a course to learn how to trade, but afterwards decided not to seek financing to enable him to take the opportunity to trade with others' funds. This activity did not therefore constitute a trade. Even if it had, the taxpayer's casual attitude signified that any trade would not have been carried out on commercially.

The taxpayer's appeal was dismissed.

Comments - Among the the FTT considered many factors, but arguably the most important one seems to have been the taxpayer's casual and cavlier attitude, which seemed to indicate that he had undertaken his activities as hobbies rather than as commercial ventures.

C Lucy v HMRC TC4878

Restitution of ACT on FIDs

Summary - In another instalment of the FII Group Litigation saga, the High Court granted summary judgment to seven claimants.

The claims were for advance corporation tax (ACT) paid on foreign income dividends (FIDs) between 1 July 1994, when the FID regime was introduced in the UK, and 5 April 1999, when ACT was abolished.

The sums relate to the time value of the ACT from the date the taxpayers paid it to HMRC up to when it was deemed to be used or repaid, calculated on the basis that the sum of tax would have attracted compound interest throughout this period.

Decision:

Mr Justice Henderson allowed the claims for payment of the principal sums but not for compound interest on the periods after use or repayment of the relevant advance corporation tax. He refused another of the claims because it was the subject of proceedings in the First-tier Tribunal.

Comments - In another instalment of the FII Group Litigation saga, the High Court granted summary judgment to seven claimants. This case is now only of historic interest

Re FII Group Litigation Evonik Degussa UK Holdings Ltd and others

Holiday karma - Income from letting holiday cottages property or trading income?

Summary – The First Tier Tribunal decided that the taxpayer was receiving income from property and was not carrying on a trade.

In his 2009/10 tax return, the taxpayer showed income from holiday accommodation, music and farming. After an enquiry HMRC concluded that the income from the holiday cottages was property income from furnished holiday lettings.

The taxpayer appealed, saying the holiday cottages income was from a trade.

Decision:

The First-tier Tribunal noted that a whole letting activity would constitute a trade only if the owner remained in occupation of the property and provided services 'substantially beyond those normally provided by a landlord' (HMRC's *Business Income Manual* at BIM22001).

The taxpayer argued that occupation was the most important factor. He said that the estate on which the holiday cottages stood should be viewed as a single parcel of land of which he was the occupier.

The tribunal concluded that the taxpayer did not occupy each unit of accommodation and that to treat the estate as a single parcel of land was 'unduly artificial'. The estate also comprised a manor house rented out by the taxpayer, a cottage owned by his sister and two other residential cottages, in one of which he lived. It would be unrealistic to ignore these so that the taxpayer could be regarded as occupying a single parcel of land.

On the services offered by the taxpayer to guests, the tribunal agreed with HMRC that they were 'typically provided by a landlord' of furnished holiday properties. Rather than being additional services, the recreational facilities increased the attractiveness of the accommodation.

Similarly the provision of breakfast and daily cleaning for an extra charge enhanced the main profit-generating activity of letting the cottages.

The tribunal considered various cases in reaching its conclusion. These included *Sywell Aerodrome Ltd v Croft* 24 TC 126, *Griffiths v Jackson* 1983 STC 184 and *Maclean* (SpC594). The judge said the decision in *CRC v Pawson's Personal Representatives* concerned inheritance tax business property relief and was therefore not relevant.

The taxpayer's appeal was dismissed.

Comments - This is another case to add on the 'dividing line' between trading and property letting. It was interesting to see the Tribunal, in its discussion, question HMRC's formulation in their Manuals – for establishing a trade in the case of furnished accommodation – of '(landlord's) *occupation* plus (substantial) services' (emphasis added); and then express a preference for the 'profit derivation' test. The Tribunal also, separately, expressed its view on the meaning of 'occupation' in the context of s10 ITTOIA 2005.

J Nott v HMRC TC4897

Consequences of breaching an order of the tax tribunals

Summary - The Court of Appeal allowed BPP's appeal from the Upper Tribunal and restored the order made by the First-tier Tribunal to bar HMRC from participating further in the proceedings.

The FTT had debarred HMRC from further participation in the relevant proceedings for its serious and prolonged breach of an order requiring it to give proper particulars of its pleaded case against BPP. The UT had decided that HMRC should not be debarred.

The issue was therefore the proper approach of the tax tribunals in the case of breach of an order. It was established that:

- HMRC had not complied with the order;
- HMRC had not given any reason for its failure; and
- a prejudice had been caused to the taxpayer as 'litigation is not to be conducted by ambush' and HMRC's failure had caused significant delays.

The court observed that there were two conflicting decisions of the UT about the principles that are to be applied when non-compliance with rules and directions falls to be considered by a tax tribunal. In *McCarthy & Stone (Developments) Ltd v HMRC* [2014] UKUT 197, the UT had held that the stricter approach to compliance with rules and directions made under the civil procedure rules (CPR) applied; while in*Leeds City Council v HMRC* [2014] UKUT 350, it had held that that it was not open to it to apply the CPR by analogy.

The Court of Appeal found that the stricter approach should prevail for the following reasons (inter alia):

- The UT is a superior court of record which can take its own view on interpretation and can develop its own precedent.
- There is no justification for a more relaxed approach to compliance with rules and directions in the tribunals.
- It is appropriate that compliance and the efficient conduct of litigation at a proportionate cost are given the weight accorded to them by the FTT in this case.
- If HMRC has a difficulty with compliance it should, where possible, make application to the tribunal to be relieved of compliance on the basis of some alternative proposal.

Comment - Permission for the matter to go to the Court of Appeal was given by Judge Bishopp, who recognised that the key question raised in the appeal is 'a matter of considerable importance to practitioners and the tribunals'. There have been many cases concerning the consequences that should follow if a person fails to comply with a rule or direction and the matters that the court or tribunal should take into account when considering an application for relief from sanctions. However, usually the result turns on the facts

BPP Holdings v HMRC EWCA Civ 121

Discovery assessments and enquiries into returns

Summary - The UT decided that when an HMRC review concluded that a discovery assessment should be cancelled, there was an agreement under s54 TMA 1970 that there had been no understatement of business takings. As the enquiry was querying this same issue, the FTT should have directed that HMRC close the enquiry.

HMRC enquired into the tax return of the appellant ('Easinghall') for the year ended 31 March 2011. Having found that the company had suppressed its purchases and subsequently its sales, and therefore understated its profits the HMRC officer issued a closure notice amending Easinghall's taxable profits. Prior to the end of the enquiry Easinghall submitted its tax return for the year ended 31 March 2012, and the officer also concluded that it was likely that Easinghall had similarly understated its profits and tax liability for that year and therefore issued a discovery assessment for that year. Easinghall appealed against both the amendment and the discovery assessment and sought a review under s42 TMA 1970. The review concluded that in respect of the year ended 31 March 2012, the assessment should be reduced to nil as the reviewing officer found that having considered the basis of presumption of continuity 'there was insufficient evidence to support the amount assessed in this year'.

A week after the review letter the HMRC officer who conducted the original enquiry opened an enquiry in relation to the year ended 31 March 2012.

Easinghall applied to the FTT for a direction under *Finance Act* 1998, Sch. 18, para. 33 that the enquiry be closed on the basis that the review letter acknowledged that the appeal against the discovery assessment for the year ended 31 March 2012 was settled by a a s54 agreement and that therefore no amendment could be made which related to this same issue and, therefore, HMRC could have no reasonable grounds for continuing the enquiry.

The FTT dismissed the application. It found that the wording of the review letter meant that it was the presumption of continuity that did not justify the additional assessment and there was no wider agreement that Easinghall's profits were those shown on the return or that profits had not been suppressed.

Easinghall appealed to the Upper Tribunal, which allowed its appeal.

Decision:

The UT disagreed with the FTT on the question of what was the 'particular matter' which was the subject of the s54 agreement. The UT decided that the FTT erred in not considering the wording of the review conclusion letter in the context of the relevant statutory provisions, and referring to Scorer (HMIT) v Olin Energy Systems Ltd[1985] BTC 181, the question was not why the HMRC reviewing officer arrived at the conclusion he did but rather what that conclusion was. HMRC were bound by the reviewing officer's cancellation of the discovery assessment not to be able to assert again that Easinghall had understated its business takings in respect of the year ended 31 March 2012. That was the particular matter or point at issue that was agreed between the parties and HMRC could not amend the return as a result of an enquiry into the same matter in the light of that settlement. Although it was true that the reason why the reviewing officer came to that conclusion was because there was insufficient evidence put forward by HMRC to support the discovery assessment it was not right to describe the matter in question as 'whether there was enough evidence to show that there had been an understatement of business takings'.

The UT held that the FTT should have directed HMRC to close the enquiry into Easinghall's 31 March 2012 tax return.

Comments - Although the FTT decided that HMRC were bound by an agreement under s54 TMA 1970, it found that the scope of that agreement was only that the presumption of continuity did not justify the additional assessment. The UT has now decided that the matter agreed between the parties was that the taxpayer company had not understated its business takings and was therefore far wider in scope than the FTT had decided.

Easinghall v HMRC [2016] UKUT 105

Recapitalisation and loan relationships

Summary - The First-tier Tribunal dismissed the appeal by Stagecoach Group plc (Group) against enquiry closure notices issued by HMRC denying a tax deduction for a 'derecognition' debit under s320 CTA 2009 finding that the debit, which formed part of a scheme notified to HMRC under DOTAS provisions, was not *a loan relationships debit but a debit in respect of the recapitalisation of a subsidiary and no deduction under Part 5 CTA 2009 (loan relationships) was allowed. The FTT further held that, as a consequence, the arbitrage notice issued to Stagecoach Holdings Limited (Holdings) (the subsidiary company) under s249 TIOPA 2010 was not required and Holdings appeal was allowed.*

The Appellants were Stagecoach Group plc (Group) and one of its (indirect but wholly owned) subsidiaries Stagecoach Holdings Limited (Holdings) and the appeals had been designated as lead cases under the *Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules* 2009 (SI 2009/273), rule 18(2)(b).

In December 2009, Group loaned £88m to Stagecoach Transport Holdings plc (Transport). Transport was a direct subsidiary of Group and the parent of Holding's parent company. The loan was due to be repaid on 31 March 2010 but was then extended until 31 December 2010.

In early 2010, Holdings balance sheet showed net liabilities of £10.8m and Holdings was technically insolvent. Advice was sought from KPMG on recapitalising Holdings. The thrust of the advice given by KPMG was that if the recapitalisation proceeded by way of a forward subscription agreement (FSA), the contingent subscription amount would not be taxable in the hands of Holdings and would be given tax relief as a 'derecognition debit'. In other words, tax relief could be obtained for the cost of a share subscription in Holdings without Holdings being taxable on the monies it received. The arrangements were notified to HMRC under the Disclosure of Tax Avoidance Schemes (DOTAS) provisions, described as 'Tax-efficient recapitalisation of subgroup by derecognition …' and a scheme reference number was issued.

In October 2010, Group and Holdings entered into the FSA pursuant to which Holdings agreed to issue 20,000 ordinary shares of £1 each to its parent company Integrated Transport Company Ltd (ITCO) on 31 December 2010 and Group agreed to pay the nominal subscription amount of £20,000 plus a contingent subscription in a sum equal to 22.4% of the principal and interest repaid to Group under the Transport loan up to a maximum of £20m. On entering into the agreement and following UK GAAP and FRS 26, Group derecognised an amount equal to £19.735m representing the 22.4% of the principal amount of its loan to Transport that would now pass to Holdings. The accounting entries were debit (increasing) the cost of investment in Holdings and credit (decreasing) the loan receivable due from Transport.

The nominal subscription amount of £20,000 was paid to Holdings the following day. On 31 December Transport repaid the full amount of its loan plus interest and as 22.4% of the amount received exceeded the £20m limit, a payment of £19.980m (£20m minus the £20,000 already paid) was made to Holdings. Holdings issued £20,000 shares of £1 each to ITCO.

In its corporation tax return, Group brought into account a non-trading deficit of £37.7m in respect of its loan relationships for the accounting period ended 30 April 2011. Within this amount was the loan relationship derecognition debit claimed under s320 CTA 2009 pursuant to the FSA with Holdings. In its corporation tax return for the period ended 30 April 2011, Holdings did not recognise as taxable any amounts received from Group under the terms of the FSA. HMRC issued Holdings with an arbitrage notice under s249 TIOPA 2010 and Group with an enquiry closure notice concluding that Group was not entitled to claim a deduction for the derecognised amounts representing the proportionate share of the loan asset to be passed to Holdings. Group appealed the closure notices and Holdings appealed the arbitrage notice.

The parties presented the FTT with a list of issues to be determined:

Issue aa: whether the debit claimed by the Appellant (Group) is in respect of a company's loan relationship within s320 CTA 2009;

(1)Issue a: whether the deductibility of debits under s320 CTA 2009 was subject to the provisions of s307(3) CTA 2009;

(2)Issue b: if so, whether s307(3) CTA 2009 required the debits and credits to be tested to establish their nature;

(3)Issue c: if so, the issue of whether the debits claimed by the Appellants fairly represented losses arising from their respective loan relationships under s307 CTA 2009;

(4)Issue d: whether there was an amount to be brought into account under the relevant provisions of TIOPA 2010, and in particular whether the receipt scheme conditions in s250 TIOPA 2010 were satisfied;

(5)Issue e: whether, under s254(1)(b) TIOPA 2010 each of the receipt scheme conditions has to be met in relation to the company at the time the notice is given, so that notices given after the 'schemes' have been completed were invalid (this issue was subsequently withdrawn);

(6)Issue f: whether there could be a charge to tax under Sch D Case VI in the relevant periods, as stated in HMRC's closure notices.

Decision:

Dealing with issue (aa) first, the FTT determined that the debit to investments was not a loan relationships debit. The loan by Group to Transport already existed when the FSAs were entered into and the debit brought into account. The debit was in respect of the recapitalisation of the subsidiary through the medium of an FSA and that was the transaction. The pre-existing loan relationship was incidental; it was essentially the mechanism by which the contingent subscription amount was calculated and that sum was not in respect of the loan relationship, it was in respect of the FSA which determined its amount and specified the obligations to be implemented in respect of it.

The debit was not a loss from a loan relationship, it did not represent a loss at all. The loan principal and interest were repaid in full and that loan relationship led to a profit not a loss. The debit represented increased investment in the subsidiary and future economic benefit.

S320 CTA 2009 was to be construed in the context of the overall purpose of Part 5 CTA 2009, namely to determine how profits and deficits arising to a company from its loan relationship were to be brought into account for corporation tax purposes. S320 CTA 2009 gave relief for an expense in respect of a company's loan relationship where because, and only because, of the accounting treatment (debiting the balance sheet rather than the profit and loss account), that relief would otherwise be denied. But the debit in question did not create a deficit in respect of a loan relationship.

Accordingly, the FTT answered issue (aa) by holding that the debit claimed by Group was not in respect of a company's loan relationship within s320 CTA 2009. On that basis Group's appeal failed. The receipt notice on Holdings was no longer required and would fall away and the appeal against Holdings was, therefore, to be allowed. However, given the decision could be appealed, the FTT continued to set out their views on the remaining issues albeit noting that these views were obiter.

The FTT noted that it was difficult to accept that a loan relationship on which a creditor received full payment including interest and thus made a profit, somehow yielded a relievable loan relationship loss but even if, contrary to their view, the debit to investments was somehow a debit in respect of a loan relationship falling within s320 CTA 2009, it did not fall within the debits specified in s307(3) and could not be brought into account in determining Group's profit and losses for corporation tax purposes.

Accordingly, the FTT answered issue (a) by holding that the deductibility of debits under s320 CTA 2009 was subject to the provisions of s307(3) ; issue (b) by holding that s307(3) required the debits and credits to be tested to establish their nature, and issue (c) by holding that the debit claimed by Group did not fairly represent losses arising from its loan relationships under s307.

Turning to issues (d) and (f), the FTT noted that tax arbitrage was the exploitation of asymmetries between different tax regimes to achieve a reduction in the overall tax liability of entities such as companies, often in a group. Usually, there was a mismatch between two tax regimes or codes, e.g. where a tax deduction by one company was not matched by a taxable receipt of another company. Such mismatches and other contrived arrangements to avoid tax were the subject of anti-arbitrage rules in Part 6 TIOPA 2010. Two kinds of counter-action notices could be issued: deduction notices and receipts notices. Both required the company to recalculate its liability to corporation tax less advantageously.

Holdings had been issued with a receipts notice under s249 TIOPA 2010. Receipts notices were dealt with by ss249 to 254 TIOPA 2010. Four receipt scheme conditions had to be met (A, B, C and D). It was already accepted that condition A was met (there was a scheme). The FTT found that the argument that the injection of about £19.8m into Holdings was somehow not a contribution to its capital could not be accepted and receipt scheme condition B was met.

Group and Holdings expected that a benefit (within the meaning of receipt scheme condition C) would arise: tax relief on the debit and no tax charge on the receipt constituted a benefit for Group and/or Holdings within any reasonable construction of that phrase as it appeared in receipt scheme condition C and condition C was satisfied. For the purposes of condition D, the deductible amount was the (assumed) allowable debit under s320 CTA 2009 and there was no taxable income against which the deductible amount was to be set and condition D was also satisfied.

Accordingly, the FTT answered issue (d) by holding that there was an amount to be brought into account under the relevant provisions of TIOPA 2010 and that the receipt conditions in s250 TIOPA 2010 were satisfied.

The argument on issue (f) was that even if Holdings were required to bring the £19m into account there was no mechanism for charging it to tax because s254 TIOPA 2010 was not a charging or application provision, nor TIOPA 2010 a charging act. The FTT noted that ss2 and 5 CTA 2009 imposed a charge on profits, which included income and chargeable gains. Holdings was require to recalculate its income on the basis that the qualifying payment was chargeable to corporation tax. The recalculated income plainly did fall within the charge to corporation tax on income by virtue of s254 TIOPA 2010. The FTT answered issue (f) by holding that although there could not be a charge to tax under Sch D Case VI in the relevant period, as stated in HMRC's Closure Notices, there was a charge to tax by virtue of s254 TIOPA 2010 and ss2 and 5 CTA 2009[5]. The FTT noted that no point had been taken on the basis that the Notice wrongly referred to Sch D Case VI rather than mirroring the equivalent words of s254(2) TIOPA 2010.

In summary, therefore, the FTT dismissed Group's appeal and, as a consequence, allowed Holding's appeal but stated that in the event that Group appealed the decision against it, the FTT expected HMRC to appeal the Holding's decision so that all the issues could be heard together again.

Comments - In this case a group of companies entered into a tax avoidance scheme designed to create a tax deduction in the parent company (Group) without a corresponding taxable receipt in any other company. The transactions involved a subscription by Group for shares in a subsidiary (Holdings) using a forward subscription agreement which was linked to an existing group loan. Tying the subscription in with the loan was said to bring what was effectively the debit for the subscription price paid for the shares within the loan relationships provisions, creating a tax deductible loan relationships debit. The FTT has ruled, however, that the debit was not a loan relationships debit at all and consequently the scheme failed. The FTT has also expressed a view on all of the issues raised in respect of the tax arbitrage notice issued by HMRC on Holdings albeit that these views were all obiter. The conjoined appeal by Holdings was allowed as the consequence of the finding that there was no tax deductible debit for Group was that the tax arbitrage notice was no longer required and fell away.

Stagecoach Group and Stagecoach Holdings v HMRC TC4866

Profit extraction under the new dividend tax regime (Lecture B948 – 19.34 minutes)

Tax rules affecting profit extraction

Personal savings allowance: the first £1,000 of interest is taxed at 0% if a basic rate taxpayer (£500 if a higher rate taxpayer)

Starting rate of tax: there is a 0% tax rate on the first £5,000 of interest income, if general income is covered by the personal allowance. This will not therefore apply if the taxpayer has significant other income outside company, e.g. rental income, self-employment income

Dividend allowance: the first £5,000 of dividends will be taxed at 0%, irrespective of level of income from 2016/17 onwards

Dividend tax rates: from 2016/17 dividends not covered by allowances are taxed at 7.5% in the basic rate band from 2016/17 (effective rate is nil in 2015/16), 32.5% in the higher rate band (effective rate is 25% in 2015/16) and 38.1% in additional rate tax band (effective rate is 30.56% in 2015/16)

Doing nothing different in 2016/17

Assuming a salary is taken equal to the NIC primary threshold of £8,060 (both years) and all post-tax profit is taken as dividends, for corporate profits above £17,985, more tax will be payable in 2016/17 if no action is taken. This assumes the taxpayer has negligible other income.

Profit before salary and tax		50000
Salary		8060
		41940
Corporation tax	20%	8388
Post tax profit (= dividend)		33552

		2015/16			2016/17		
		Salary	Divs	Total	Salary	Divs	Total
Salary		8060		8060	8060		8060
Dividends	(x100/90)		37280	37280		33552	33552
				45340			41612
Maximum	PA	8060	2540	10600	8060	2940	11000
		0	34740	34740	0	30612	30612
Tax		0	20%	0	0	20%	0
		31785	10%	3179	5000	0%	0
		2955	32.50%	960	25612	7.50%	1921
		0	37.50%	0	0	32.50%	0
					0	38.10%	0
	Tax credit	34740	10%	-3474			
	Net liability			665			1921

Actions to consider for 2015/16 and beyond

Charging interest on loan balances

Because of the starting rate of 0% for interest, it is worth the director/shareholder charging interest to the company for any loan balance.

This will give a tax deduction in the company and no income tax for the owner. As the loan is unsecured, the interest rate can be set appropriately high.

For 2016/17, if the loan balance owed to the director/shareholder justifies, interest of up to £7,940 can be charged with no income tax cost. This is in addition to salary of £8,060 and dividends of £5,000.

£2,940 of the interest will be covered by the personal allowance and the other £5,000 will be taxed at the starting rate of 0%.

This enables the withdrawal of a total of £21,000 tax free for the owner/shareholder. The company saves tax on the interest of £1,588 increasing distributable profits.

The loan balance might originate from incorporation when goodwill and other assets were transferred in to the company.

Any loan balance could be increased by crediting 2015/16 dividends to the loan account if the cash is not needed.

CT61s would be needed for interest paid by the company to the individual and 20% income tax would need to be deducted at source and paid over to HMRC

Accelerating dividends into 2015/16

Assuming that dividends in excess of the dividend allowance would be paid in future years, is it worth voting more dividends in 2015/16?

A comparison of marginal tax rates is needed. If the accelerated dividends would not affect tax banding (e.g. moving from basic rate to higher rate, or higher rate to additional rate) it is worth accelerating the dividends where possible.

If additional dividends would move the taxpayer from basic rate to higher rate in 2015/16 not it is worthwhile if the taxpayer would not be higher rate in 2016/17

- 25% tax in 2015/16, 7.5% tax in 2016/17

Similarly if additional dividends move the taxpayer from higher rate to additional rate in 2015/16 , it would not be worthwhile accelerating

- 37.5% tax in 2015/16, 32.5% tax in 2016/17

We also need to factor in the possible loss of child benefit above £50,000 and personal allowances above £100,000 when considering acceleration of dividends.

Deferring dividends to 2016/17

A taxpayer who can draw dividends from his limited company, but for whom other income forms the main part of his taxable income could forgo dividends of up to £21,667 in 2015/16 in favour of 2016/17 (and subsequent years) and pay the same or less tax on the distribution.

The equivalent amount for additional rate taxpayers is £25,250.

Some clients may therefore wish to retain a debit balance on the director's loan account rather than clearing it with dividends before 6 April 2016.

Utilising the dividend allowance of others

Family members (e.g. children over 18) could be gifted shares in the company and receive their share of dividends in future. This would not work for children under 18 as the income would still be taxed on the parent.

Be mindful of possible CGT exposure on gifts if the company is not a qualifying trading company

The gift must be 'no-strings' so the income would be the family members' to do with it what they like.

Each family member is entitled to £5,000 dividends tax free. This can be potentially useful where adult children are at university. The dividends can be used as living expenses rather than parents paying these out of post-tax income.

The dividends will count towards the income limit after University when calculating student loan repayments so unless the structure is unwound later, marginal 'tax' (loan repayments) of 9% would arise when the child's income goes above the limit for student loan repayments.
It is possible to use alphabet shares to provide for different dividend rates for family members. Care needs to be taken to ensure no possibility of attack under income-shifting laws so you should take advice where necessary.

Other tax efficient use of company funds

It is always worth considering additional pension contributions as a tax-free benefit in place of additional dividends.

Be mindful of the annual allowance (and its possible tapering in 2016/17 where income is very high).

It is also worth considering the use of trivial benefits to extract a little more tax-free benefit from the company. These must be no more than £50 per benefit, with a maximum of £300 for a director and their family if it is a close company and must not be a reward for services.

Contributed by Malcolm Greenbaum

VAT

No direct link - Claim for deduction of input tax

Summary - The Upper Tribunal dismissed the company’s appeal against the decision of the First-tier Tribunal to uphold HMRC’s rejection of its claim to recover input tax on the basis that no economic activity was being carried out

The taxpayer was a UK parent company of a group that carried out gold mining activities in Australia. The taxpayer was registered for VAT under the classification for management consultancy and claimed input tax on UK expenses. HMRC refused the claim on the basis that the taxpayer had not been carrying on economic activity because it had not been making, nor did it have an intention to make, supplies for consideration for VAT purposes.

The First-tier Tribunal dismissed the taxpayer's appeal.

Decision:

The Upper Tribunal said the main issue was whether the supplies made by the taxpayer to its subsidiaries had been for consideration within the meaning of art 2(1) of the Principal VAT Directive and s5(2) VATA 1994.

Mr Justice Warren said the supplies had not been made for consideration; they had been made gratuitously. The taxpayer had agreed that a charge would be made only when the subsidiaries could afford to pay. He agreed with the First-tier Tribunal's findings that there was no evidence to suggest that there had been any intention, once the supplies had been made without payment, that they would be paid for later.

He said an intention to make supplies was not a sufficient basis on which to recover input tax. The taxpayer needed to establish that it had the intention of making at some time in the future supplies for a consideration. It had to establish a direct and immediate link between the services supplied and the sums levied or to be levied. The taxpayer relied on a vague intention that payment would be made but had failed to establish that consideration had been given for the services provided.

The taxpayer's appeal was dismissed.

Comments - If Norseman had made supplies of management services to the subsidiaries, such supplies would have been taxable supplies until 31 December 2009, when s7A VATA 1994 applied and the law on the place of supply were changed.

Norseman Gold plc v CRC, Upper Tribunal

Multi-conversion – Zero rating where an additional dwelling is created

Summary - The First-tier Tribunal applied zero rating to the whole onward supply when an additional dwelling is created out of a mixed use property.

In *Calam Vale Ltd* (VTD 16,869), it was decided that a project that incorporated part of the previously residential part in each of two new dwellings did not qualify for zero-rating; if the upstairs had been residential and the downstairs not, then a conversion into ground floor and second floor flats would qualify for zero-rating on half, but a conversion into two semi-detached houses would not qualify at all.

This approach was not followed in the later case of *Alexandra Countryside Investments Ltd* (TC02751), where the judge noted the CA decision in relation to DIY claims in *HMRC v Jacobs* and concluded that there was no logical reason to allow a DIY claim under s.35 VATA 1994 but to disallow the zero-rating of an identical project under s.30 and Sch.8 Group 5. HMRC did not appeal that decision, but have never agreed with it, and put to the present Tribunal that it had been wrongly decided.

Macpherson

The *Macpherson* appeal related to the same kind of project – the conversion of a shop with living accommodation above into two semi-detached houses. HMRC ruled that the sales of both houses could only be exempt. The key point is the application of Group 5 Notes 7 and 9:

7: For the purposes of item 1(b), and for the purposes of these Notes so far as having effect for the purposes of item 1(b), a building or part of a building is "non-residential" if-

(a) it is neither designed, nor adapted, for use—

(i) as a dwelling or number of dwellings, or

(ii) for a relevant residential purpose; or

(b) it is designed, or adapted, for such use but—

(i) it was constructed more than 10 years before the grant of the major interest; and

(ii) no part of it has, in the period of 10 years immediately preceding the grant, been used as a dwelling or for a relevant residential purpose.

9: The conversion, other than to a building designed for a relevant residential purpose, of a non-residential part of a building which already contains a residential part is not included within items 1(b) or 3 unless the result of that conversion is to create an additional dwelling or dwellings.

The Tribunal "respectfully disagreed" with the Tribunal in *Alexandra Countryside Investments*. The Tribunal had to consider the conversion that had actually taken place: it was clear that the building that had been converted had not been, within the definition of the law in Note 7, "a non-residential building" before the conversion. In s.35, the law used the phrase "to the extent that", which allowed a project to qualify in part. Under s.30, it had to qualify or not qualify.

To put it another way, the judge in *Alexandra* appeared to have concluded that "Note 9 requires an additional dwelling to be constructed, which has happened, so the project falls within Item 1(b)"; the judge in the present case started from the opposite direction, holding that "Zero-rating requires the project to fall within Item 1(b) to begin with, which it doesn't because of Note 7, so it doesn't matter what the outcome of the project was." Similarly, Note 10 (which deals with apportionment) was not engaged. The project was wholly exempt, and the appeal was dismissed.

Languard

Now another FTT judge (Jane Bailey) had disagreed again. She was considering a similar situation to *Macpherson*, and was aware of the decision that the FTT had reached in that case – this is not a parallel case that happened to come to a different decision, but a subsequent case that disagreed.

The project converted a three-storey pub into a four-storey building containing four dwellings. The two lower floors became maisonettes that incorporated part of the ground floor (formerly pub) and first floor (formerly manager's accommodation); two more "upper maisonettes" comprised the old top floor (formerly manager's accommodation) and the new top floor (new construction).

The appellant treated the sale of major interests in all four properties as zero-rated in 2011. It was subsequently agreed that the sale of the upper maisonettes was exempt, but the company appealed to the Tribunal in relation to the lower maisonettes.

The taxpayer's representative criticised the decision in *Macpherson* for a lack of any indication of when Note 9 would, or could, be engaged. He suggested that the reasoning of the Court of Appeal in *Jacobs* was compelling in relation to s.30, even if not binding as it would be in relation to s.35.

The judge posed the question as "*whether the ground floor was converted 'into a building designed as a dwelling or number of dwellings'*". She noted that the Tribunal in *Calam Vale* had decided this kind of project was not within Item 1(b), because it refers to "converting a non-residential building or a non-residential part of a building into a building designed as a dwelling or number of dwellings" rather than "converting a non-residential building or a non-residential part of a building into a building or part of a building designed as a dwelling or number of dwellings".

The judge commented that if this was correct, Note 9 could have no application. If item 1(b) could only apply to buildings that were wholly non-residential before the conversion, then there would always be a new dwelling or dwellings afterwards, because there would be no dwellings beforehand – so Note 9, which was drafted at the same time as item 1(b), would be meaningless. HMRC's representative was invited to suggest when it might apply, but could not come up with an example.

The judge also commented that a conversion would appear only to satisfy Note 9, under the reasoning in *Macpherson* if it not only was "horizontal rather than vertical" (creating two flats rather than two maisonettes) but also did not touch the formerly residential part at all – a project that affected the whole building would not be "a conversion of a non-residential part of a building", but would be "a conversion of a building containing a residential part". This seemed unnecessarily strict.

Given the confusion that these provisions have continued to cause, it is worth reproducing the careful reasoning of the judge in full:

37. We consider that the purpose of Note 9 is to exclude from Item 1(b) any conversion of a mixed use building into dwellings unless additional dwellings (when compared to the building as a whole before conversion) have been created as a result of the conversion of the non-residential part of the mixed use building. The draftsman of Item 1(b) must have considered that the conversion of the non-residential parts of mixed use buildings into dwellings would fall within Item 1(b) in order to have considered it necessary to draft Note 9 to exclude some of such conversions.

38. As the effect of converting the non-residential part of a building alone (that is to say the non-residential part not combined with any residential part) into a dwelling would always be to create more dwellings than previously existed, we conclude that the draftsman must have contemplated the possibility that one or more new dwellings would be created from bringing together residential and non-residential parts of the mixed use building. We bear in mind that to achieve the social purpose of creating additional housing it does not matter from what constituent parts the new dwellings are created provided that additional dwellings are created as a result. However Note 9 would be required in order to ensure that relief is available only in those situations where additional housing is created.

39. If we are correct in our understanding of Note 9 then a mixed use building which previously contained one dwelling would be excluded from Item 1(b) if the result of converting the non-residential part was to create one large dwelling. However, the conversion would be included in Item 1(b) if the building was converted into two or more moderately sized dwellings. In the second case, housing stock is increased and so relief under Section 30 would be available. This is in accordance with our understanding of the social purpose behind Group 5.

40. Looking at Item 1(b) in the light of our conclusions regarding Note 9, we conclude that "converting … a non-residential part of a building into a building designed as a … number of dwellings" should be construed as meaning that the non-residential part of a building has changed its character and now forms part of a building designed as a number of dwellings.

It follows that we agree with the Appellant and prefer the careful reasoning of the Court of Appeal in Jacobs and of the Tribunal in Alexandra Countryside. It seems to us that this is the better interpretation of Item 1(b) as it enables Group 5 to be interpreted as a coherent whole.

The comparison exercise was between the situation before (non-residential part of a building) and the situation afterwards (building containing four dwellings); the non-residential parts had changed their nature, and the supply of the major interest grants in the lower maisonettes fell within item 1(b). That suggests that the whole supply is zero-rated, and the VAT incurred on work relating to the conversion of the first floor should also be recoverable – there is no scope for a claim "to the extent that", as there was in *Jacobs*.

First-Tier Tribunal (TC04917): *Languard New Homes Ltd*

Too late to claim - Repayment claim to recover UK VAT paid by non-EU company

Summary – The Tribunal dismissed the taxpayer's repayment claim.

In September 2013, the taxpayer, a US-based company, submitted a claim to recover VAT paid in the UK on three expenses; the total claimed was £4,500. The UK legislation (s39 VATA 1994) implements the EU 13th Directive, and requires any claim for the year to 30 June to be submitted before 31 December of the same year. The claimant must also provide a certificate of status from the tax authority in its own country, confirming it is a business.

In this case, £4,200 of the VAT related to the year to 30 June 2013 and the balance, £309 related to the year to 30 June 2014. HMRC refused to accept the claim because there was no original certificate of status — the company had sent a copy. The department wrote to the company explaining the procedures to obtain a certificate from the authorities in Philadelphia. The company did this but submitted the correct paperwork in January 2014, which was too late for the invoices for the June 2013 period.

The taxpayer argued that the key date should be 18 September 2013, when it submitted the first claim, but HMRC said the claim 'had not been accepted or entered as a claim'. Therefore the resubmitted claim was a new one.

Decision:

The First-tier Tribunal agreed with HMRC. The taxpayer's appeal was dismissed.

Comments - Neil Warren, independent VAT consultant, noted: 'The overseas VAT repayment system benefits many non-EU businesses that incur VAT in the UK but it is important that all paperwork is correctly submitted to HMRC at the first attempt. This is one of the few VAT returns that must still be submitted on paper rather than electronically. Any business that does not follow all of the rules risks having its claim rejected — and the six-month window may then pass before matters are sorted out.'

Comoretel Holdings Ltd v HMRC TC4750

Past perfect - Nature of credits bought by a website customer

Summary – The Upper Tribunal allowed Findmypast's appeal against the decision of the First-tier Tribunal to uphold HMRC's rejection of a claim for repayment of VAT that had been accounted for on unredeemed (unused) vouchers.

The taxpayer provided online access to genealogy and ancestry information. Customers could search the historical records on the website free, but had to buy PayAsYouGo (PAYG) credits or a subscription, or use a voucher to view them. Under PAYG, a customer paid a lump sum for which he received credits that expired after a fixed time. Unused credits would be revived if the customer bought more credits within two years, otherwise they were lost.

The taxpayer claimed a repayment of VAT on the basis no VAT liability arose when credits had not been used because there had been no taxable supply. The claim related to the period from September 2008 to May 2012. After that date, the law was changed to make VAT due on single-purpose face-value vouchers at the time of their issue.

HMRC refused the claim, saying that, in return for the purchase of the credits, customers received a package including the facility to search for genealogical information and the ability to download them. The two were interdependent.

The First-tier Tribunal agreed with HMRC. The taxpayer appealed.

Decision:

Lord Glennie in the Upper Tribunal agreed with the taxpayer that the use of the search engine did not form part of a package paid for by the customer when he purchased PAYG credits. The credits gave him the right to access documents, as long as he did so within the specified time.

The judge said the service was provided when the records were accessed. There was no link between the payment and the use of the search facility; the supply of credits gave the customer access to records.

The second issue was whether the credit was a face-value voucher within Sch 10A Para 1(1) VATA 1994. The judge said the credit balance shown on the website represented the right to access documents up to a particular amount. For the customer, that was represented by credits that he had paid for.

The fact that it was recorded on the website in terms of credits rather than by reference to money value was not relevant. The customer knew he had a certain number of credits. These satisfied the conditions in para 1(1) in that they were, in effect, vouchers in electronic form that gave the customer the right to receive goods or services to the value of the amount recorded.

The taxpayer's appeal was allowed.

Comments - On 10 May 2012, the law was changed so that VAT is due on the issue of face-value vouchers, not on redemption. Findmypast's claim could not be maintained beyond that date.

Findmypast Ltd v CRC, Upper Tribunal

Extending a claim for VAT repayment with another claim

Summary - The UT agreed with HMRC that whilst it is permissible to amend a claim, it is not permissible to do so by effectively replacing one claim with another after the expiry of the statutory time limits but while the claim remains unresolved.

Vodafone had written to HMRC requesting a repayment of over £4m, representing the amount by which it claimed to have over-declared its liability for output tax under the Nectar card scheme in its VAT returns for the periods 01/04 to 01/06. HMRC had disagreed and rejected the claim. Vodafone had subsequently made further claims (the 'later claims') unrelated to the Nectar scheme. Although HMRC accepted that those claims related to overpayments of VAT, it refused to repay some of them on the ground that they had been made out of time. Vodafone contended that it was possible to amend the Nectar claim, which had been made in time, to encompass those later claims.

Decision:

The UT observed that a taxpayer's claim under s80(2) VATA 1994 was not simply for a sum of money, but was for a sum of money related to particular transactions in respect of which output tax had been wrongly accounted for. It was therefore not possible to extend the claim to cover entirely different transactions.

The UT added that *Reed Employment* [2013] UKUT 109 was authority for the proposition that 'a claim could be amended, even if the amendment consisted of a change in the amount claimed or the method of calculation, as long as the fundamental character of the claim was unchanged: in other words, the amended claim had to arise out of essentially the same facts or circumstances as the original claim'. This was not the case here and the errors discovered by Vodafone after the Nectar claim could not be subsumed into it.

Comments - This seems to be a sensible decision as the option of substituting one claim for another unrelated claim would allow taxpayers to circumvent the statutory time limit imposed by s80(4) VATA.

HMRC v Vodafone Group Services Upper Tribunal

Had a building been demolished?

Summary - The Upper Tribunal found that the FTT had correctly concluded that the retention of a small portion of the front façade of the demolished existing building prevented the work from being zero-rated under Sch 8 Item 2 VATA 1994.

The appeal concerned HMRC's decision that certain supplies by Boxmoor were not zero-rated supplies in the course of the construction of a building designed as a dwelling (Sch 8 Group 5 VATA 1994). Instead, HMRC found that they were standard rated, on the ground that the house that had originally stood on the site had not been completely demolished to ground level. A small portion of the front facade had been retained (including part of a projecting bay).

The FTT had found that the retention of the facade had been part of an understanding between the architect and the planning authorities about the limits to the degree of demolition which would be accepted at the property, without contravening a planning consent for alterations and extensions, not demolition. The UT observed that for Note 18(b) to be satisfied, the planning consent should require, rather than permit, the retention of the façade, so the FTT had been entitled to find that the retention of the façade was not a condition of the planning consent.

Decision:

The UT also rejected the argument that the FTT should have found that the retention of the projecting bay was de minimis, so that the original building should be regarded as having been completely demolished (Note 18(a)). The UT found that the projecting bay could not be considered to be de minimis, given that what remained was capable of being a facade for the purposes of Note 18(b).

Finally, the UT found that the works should be regarded as the alteration and extension of an existing building within Note 16.

Comments - It is an absolute requirement for zero-rating that the retention of part of an existing building must be no more than a single façade or, where a corner site, a double façade and that the retention must be a condition or requirement of statutory planning consent or similar. It is interesting in this case that, although the planning authority had informed the architect that planning permission would be nullified if the building were to be completely demolished, the UT refused to infer that the planning consent contained a condition or requirement that the projecting bay must be retained. Since many VAT disputes turn on the wording of the planning permission it is important to ensure that the consent is both clear and complied with.

Boxmoor Construction v HMRC Upper Tribunal

VAT periods and repayment claims

Summary - The Upper Tribunal found that claims for repayment of overpaid output tax did not comply with VATA 1994 as a global figure for a whole year did not suffice instead of prescribed accounting periods

The two appellant companies (BAC and BAS) had written to HMRC purporting to claim the repayment of wrongly paid output tax. The letter had been sent on the penultimate day of the time limit for making such claims and stated the value of BAS's claim as a global figure, not separated into individual amounts for each of the VAT periods within the year. The letter also indicated that BAC intended to make a claim on the same basis. HMRC rejected the claim on the ground that it did not satisfy the statutory requirements.

The FTT had accepted that BAS had made a valid claim; but it had found that, in relation to BAC, the letter had been no more than the notification of a prospective claim.

Decision:

The UT noted that s80(2) VATA 1994 required the claim to be 'made in such form and manner' as may be prescribed; and that VAT Regulations SI 1995/2518 reg 37 contained the prescription. There was no room within reg 37 for a claim to be made without the specification of an amount or the method of calculation, but upon the basis that these would be provided later. Consequently, even if the overall claim related to several prescribed accounting periods, a separate claim must be made for each period, identifying that period, the amount for which repayment was sought and the method by which it had been calculated.

Comments - The UT has found that the finding of the FTT was incorrect, a total for several accounting periods did not comply with s80 VATA 1994 and neither did the claims for the other years for which no amounts were specified.

HMRC v Bratt Auto Contracts and Bratt Auto Services Upper Tribunal

VAT payments on account regime – Size does matter

Summary - The FTT found that a taxpayer was required to pay VAT under the payment on account regime even though the threshold had increased and so the taxpayer's turnover was below it.

HMRC required the taxpayer to pay VAT under the payment on account (POA) regime. It said the company had made three payments late for the 9/11 quarter and imposed a surcharge.

The taxpayer said the POA regime should not have applied for the 9/11 quarter because its liability had not exceeded the relevant threshold in 3/11. As a result, two of the payments had been made early. It said the third one should have been granted the seven-day extension enjoyed by other traders that were not in the POA regime. HMRC's refusal to allow this was contrary to the EU principle of equal treatment.

The First-tier Tribunal dismissed the taxpayer's appeal.

Decision:

The Upper Tribunal found that, in the period ended 3/11, the taxpayer's VAT liability was higher than £2m, which had been the threshold at that date. The POA regime therefore applied from the 9/11 quarter, even though the taxpayer's VAT liability had not exceeded the new threshold of £2.3m.

On the EU principle of equal treatment, the tribunal said POA regime traders were not comparable to ordinary traders or large traders that opted to make monthly returns. The judge said there were several payment regimes applied by HMRC to different categories of trader and each had a bundle of obligations that had developed over time and had to be considered together.

Traders large enough to generate a VAT liability of more than £2m a year could be placed in the POA regime if was in the interests of the national economy. In the judge's view, 'the size of the VAT liability over a reference year is the “essential characteristic” which causes a trader to become subject to the POA regime in the first place' and this distinguished it from the ordinary trader who was not.

The taxpayer's appeal was dismissed.

Comments - The FTT rejected the argument that the taxpayer was entitled to choose its basic period**.**

Marsdens Caterers of Sheffield v CRC, Upper Tribunal

Tripartite arrangement on the supply of staff

Summary – The First-tier Tribunal dismissed the appeal by Adecco UK Ltd against HMRC's refusal of its claim for repayment of output VAT accounted for on the part of the fee received from its clients that represented the wages it paid to its temporary workers.

The taxpayer provided recruitment services. It supplied temporary workers to clients. It accounted for VAT on the full charge paid by clients for the services of the temporary workers. This comprised the amount paid by the client representing the worker's wages and the commission.

After the decision in *Reed Employment Ltd* (TC1069) in which the tribunal found that the employment bureau was not liable to account for VAT on the element of the charge representing the wages to be paid to the workers, the taxpayer claimed a repayment.

HMRC rejected this, on the basis that the taxpayer was liable to account for VAT on the full charge paid by the clients because it supplied the services of the non-employed temporary workers and was not supplying the service of introducing workers to its clients only.

The taxpayer said 'control' was a key issue. It claimed the duties of the temporary worker were controlled by the client, not the agency. Further, a contract was terminated by the worker or the client, never by the agency. There was no monitoring of the worker's performance by the agency — this was only carried out by the client, who had the right to dispense with the worker's services if they were not performing to an acceptable standard. The agency had no obligation to provide work to the worker. However, the risk of a bad debt was wholly the taxpayer's, so a temporary worker would be paid, even if the client did not pay the agency.

Decision:

The tribunal decided that the economic reality and contractual position were that taxpayer provided services to the client and not the worker, while the latter provided services to taxpayer. Output tax was therefore due on the full value of the payment made by the client to the taxpayer.

The appeal was dismissed.

Comments - Neil Warren, independent VAT consultant, commented: 'There have been several recent First-tier Tribunal cases in which the decision reached appears to have contradicted a previous case even though the facts seemed to be identical. In this one, the court has, in effect, overruled the verdict in *Reed Employment Ltd.* It is likely the taxpayers will appeal, and a hearing in a higher court might be useful.'

Adecco UK Ltd and others v HMRC TC4743

Exemption for political clubs

Summary - The FTT found that club's membership subscription did not fall within the exemption for a body whose objects were 'in the public domain' and of a 'political nature'

The club was a not for profit organisation. Its stated object was to 'promote by all proper means the principles of Conservatism, and the implementation of the Conservative Party's policies'. It contended that its membership fee were exempt.

Decision:

The FTT stated that it must decide 'what the members actually got in return for their subscription'. It considered that members received the right to attend the premises of the club with its low-price bar, to read the magazines, to take part in the various social and political activities, to use the sports facilities and to enjoy live entertainment. They benefited from this right in a venue in which they could freely discuss political matters with people of similar political beliefs.

Agreeing with HMRC, the FTT also found that the membership subscription was in return for a single supply, which comprised indivisible elements that it would be artificial to split. The question was therefore whether all the services that were part of that single supply were primarily referable to the club's political aims.

The FTT found that the emphasis of the club was social rather than political. It pointed, in particular, to the very few references to political matters in the minutes of the club's AGMs. The membership fee therefore did not fall within the scope of the exemption.

Finally, the club wished to rely on a legitimate expectation arising from extra-statutory concession 3.35, which allowed a non-profit club to divide up a single composite supply and to be taxed it as if it were a bundle of separate supplies. As this was clearly contrary to the Principal VAT Directive, the FTT found that it did not have jurisdiction to hear such a claim.

Comments - The FTT confirmed that a club with a stated political object may not always benefit from the exemption. The FTT had no jurisdiction and it recommended a claim for judicial review.

Shanklin Conservative and Unionist Club v HMRC TC4923

BBC - Exempt supplies of education?

Summary - The Court of Appeal found that supplies by the BBC to the Open University were exempt supplies of education.

The appeal concerned a repayment claim of approximately £21m in relation to supplies of television and radio programmes by the BBC to the OU and relating to the OU's courses. The issue was whether the supply by the BBC had fallen within the education exemption (Sch 9 Group 6 item 4 VATA 1994).

During the entirety of the relevant period, the UK had failed to implement the Sixth Council Directive 77/388/EEC article 13A correctly, in that it only exempted supplies 'closely related' to education if they were made by the same person who supplied that education. Article 13A had, however, had direct effect in the UK.

HMRC had always accepted that the OU had the educational aim required by article 13A(1)(i); and that the services supplied by the BBC to the OU during the relevant period were closely related to the university education provided by the OU. The issues were whether, for the purposes of article 13A(1)(i), during the relevant period: (1) the BBC had been a 'body governed by public law'; and, if so, whether (2) it had had the requisite educational aim. If it did not satisfy both these conditions, nevertheless the issue was whether: (3) the BBC was 'defined' by the UK as having 'similar objects'; or, if it was not so defined, whether it could still claim the direct benefit of the exemption.

Decision:

The Court of Appeal referred to 'the relevant and well established legal principle' endorsed by the CJEU in *Saudaçor* (Case C-174/14). This said that a person which, not being part of the public administration, independently performs acts falling within the powers of the public authority cannot be classified as a body governed by public law. The court found that the fact that the Secretary of State, the Crown and Parliament may separately or together have been able to exercise a decisive influence over the BBC, being able to close it down by depriving it of finance or revoking its licence, was not determinative. What was critical was the independence of the BBC, so long as it remained in existence, in the production and content of its broadcasting and control over the deployment of its staff. The BBC was therefore not a body governed by public law.

In relation to (3), 'similar objects', the court noted that the essence of article 13A(1)(i) was the imparting of knowledge, information and instruction with a view to educating and training the recipient and that there was no requirement for a two-way teacher/student exchange. The BBC provided the whole framework of facilities, teaching materials, technical resources, educational policy and organisational infrastructure to deliver its distance learning direct to children and young people and those seeking vocational training or retraining. The supply of education was therefore part of its objects.

The court did not reach a conclusion on the question of whether the UK had defined the BBC as having 'similar objects', as this was not necessary to decide the appeal.

Comments - The Court of Appeal stressed that the object of the education and training exemption was to increase access to education by avoiding the increased costs that would result if it was subject to VAT. To exclude the BBC from the exemption would therefore be both contrary to the objective of the Sixth Directive and contrary to the principle of fiscal neutrality.

HMRC v The Open University EWCA Civ 114

Exceptions and Exemptions – VAT registration (Lecture B950 -14.04 Minutes)

Background

Pete the plumber has traded as a sole trader for seven years and always kept below the VAT registration threshold. However, his total sales for the 12-month period ending 30 April 2015 were £85,000, exceeding the registration threshold of £82,000 which applied at the time. Here are a few tips about identifying the effective date of registration (EDR) of a business:

- The registration test is carried out on a rolling 12-month basis – and a business has a liability to be registered when it has exceeded the threshold at the end of any historic 12-month period. The EDR is the first day of the second month after the limit has been exceeded.

  Example – Pete's EDR will be 1 June 2015 ie he gets an extra month of VAT free sales after he has exceeded the limit.

- There is a second registration test, namely to consider if taxable sales in the next 30 days will exceed the threshold – if so, then the registration date is the beginning of the 30 day period ie so that VAT will be captured on the 'expected' sales.

  Example – Cliff is not VAT registered and secured a deal on 5 March to sell 100 computers for £1,000 each to a major UK retailer.

  The computers will be sold on 1 April 2015 and invoiced on the same day ie creating a tax point when the invoice is raised. The expected sales of £100,000 in the next 30 days mean that Cliff will need to register on 5 March.

  Note - it would probably make sense for Cliff to register on a voluntary basis anyway because his retailer client will almost certainly be able to reclaim input tax.

- Don't forget that 'exempt' and 'outside the scope' sales are ignored as far as the threshold is concerned, which is particularly relevant for a service business with overseas business customers.

  Example – John is a sole trader accountant with the following sources of annual income: work for UK clients (£50,000); work for French based businesses (£40,000).

In this situation, John's taxable sales are £50,000 and therefore well below the threshold. The income from French customers is outside the scope of UK VAT under the general B2B (business to business) rule ie the place of supply is France.

Exemption and exception from registration

What is the difference between gaining 'exemption' from registration and an 'exception'? The two words sound quite similar but they apply in very different situations.

Exemption and exceptions to being VAT registered

- ***Exemption*** – a business has exceeded the registration threshold but most/all of its sales are zero-rated, so VAT returns submitted by the taxpayer when he is registered will be repayment ie input tax will exceed output tax. So the business can write to HMRC with an explanation of the facts, and hopefully obtain an agreement that no registration is needed (HMRC Notice 700/1, para 3.11)
- ***Exception*** – this is more important for most businesses and applies when the business has exceeded the threshold but can persuade HMRC that in the next 12 months after the limit has been exceeded taxable sales will not exceed the deregistration threshold ie £80,000 (for period 1 April 2015 to 31 March 2016). HMRC need to be persuaded in writing that the reason the business exceeded the limit in the first place was due to a one-off job or fee that will not be repeated. For example, if Pete the plumber had a one-off good job to supply and fit a new bathroom suite for £30,000 in the mansion of a wealthy footballer – and his normal work is to supply and fit £300 bathroom suites in small houses, this would be a good example of when an exception might be relevant (HMRC Notice 700/1, para 3.7).

At this stage in the story, it will be useful to know the type of customers that use Pete's business ie the mixture of commercial/non-commercial clients – and whether the commercial clients are VAT registered and can claim input tax. The reason I say this is because if all or most of his clients can claim input tax, it might be worth applying to register Pete before 1 June 2013 and select a date as far back as February 2011. This is because a business has the option to voluntarily register on a retrospective basis if it wishes to do so, the time cap being four years from the application date. Pete can then issue VAT only invoices to these customers for the last four years (and they should be happy to pay it), allowing him to claim input tax on all of his material purchases and other costs. A happy VAT ending so to speak.

Geoffrey Lane (TC4815) – were HMRC correct to refuse an 'exception' to being VAT registered?

The taxpayer was a consultant gynaecologist with mainly exempt income as a medical professional but he also had taxable income in relation to giving reports on claims in relation to legal matters – working for legal firms. His taxable income exceeded the registration threshold for the first time in October 2013. He wrote to HMRC requesting an exception to being registered on the basis that his expected income for the 12-month period beginning 1 December 2013 would be £65,000 ie less than the deregistration threshold. He was due to retire in August 2014 – hence the reduced fees.

In effect, the taxpayer scored an own goal because HMRC will refuse an exception if the reduced fees are because of a shorter trading period than 12 months ie Mr Lane's projected income of £65,000 was based on 9 months of trading – as per VATA1994, Sch 1, para 4(2).

The taxpayer's appeal in September 2014 confirmed that actual turnover to August 2014 was £61,605, but additional turnover was projected for September to November of £10,500 ie a total of £72,105 – which was still below the deregistration threshold. But the existence of sales in September to November contradicted Mr Lane's earlier claim of retirement at the end of August 2014 and HMRC also felt that expected sales of £65,000 at the time of requesting an exception was too close to the deregistration threshold of £77,000 ie it could not justify an exception being given. To give HMRC's key conclusion (para 25):

> 'It is the lack of long term precision, and the necessary limitations in having that precision, that suggest that the Commissioners could not reasonably have been satisfied at the material time, certainly not in projection over a whole year to come.'

The key issue in a case of this nature is whether HMRC's action in refusing to grant an exception was reasonable – and the tribunal felt it was (para 65):

> "The Tribunal can only interfere with the Commissioners' decision if it is shown that the decision is one which no reasonable body of Commissioner could reach. We are of the view that the Commissioners' decision was reasonably reached, and there is no cause for the Tribunal to interfere."

The appeal was dismissed.

Note - the strange issue with this case is that all of Mr Lane's customers were legal firms who were able to claim input tax on his fees. So it would be expected that Mr Lane would be happy to register for VAT in order to reduce his own costs by claiming input tax. But if he had become registered, he would have been partially exempt which is not a welcome proposition for most SMEs – so he probably wanted to keep out of the VAT club for as long as possible. As a separate point, advisers should be clear that when applying for an exception, the relevant issue is the **known facts at the time of the request** ie when the limit was exceeded and not the actual turnover or future events that occur after this time.

Final tip

If a business forgets to apply for an exception within 30 days of exceeding the registration threshold, and just carries on not being VAT registered, it is possible to apply for an exception on a retrospective basis but the challenge is to highlight the known circumstances of the business at the time the limit was registration exceeded ie that the business knew it would have taxable sales in the following 12 months that were less than the deregistration threshold.

Contributed by Neil Warren