

Personal tax round up (Lecture P1306 – 22.01 minutes)

The Spring Statement

There was some uncertainty as to what was actually going to happen at the time of the Spring Statement but some anticipation that we might be getting some significant announcements. In the end it was something and nothing (as is often the case!).

The Chancellor waved a blue booklet entitled 'The Tax Plan' which turned out to contain nothing of any substance. There were some announcements, mostly relating to personal tax. There were also some promises of changes to be brought in from the Autumn Budget with some details of the direction of travel for those changes (but which it is stressed are still subject to change).

The overall aim is to reduce taxes and promote prosperity at a time when unprecedented (at least in recent years) rises in the cost of living are threatening those working class voters that the current Government cannot afford to alienate.

The Government is investing £161m over the next five years to increase compliance and debt management resource in HMRC. This will fund additional staff primarily. There is also an addition of £510m to increase the capacity of DWP to prevent and detect fraud and error in the benefits system and £12m to help claimants keep tax credit claims accurate through health-check calls, compliance activity and use of SMS nudges.

Income tax

It has been announced that the basic rate of income tax will be reduced to 19% with effect from April 2024. This will apply to the basic rate of non-savings, non-dividend income for taxpayers in England, Wales and Northern Ireland as well as the savings basic rate (which applies to savings income for taxpayers across the UK) and the default basic rate for trustees and non-residents.

A three-year transition period will apply to maintain the rate of relief on Gift Aid payments to 20% to reduce the impact on charities of this reduction which will impact their income where the gift aid payments they receive are significant.

Health and Social Care Levy

The Health and Social Care Levy which is coming in from 6 April 2022 is not being changed. There will be a rise in all rates of Class 1 and 4 National Insurance Contributions rates and a rise in the rates of dividend tax. This has been announced and discussed at length already. This is being introduced to fund the NHS and Social Care, as the name suggests.

National Insurance Contributions

The Primary Threshold (PT) for Class 1 NICs and the Lower Profits Limit (LPL) for Class 4 NICs will be aligned with the income tax personal allowance at £12,570 from July 2022. The intention is to keep those thresholds aligned, although the personal allowance is currently frozen until 5 April 2026. This change will apply from 6 July 2022 for employees (as the beginning of month 4).

For the self-employed, there will be a pro-rated Lower Profits Limit for the 2022/23 tax year being £11,908 (as 13 weeks @ £9,880 and 39 weeks @ £12,570). This will go up to the full £12,570 from 6 April 2023.

From April 2022, self-employed individuals between the small profits threshold (SPT) and the Lower Profits Limit will be able to build up NI credits without having to pay any Class 2 NICs.

There are no changes to the secondary threshold for employers.

		2021/22	2022/23		2023/24
			6 April – 5 July	6 July – 5 April	
PT	Weekly	£184	£190	£242	£242
	Monthly	£797	£823	£1,048	£1,048
	Annual	£9,568	£9,880	£12,570	£12,570
LPL		£9,568		£11,908	£12,570
Class 2		£3.05			

Example 1

For an individual who is earning £20,000 per year, the figures (ignoring the split year, so treating the income as arising in 2023/24):

Tax payable would be £20,000 less £12,570 x 20% = £1,486

Class 1 NICs payable would be £20,000 less £12,570 x 13.25% = £984.48

The net take-home pay would be £17,529.52. Without an increase in the NI threshold, the Class 1 NICs would have been £20,000 less £9,880 x 13.25% = £1,340.90 so take-home pay would have been £17,173.10. The individual is £356.42 better off.

If the limit had remained the same, but the HSL had been removed, then the Class 1 NICs would have been £1,214.40 and the take-home pay would have been £17,299.60. So this individual is better off with the rise in the threshold.

Example 2

For an individual who is earning £50,000 per year, the figures (ignoring the split year, so treating the income as arising in 2023/24):

Tax payable would be £50,000 less £12,570 x 20% = £7,486.

Class 1 NICs payable would be £50,000 less £12,570 x 13.25% = £4,959.48

The net take-home pay would be £37,554.52. Without an increase in the NI threshold, the Class 1 NICs would have been £50,000 less £9,880 x 13.25% = £5,416.20 so take-home pay would have been £37,097.80. The individual is £456.72 better off.

If the limit had remained the same, but the HSL had been removed, then the Class 1 NICs would have been £4,814.40 and the take-home pay would have been £37,699.60. So this individual is worse off with the rise in the threshold.

Company director and shareholder

For an individual who is a company director, taking a salary up to the NI threshold and then taking the balance out as dividends, what is their position?

Let us take an example of a company with profits of £50,000 before deduction of salary.

	£
Profit	50,000.00
Less salary	<u>(12,570.00)</u>
Less Ers NI	<u>(525.70)</u>
Net profit	36,904.30
Corporation tax	<u>(7,011.81)</u>
Net reserves	<u>£29,892.49</u>

If this is all distributed

2,000 x 0%	Nil
27,892.49 x 8.75%	2,440.59

Net take-home pay for the individual would be £40,021.90

Without the Employers National Insurance (ie if the employment allowance was available), the net take-home pay would be £40,410.

Without the increase in NI thresholds, the take-home pay would have been £39,621.35. If the threshold had been left as it was but the HSL removed, the take-home pay would have been £40,009.26. So the individual is very slightly better off by having an increase in the threshold if no employers allowance is available or worse off if it is.

Employment allowance

The Employment Allowance is increased to £5,000 per year for eligible employers to take effect from April 2022. There are no changes to the conditions for this to be available.

Share schemes

A review of EMI was launched in 2020 but the Government have concluded that the current scheme remains effective and appropriately targeted. However, they are looking at the Company Share Option Plan to see if this could be reformed or expanded to make it more useful in recruiting and retaining employees.

Capital allowances

It is acknowledged that there may be scope for increasing the reliefs available for capital expenditure. The following are options which are being considered:

- Increase the permanent level of the Annual Investment Allowance to £500,000;
- Increase writing down allowance from 18% to 20% for main rate expenditure and from 6% to 8% for special rate pools;
- Introduce a first year allowance for main and special rate pools – the given figure is 40% and 13% respectively;
- Introduce an additional first year allowance to bring the actual relief to more than 100% (as has been done with the superdeduction);
- Introduce full expensing to allow businesses to write off the costs of investment in one go. This one is highly unlikely due to cost!

Specific proposals will be announced at the time of the Autumn Budget 2022:

Research and development tax relief reform

At the time of the Autumn 2021 Budget, it was announced that there would be reform of R&D tax reliefs. This included the expansion of the types of costs which would qualify for relief but also a refocussing of support to R&D carried on in the UK only. This has been subject to extensive discussion with HMRC as there were concerns about the impact of the latter proposal.

As regards the costs, it is now confirmed that all cloud computing costs, including storage, will qualify for relief. They will also amend legislation so that pure mathematics is a qualifying cost.

As regards the refocussing, it is now recognised that there are some cases where it is necessary for R&D to take place overseas. Overseas activities will therefore continue to qualify where there are:

- Material factors such as geography, environment, population or other conditions that are not present in the UK and are required for the research;
- Regulatory or other legal requirements that activities must take place outside the UK.

These changes will apply from April 2023.

In addition, they are considering whether to increase the RDEC rate to boost investment in the UK but again this has yet to be decided.

Business rates

The business rates multiplier will be frozen in 2022/23. There will also be a new temporary 50% Business Rates Relief for eligible retail, hospitality and leisure businesses.

In the Budget at the end of 2021, the Government announced the introduction of targeted business rate exemptions for eligible plant and machinery used in onsite renewable energy generation and storage and a 100% relief for eligible low-carbon heat networks with their own rates bill to support the decarbonisation of non-domestic buildings. This was due to take effect from 1 April 2023 but is being brought forward to 1 April 2022. It will last until 31 March 2035.

VAT on energy saving material

There is an extension of VAT relief on the installation of energy saving materials. The Government is to include additional technologies (including wind and water turbines) and remove complex eligibility conditions to allow the relief to be extended. There will also be the introduction of a time-limited zero rate for the installation of such materials. These changes will take effect from April 2022 although they will not be available in Northern Ireland due to the Brexit Northern Ireland Protocol.

Fuel duty

There is to be a temporary 12-month cut in the fuel duty on petrol and diesel of 5p per litre. This has effect from 6pm on 23 March 2022. It is said to be worth £100 over than 12-month period for the average car driver, £200 to the average van driver and £1,500 to the average haulier.

Contributed by Ros Martin

Matalan man

Summary – Following the Supreme Court’s decision in ‘Tooth’, a discovery was held not to be stale, making the assessment valid.

John Hargreaves was Matalan plc’s executive chairman. On 11 March 2000, he started to spend time in Monaco. Initially living in a hotel suite but from 1 September 2000, he obtained the lease of an apartment in Monaco.

On 15 March 2000, he submitted Form P85 to HMRC indicating that had left the UK to live in Monaco and that he expected to spend “no more than two months” per annum in the UK.

However, he continued to work as Matalan’s executive chairman and spent a lot of time in the UK. Further, he owned a property in the UK that was available for his use.

In May 2000 he sold shares in Matalan for £231 million. His 2000/01 tax return was filed with:

- no CGT supplementary pages and without these, HMRC had no knowledge of the £80 million gain that arose;
- a white space note stating that he was non-UK resident

John Hargreaves claimed this was consistent with HMRC’s guidance where persons claiming not to be resident or ordinarily resident in the UK did not need to fill in these pages. He also stated that he had calculated his liability to income tax without regard to £5.6million of investment and employment income. He considered these items not to be liable to income tax because he was not resident in the UK.

Finally, in January 2007, HMRC raised a discovery assessment to collect £84million of additional tax.

John Hargreaves appealed to the First Tier Tribunal, initially on two grounds:

1. In 2000/01, he had been neither UK resident nor ordinarily resident and so was not liable to income or capital gains tax;
2. HMRC had not been entitled to make the discovery assessment made and so it was invalid.

Prior to the hearing, John Hargreaves accepted that he was in fact UK resident in 2000/01.

The First Tier Tribunal allowed the appeal on the grounds that the discovery on which the assessment was based had become “stale” as a consequence of HMRC’s delay in making the assessment. Discussions with John Hargreaves were opened in 2003 following the publication of a newspaper article, but it took HMRC until 2007 to raise the assessment.

However, in case the Tribunal was wrong, it also determined that, had the assessment not been stale, John Hargreaves’ appeal would have failed. The return had not been made in accordance with the practice prevailing at the time, nor had HMRC been given enough information to be aware of the insufficiency of tax prior to the discovery.

HMRC appealed the decision that the assessment had become stale, while John Hargreaves appealed arguing that if the discovery was not stale, the First Tier Tribunal had been wrong in their subsequent determinations.

Decision

Both parties agreed that HMRC’s appeal must be allowed given the judgment of the Supreme Court in *HMRC v Tooth* [2021] 3 All ER 711 which was handed down after the First Tier Tribunal’s Decision.

The Upper Tribunal agreed with the First Tier Tribunal that even if a hypothetical officer could have realised that John Hargreaves was UK resident, with no CGT pages submitted that officer could not have been aware of an insufficiency in John Hargreaves’ return,

John Hargreaves v HMRC [2022] UKUT 00034 (TCC)

Gift of shares to charity

Summary – When valuing gifted shares the taxpayers had failed to take into account relevant information that was available to the public. HMRC’s valuation of shares was held to reflect the appropriate valuation.

Five individuals (Alfred and Amanda Dwan, Malcolm Hunnisett, Andrew Openshaw-Blower and Richard Parkinson) made gifts of shares in Taskcatch plc to charity.

The gifting dates were 31 March 2003 and 5/6 October 2004 and each claimed tax relief on the value of the gifted shares at these dates. The taxpayers argued that the value used should be based on information publicly available at that time and their expert valuer stated that they would not undertake “any other type of valuation, verification or cross check”.

Their valuation was therefore based on four very small trades registered on the AIM market and the values given when new shares were issued.

These values were:

- 32.5p per share as at 31 March 2003 (Mr Dwan);
- 40p as at 5 October 2004 (Mr Dwan and Mrs Dwan); and
- 39.75p on 6 October 2004 (Mr Hunnisett, Mr Openshaw-Blower and Mr Parkinson).

HMRC argued that these values overstated the gift relief claims. Their expert valuer was instructed to “assess the market value by taking into account the documents to which a prudent prospective purchaser of the gifted shares, who made appropriate enquiries, would have had access to, using the most appropriate valuation methods to determine the price that those shares would have reasonably been expected to fetch on a sale in the open market.” As a result, they considered other factors, including the much lower value given in other company documents such as when acquiring another company in an arm’s length transaction at 7p per share.

The individuals appealed to the First Tier Tribunal.

Decision

The First tier Tribunal noted that a Joint Report was prepared that set out the areas of agreement and disagreements between the parties, in relation to information readily available in the public domain, details of which are given in the case report. It was agreed to disregard internal unpublished Taskcatch Plc financial information, confidential documents produced by Taskcatch Plc’s professional advisors and private share sales not reported on a regulated market and not in the public domain.

The report stated that the parties agreed that where shares were thinly traded, the market price may not accurately reflect open market value. However in arriving at their values the individuals’ expert valuer did not take into account all of the publicly announced transactions but focused on the most recent AIM trades. The valuer was unable to explain why they had placed significant weight on what were small transactions rather than another transaction which took place at the same time, namely the acquisition of Skylark by the issue of 15,000,000 shares (49.4% of Taskcatch Plc’s share capital as at 31 March 2003) at price of 7p per share.

The First Tier Tribunal concluded that a prudent purchaser would inform themselves of the relevant facts, which was not the case here. The Tribunal found that the shares values should be taken as the midpoint of the upper and lower limits calculated by the HMRC expert. The market value of the Taskcatch Plc shares was held to be 8.85p per share at 31 March 2003 and 6.25p per share in October 2004.

Alfred Michael Dwan and others v HMRC (TC08388/V)

NOTE: Since 15 December 2009, there is an anti-avoidance provision which means that if the donor has held shares for less than 4 years (which was true in this case as they had only incorporated the company in early 2003) then you use the acquisition cost rather than market value for the value of the gift where it is part of a scheme where the main purpose is to obtain the relief. Although this is not the purpose of the decision in this case it could well apply in other cases.

Properties not eligible for PPR

Summary – Buying and selling four properties within five years did not constitute trading activity. However the profits were liable to capital gains tax with no PPR relief available.

In 2017, having discovered that Mark Campbell had disposed of a property, HMRC wrote to Mark Campbell asking him to submit a Self Assessment tax return for 2015/16.

He informed HMRC that he had disposed of a bungalow, the only property that he owned whilst living at his parents' home as his father's carer, and that this was Job-Related Accommodation.

In fact, Mark Campbell had bought and sold four properties over five years. Each property needed to be refurbished and was left empty while this work was undertaken. All four properties were then sold on at a profit.

Mark Campbell argued that he had intended to live in each property as his main residence but gave various reasons as to why he had not done so, including the fact that he was his father's carer and needed to stay in his father's home.

HMRC issued a closure notice for 2015/16 for £131,000 and two discovery assessments for earlier years of £100,000 on the basis the transactions were a trading activity. If not trading, the transactions were subject to CGT, with no principal private residence relief being available.

Decision

The First Tier Tribunal acknowledged that Mark Campbell had been 'very active' in the property market and no evidence had been put forward to support his argument that he intended to live in any of the four properties that he had bought.

However, the Tribunal concluded that he was not a property developer. The property transactions were not linked to an existing trade, and had not occurred over a long period. The Tribunal stated:

“Having considered all of the evidence, cumulatively, while the appellant clearly generated profits from the sale of the properties, and while the length of ownership for all but the very first purchase was relatively short, I find that this does not point towards trading.”

These were a capital rather than trading transactions that fell within the CGT regime. The Tribunal concluded that:

- living at home with his parents due to his father's illness did not explain his claim that he was living in job-related accommodation.
- the evidence provided did not indicate 'any degree of permanence, continuity or expectation of continuity in relation to any of the properties'.

Mark Campbell had not intended to live in any of the properties as his main residence, so the gains were taxable in full.

HMRC's penalties for deliberate behaviour totalling some £40,000 were upheld as Mark Campbell had failed to declare the property sales and should have known that his transactions had tax implications.

His appeal was dismissed.

Mark Campbell v HMRC (TC08398)

Artificially large UK gain

Summary – HMRC had been correct to calculate the gain on the sale of an overseas asset using the rules contained within legislation, despite this resulting in an artificially large UK gain due to exchange rate movements.

Howard and Monique Rawlings were both UK tax resident taxpayers. In August 2006, they jointly bought a property in Switzerland for CHF 563,000. This was partly funded by a Swiss franc mortgage secured on the property, which was let as a holiday let.

In December 2016, the property was sold for CHF 730,000 with the Rawlings each declaring 50% of a total capital gain calculated as £39,433.

HMRC opened an in-time enquiry into Howard Rawlings' return and sought further information as to the basis on which the capital gain had been calculated.

HMRC considered all costs deducted in connection with the mortgages were disallowed and recalculated the gain as £267,000 which was to be allocated 50:50 between the couple.

HMRC's calculation translated the sales proceeds and related fees into sterling using the exchange rate in 2016 and the costs that were deducted in arriving at the gain using the exchange applicable in 2006, when the property was bought.

HMRC issued a closure notice in respect of Howard Rawlings share of the gain and a discovery assessment in respect of Monique' share. Further, HMRC issued carelessness penalties against each of the Rawlings based on 15% of the tax charged, having given full mitigation for the penalty.

The Rawlings argued that the economic gain calculated by HMRC was artificially increased by the currency rate fluctuations affecting their mortgage repayments.

Decision

The First Tier Tribunal confirmed that capital gains are calculated in the "mechanistic way" adopted by HMRC and consequently found that the gain had been correctly calculated.

The Tribunal stated that when the Rawlings bought their Swiss property, they did not share ownership of it with the bank who provided the mortgage, stating:

"The basis on which the purchase was funded is not taken into account when determining the difference between disposal value and acquisition cost. The fact that their mortgage was a foreign currency mortgage cannot influence the underlying premise that funding decisions carry no consequence in terms of the capital gains tax calculation."

Although sympathetic to the Rawlings position, the Tribunal found that tax is collected by reference to the legislative provisions, even where" the results in some situations appear absurd."

The appeal was dismissed.

NOTE: In Recommendation 11 of the OTS's CGT review (2nd report), the OTS stated that the government should consider whether gains or losses on foreign assets should be calculated in the relevant foreign currency and then converted into sterling. This would bring the position into line with the treatment with foreign currency bank accounts where taxpayers are not taxed on currency gains.

Howard and Monique Rawlings v HMRC (TC08384)

<https://www.gov.uk/government/publications/ots-capital-gains-tax-review-simplifying-practical-technical-and-administrative-issues>

Residential, not mixed use property

Summary – Grounds in these two cases were residential property, liable to the higher SDLT residential rates.

The Court of Appeal considered the decision in two Upper Tribunal cases: Hyman and Goodfellow. As a brief reminder, in the:

- Hyman case, a house was bought along with 3.5 acres of land that included a run-down barn and a meadow which the Hyman's argued were not residential property;
- Goodfellow case, a house and 4.5 acres of land was bought with a garage office, stables and paddocks that the Goodfellow's argued were not residential property.

S.116 FA 2003 states that land forming part of the gardens or grounds of a property is residential property, with SDLT payable at residential rates.

In both the Hyman and Goodfellow cases, the taxpayers argued that the land described above did not form part of the garden or grounds, as it was not needed for the reasonable enjoyment of the dwelling. Consequently, the purchase should be treated as mixed-use property taxable at the lower non-residential rates of SDLT.

The taxpayers relied on HMRC guidance, statements of practice relating to stamp duty relief in disadvantaged areas, produced at the time legislation was introduced. This limited the land that should be viewed as residential property for SDLT purposes, similar to the capital gains tax test for land when considering principal private residence relief.

Both the First Tier and Upper Tribunals disagreed and the cases have now been heard jointly by the Court of Appeal.

Decision

The Court of Appeal turned to the Supreme Court's decision in *R (on the application of O) v Secretary of State for the Home Department [2022] UKSC 3*. This decision found that taxpayers must rely on statute and went on to find that other documents can assist with understanding but played only a secondary role when interpreting the law.

The Court of Appeal pointed out that the guidance being relied upon related to Stamp Duty, not Stamp Duty Land Tax. There was no reason why Parliament would have intended that this guidance also be applied to Stamp Duty Land Tax. The words in the SDLT legislation were 'clear and unambiguous'

The Court of Appeal stated that the permitted gardens and grounds for CGT purposes imposed a limit land qualifying for PPR relief, while s.116 FA 2003 had a different purpose. It sought to classify property as residential or non-residential. Unfortunately, including significant amounts of land did not make the property mixed use.

The appeals were dismissed.

David and Sally Hyman and Craig and Julie Goodfellow v HMRC [2022] EWCA Civ 185

NOTE: We are waiting to hear the outcome of a consultation on the definition of residential/non-residential which could change things going forward.