

Personal tax round up

(Lecture P1111 – 19.04 minutes)

Draft Scottish Budget 2019/20

The draft Scottish Budget 2019/20 includes the following highlights:

1. The income tax higher rate threshold will remain frozen at £43,430 so widening the gap with the UK higher rate threshold, which will be £50,000 in 2019/20;
2. The additional dwelling supplement for land and buildings transaction tax will rise from 3% to 4% from 25 January 2019;
3. The LBTT non-residential transaction rates and thresholds will change with effect from 25 January 2019; the lower rate threshold will be reduced from £350,000 to £250,000 and at the same time, the rate will be reduced from 3% to 1%. The upper rate will increase from 4.5% to 5%.

<u>Residential</u>		<u>Non-residential *</u>		<u>Non-residential leases</u>	
Purchase price	Rate	Purchase price	Rate	NPV of rent payable	Rate
Up to £145,000	0%	Up to £150,000	0%	Up to £150,000	0%
£145,001 to £250,000	2%	£150,001 to £250,000	1%	Over £150,000	1%
£250,001 to £325,000	5%	Over £250,000	5%		
£325,001 to £750,000	10%				
Over £750,000	12%				

The Budget remains in draft until it is approved by the Scottish Parliament, which based on previous years is likely to be in February 2019.

news.gov.scot/news/tax-decisions-to-protect-public-services

Diving earnings

Summary – Taxpayer's diving activities were treated as carrying on a trade and so could not constitute employment income for UK income tax purposes

Mr Fowler was a South African resident who worked as a diver. In 2011/12 and 2012/13, he worked as a diver in the UK continental shelf waters of the North Sea. He had no permanent establishment in the UK and was employed under an employment contract.

HMRC said the earnings were income from employment within Art 14 of the South Africa/UK double tax treaty and was therefore chargeable to UK income tax.

However, s15 ITTOIA 2005 deems divers who work on the continental shelf to be self-employed and so Mr Fowler believed that his income was trading profits covered within Art 7 of the UK/South Africa double tax treaty, making his earnings exempt from UK income tax because he had no permanent establishment in the UK

The First Tier Tribunal found in favour of Mr Fowler but the Upper Tribunal overturned the decision. Mr Fowler appealed to the Court of Appeal.

Decision

The Court of Appeal found that the effect of s15 ITTOIA 2005 was that, for all income tax purposes, including any double tax treaty, the taxpayer was treated as carrying on a trade. The fact that the taxpayer's earnings were from employment activities should be ignored and so did not fall within Art 14 of the treaty.

The income was not therefore taxable in the UK as it fell within Art 7 — business profits — meaning that the UK ceded its right to tax that income to South Africa because the taxpayer had no UK 'permanent establishment'.

The taxpayer's appeal was allowed.

Fowler v CRC, Court of Appeal

Adapted from case summary in Taxation (6 December 2018)

Ordinary residence

Summary – The Upper Tribunal found that the taxpayer had been ordinarily resident for the purpose of s26 ITEPA 2003.

Mr Mackay was born and brought up in Australia. He spent the majority of his adult life living and working outside the UK. However, he married in the UK but continued to work abroad.

Mr and Mrs Mackay decided that they wanted their children to be brought up and educated in the UK and they decided that Mrs Mackay would return to the UK with the children and he would continue to work in Hong Kong. They bought a house in Surrey in 1997 and Mrs Mackay and the children moved there in July 1997.

In the period 2000 to 2004, when Mr Mackay was based in Hong Kong and Japan, Mr Mackay came to the UK every 4 to 6 weeks and stayed with his family.

In December 2004, Mr Mackay was posted to the UK and he returned to live with his family. His first role in London only involved spending 15% to 20% of his working days abroad. However his second role, from July 2005 to October 2007, involved 30% to 40% of travelling time abroad. Mr Mackay contended that in January 2005, his expectation had been that he would not be based in the UK for more than three years.

Both parties agreed that Mr Mackay was non- UK domiciled but UK resident in 2005/06, 2006/07 and 2007/08.

Mr Mackay said that as his intention was to continue to work in the UK for no more than three years, this meant that he was not ordinarily resident in the UK. HMRC disagreed. This decision was relevant to the application of s 26 on overseas workday relief, which applies to general earnings for a tax year in which the employee is resident, but not ordinarily resident in the UK.

Decision

Parliament did not enact a statutory definition of ordinary residence but has left it to the tribunals and courts to apply the common law definition of ordinary residence.

The suggestion in the former IR20 booklet that a three-year period was required did not reflect the law. The Upper Tribunal said that there is no “three-year rule”. It was possible to become ordinarily resident in as little as one year. The authorities cited by the First Tier Tribunal clearly indicate that there is no prescribed minimum period by which a taxpayer will become ordinarily resident in the UK. It is a question of fact to be determined in each case.

The Upper Tribunal agreed with the First tier tribunal that the UK was his base both for work and home life. It was to the UK he returned from holidays, from work and from travel. On an ordinary day you would find him at work in the UK or at home in the evening and at weekends. The Upper Tribunal found that the period for which Mr Mackay had intended to stay in the UK had been long enough for it to be regarded as 'settled'. He was ordinarily resident in the UK.

A Mackay v HMRC [2018] UKUT 378

Voluntary Class 3 – too late to pay

Summary – Earnings from employments could be aggregated for class 1 and subsequent entitlement to contribution credit. Failing to receive deficiency notices allowed the taxpayer to pay class 3 voluntary contributions.

On 17 October 2014 Louise Willmott wrote to the Department for Work and Pensions (DWP) about a pension statement she had received. She was concerned that it was much less than she had expected and asked to add some qualifying years to increase it. She was referred by the DWP to HMRC's National Insurance Contributions Office for more information about Class 3 NICs.

HMRC explained that she had fallen below the lower earnings limit in a number of years. They explained that in each tax year a person is required to earn over the lower earnings limit in each week or month to make their earnings count for pension purposes.

Louise Willmott said that she had two employments for the disputed years and that if they had added both earnings together, they would have exceeded the lower limit. HMRC argued that they could not be aggregated.

HMRC also said that she was too late to pay Class 3 voluntary contributions. HMRC claimed to have sent her deficiency notices for the three earlier years but not for the later three and, although it had also issued her forms to obtain a pension forecast, she had failed to follow these up.

Decision

The First-tier Tribunal held that, on the balance of probabilities, Louise Willmott had not received the deficiency notices. She had paid the voluntary contributions for 1994/95 without asking to make payments for the earlier years, suggesting that she was unaware of the deficiency. She had contacted HMRC and so had acted with due care and diligence.

Under the Social Security (Contributions) Regulations SI 2001/1004, regs 13 to 17, earnings from more than one employment could be aggregated. The First Tier Tribunal ruled that her earnings from 1999/2000 to 2001/02 should be amalgamated for the purpose of calculating class 1 National Insurance and her entitlement to contribution credit for those years. For the earlier years, she should be allowed to pay class 3 contributions.

Her appeal was allowed.

Louise Willmott v HMRC (TC06789)

Contributions made after fixed protection

Summary –When cancelling the fixed protection certificate, HMRC had ignored the fact that the payments might have been void in law because they were made by mistake. The Tribunal judge made an order requiring HMRC to reinstate the certificate.

Gary Hymanson had a large main pension scheme funded by annual contributions as well as a number of small schemes into which modest sums were paid monthly.

He applied for fixed protection to cap his lifetime allowance at £1.8m and was advised at that time that he should stop all further pension contributions. He stopped his annual contributions but continued the smaller standing orders. These were later stopped following a review of his financial affairs when he was diagnosed with potential terminal cancer.

HMRC revoked the certificate of fixed protection because the additional pension contributions had been made.

Decision

The First Tier Tribunal concluded that Gary Hymanson would not have continued making the contributions had he understood the tax consequences. The effect of making even the first additional contribution of some £62 would have caused a loss of tax estimated at £50,000. This was a genuine mistake.

The judge said that were the case to proceed to the High Court, it would make an order rescinding the contributions erroneously made. In other words, they would be treated as having never been made.

The taxpayer's appeal was allowed.

Gary Hymanson v HMRC (TC06815)

Sale of properties by pension plan

Summary - The sale of properties with proceeds kept outside of the pension fund was an unauthorised payment.

Allan McCashin was a member and joint trustee of a SIPP, administered by a company called IPS and partly funded by bank borrowing. All of the funds were invested in two commercial properties that were leased to Allan McCashin's business.

He wanted to emigrate to Gibraltar but to do so, he needed to invest net worth of £2 million. To generate these funds, his business sold the two properties owned by the SIPP and remitted the proceeds to his bank. The balance in excess of the mortgage on the properties was used to repay loans provided for investments in Gibraltar.

IPS asked Mr McCashin for the proceeds to be remitted to the SIPP to be used to provide a pension. IPS believed that this unauthorised payment from the fund would result in a tax charge. In July 2009, they reported the sale to HMRC who opened an enquiry.

Allan McCashin claimed that he had moved the funds to a scheme in Gibraltar.

HMRC raised a discovery assessment on the basis that the transfer had been an unauthorised payment and the taxpayer appealed.

Decision

The First Tier Tribunal decided that the discovery assessment had not become stale, concluding that HMRC had acted promptly when alerted to the situation. Allan McCashin had not been cooperative and had caused delays to obtaining information.

The Tribunal judge said:

'Right up until, and in the hearing, the appellant believed that, because he was non-resident, paid tax in Gibraltar and all funds were intended for his retirement, he had no exposure to UK tax. He was wrong.'

The taxpayer's appeal was dismissed and the assessment was confirmed at £452,675 which comprised an unauthorised payment charge of £329,218 and an unauthorised payment surcharge of £123,417.

Allan McCashin v HMRC (TC06776)

Gifts to political parties

Summary – Although s24 IHTA 1984 was incompatible with the European Convention of Human Rights, the Tribunal was not prepared to redraft the provision.

During 2014 and 2015, Arron Banks, as well as the companies that he controlled, had made several large donations to UKIP. Under s94 IHTA 1984, the transfers of value made by the companies controlled by Mr Banks were treated as made by him. The issue was whether the donations were exempt from IHT (s 24 IHTA) as gifts to qualifying political parties?

Under s 24, a qualifying political party is one that obtained at least:

- Two seats at the last election; or
- One seat at the last election and 150,000 votes.

In the 2010 general election, UKIP obtained no seats and so HMRC argued that the exemption did not apply. However, at the time of some of the donations, there were UKIP MPs, but they had been elected at by-elections held after the relevant general election. At the general election, UKIP had secured a greater proportion of the vote than other parties that did succeed in having candidates elected.

The taxpayer appealed accepting that 'on its strict terms', s24 did not apply to him but argued that its application was a breach of his human rights (ECHR art 14 and A1P1) and a breach of EU law. S24 IHTA 1984 amounted to discrimination on the grounds of his political opinion, as his donations were a clear manifestation of his opinion.

Decision

The First Tier Tribunal agreed with Mr Banks stating:

'the concentration in s 24(2) on MPs elected at the previous general election under a first past the post system does not strike a fair balance in the context of the provision of tax relief for the funding of political parties — whatever the advantages and disadvantages of that electoral system for the purposes of representative democracy'

However, the Tribunal dismissed the appeal as making legislation compliant with EU legislation was a matter for Parliament and not them.

Arron Banks v HMRC (TC06768)

IHT automation

The OTS has published its recommendations on administrative issues in relation to IHT saying that too many people have to fill in inheritance tax forms, and the process is complex and old fashioned.

The report highlights the benefits of:

- Designing a short form for the simplest estates;
- Reviewing the requirement for trustees to submit forms when no IHT is due and no reliefs or exemptions are claimed;
- Changing the existing form for lifetime charges and trusts, to include splitting up the form, improving guidance and aligning signature requirements for trustees with other parts of the tax system;
- Simplifying the administration and guidance; and ultimately
- Introducing a fully-integrated digital system for IHT.

<https://www.gov.uk/government/publications/office-of-tax-simplification-inheritance-tax-review>

Discovery had gone stale

Summary – With a discovery made in 2005 but a delay of nearly two and a half years before the assessment was issued, the discovery had lost its quality of newness so the assessment was not valid.

Mr Beagles had filed his 2001/02 return on time. He had entered into certain tax avoidance arrangements, marketed by KPMG, that were designed to create a tax loss without a corresponding taxable amount. The arrangements were essentially the same as those considered by the Court of Appeal in the Astall case that were found to be unsuccessful.

The last date by which HMRC could give notice of intention to enquire into the 2001/02 return was 31 January 2004. In June 2004, realising that they had missed the deadline, HMRC decided to defer taking any action until progress had been made against the other participants in the KPMG scheme, in relation to which enquiries had been opened. Mr Beagle was the only scheme participant for whom HMRC did not raise an enquiry within the statutory time limit for 2001/02.

In August 2005, HMRC wrote to KPMG notifying them that it had received advice from counsel that the scheme did not work and that they intended to challenge the scheme through the courts. The letter identified the cases of Mr Astall and Mr Edwards, who eventually became the appellants in Astall, as potential test cases. The letter also referred to the possibility that a discovery assessment may be issued to Mr Beagles, if the scheme was found not to be successful.

The decision of the Special Commissioner in Astall was released on 14 August 2007. Subsequently, on 15 January 2008, HMRC issued Mr Beagles with a discovery assessment totalling £437,389.60.

Subject to certain exceptions, which the Upper Tribunal said were not relevant in this case, s34 TMA 1970 provides the time limit within which an assessment under s29 TMA 1970 could be made. It states that it may be made at any time not later than five years after the 31st January next following the year of assessment to which it relates. Although within time, Mr Beagle appealed against the assessment arguing that the discovery had become 'stale'.

Decision

The Upper Tribunal noted that by August 2005, HMRC believed that KPMG's scheme did not work and was aware of the insufficiency in Mr Beagles' return. There followed a 'lengthy' delay of nearly two and a half years before the assessment was issued. There was no 'ongoing litigation at the time of the discovery' and the evidence showed that HMRC had 'actively considered the issue of an assessment' before closure notices were issued in January 2007 to the taxpayers involved in Astall but decided against it.

The Upper Tribunal said that the First Tier Tribunal had made an error of law when they found that the discovery had taken place following the decision in Astall. The insufficiency of tax could not 'newly appear' twice. The judge concluded the delay was material; the discovery lost its quality of newness by the time the assessment was issued and it was therefore invalid. The appeal was allowed.

Clive Beagles v HMRC ([2018] UKUT 0380 (TCC))