

## **Business tax round up**

**(Lecture B1156 – 18.06 minutes)**

### **IR35 attack on GSK contractors**

An article in AccountingWeb written by Mark Taylor at Chartergate Legal Services states that HMRC has sent generic, unsigned letters to around 1,500 personal service companies that did work for GlaxoSmithKline last year stating:

“After looking at the information we have for the 2018 to 2019 tax year, our view is that the contract between your PSC and GlaxoSmithKline (GSK) comes under the off-payroll working rules ‘IR35’.”

As Mark Taylor questions in his article, why do HMRC now think some 1500 other personal service companies have fallen foul of the IR35 rules, especially as back in 2011, HMRC failed in their attempt to class a GSK contractor as a deemed employee under the IR35 rules? In Primary Path Limited v HMRC case (TC 01306), the company Primary Path Limited had been set up to provide software development services to the pharmaceutical industry and in this case, GSK was the end client. The Tribunal concluded that the level of control did not go beyond that expected when hiring an independent contractor and in addition, the ability to supply a substitute was inconsistent with a contract of service.

Mark Taylor believes that HMRC are targeting this group of companies by sending a vague but threatening letter and then waiting to see what happens. HMRC are hoping that taxpayers will simply accept these unsubstantiated letters and will collect additional taxes with minimal effort from them.

It is important for the 1500 companies check that they did not fall foul of the IR35 rules, and are able to defend their position should HMRC come knocking by issuing a formal enquiry letter or request for information. Until that time, there is no need to respond to the letters.

*<https://www.accountingweb.co.uk/community/blogs/marktaylor/hmrc-launches-ir35-attack-on-gsk-contractors>*

### **LLPs and film production**

*Summary – The First Tier tribunal had erred in law. Trading loss relief was denied as the LLPs were not considered to be trading with a view to making a profit.*

This appeal concerned three LLPs of the Ingenious Group. Each had a number of members, subscribing 30% to the LLP, with the balance provided by a corporate member. The amount invested was used to produce a film, the production of which was outsourced to a production services company.

Not knowing whether a film will be successful or not, on completion of the film it was valued at its net realisable value, typically giving rise to a loss at that time. If the film proved successful, this loss would be reversed and future profits would be taxable.

Overall there would only be a tax deferral for investors, rather than a tax saving. Crucially, the initial loss was expected to be a trading loss that could be offset against other income. Unsurprisingly, HMRC argued that this was an investment activity and denied the sideways loss relief claims.

In addition to arguing that LLPs were not trading, HMRC challenged in a number of other ways:

- were they carrying on their activities with a view to profit?
- the extent and deductibility of expenses incurred by the partnerships?
- whether the accounts were computed correctly under GAAP?
- whether the expenditure incurred by the LLPs was revenue or capital?

On appeal to the First Tier Tribunal, they concluded that the LLPs were trading, but only to the extent of the 30% contributed by the members. However, they held that the expenditure incurred was capital so trading loss relief was denied.

#### *Decision*

The Upper Tribunal concluded that the key issue was whether this was a trading activity, concluding that it was not. Interestingly, the Upper Tribunal rejected using the badges of trade as they did not believe that these were appropriate to this case. They stated that focussing on the badges of trade 'may have led the First Tier Tribunal into error by obscuring the key significance of the nature or character of the activity undertaken, as opposed to the manner in which it was undertaken.' They focused instead on the facts of several other film cases, taking the view that if a business operates in a commercial way that is common to similar businesses it is likely to be trading, unless the activity as a whole represents a complex tax scheme. The Upper Tribunal commented that when 'account is taken of the reality of the insignificance of the LLPs' ownership rights of the films, what is left is negotiation of and entry into a series of speculative investment in financial assets, and little serious ongoing involvement in the production of the films'.

The Upper Tribunal concluded that the LLPs had acquired and held rights in a potential income stream and so were not trading. With no trading activity, loss relief was denied. The First Tier Tribunal had erred in law.

*Ingenious Games LLP Inside Track Productions LLP Ingenious Film Partners 2 LLP v HMRC*  
[2019] UKUT 0226 (TCC)

## **Plant or premises?**

The First-tier Tribunal has recently considered yet another case on the meaning of plant. In fact, this was a dual appeal from two connected companies: Cheshire Cavity Storage 1 Ltd and EDF Energy (Gas Storage Hole House) Ltd.

The case looked at whether the asset in question is merely or primarily part of the premises within which the business is performed, or whether it is apparatus with which the business activities are carried on i.e. is the asset functioning as plant or as premises? Although in this case the asset was very specific being gas storage facilities the decision is of relevance to businesses that involve storage.

In deciding that the cost of preparing the cavities was not a qualifying cost on plant, the FTT made the following points:

- the gas cavities were central to the appellants' business, but that would not in itself make them plant: premises and plant can both be essential;
- the cavities were not merely fixed to the land, but were clearly a part of it, similar to an underground reservoir;
- that did not rule out the possibility that they were plant: the matter depended on whether the cavities functioned as premises or as plant;
- the function of the cavities was to store gas in such a way that it did not dissipate and that it remained in a suitable condition;
- despite the tribunal's finding that the cavities did perform a plant-like function (equivalent to pumps/compressors, but using natural forces), this was held to be an 'incident of the construction' and not the reason they were constructed in that manner;
- a plant-like function 'does not necessarily make premises plant, in circumstances where the premises also functions as premises. It is a 'matter of degree':
  - the water tower in *Margrett v The Lowestoft Water and Gas Company* (1935) 19 TC 481 was used to store water, but its purpose was to increase pressure;
  - the silo in the case of *Schofield* [1975] STC 353 was used to store grain, but had the purpose of discharging the grain at speed, for the business was one of distribution not storage;
  - here, by contrast, the purpose of the cavities was to store gas, for however short a period, so as to profit from price fluctuations. Storage is a premises-like function and not a plant-like function;
- so, the 'significant and predominant' function of the cavities was the premises-like function of shelter and containment
- an analogy with a cold room did not help because the main function of the cold room was to reduce the temperature of what was stored, whereas altering the temperature of the gas was not a function of the cavity
- the fact that the cavities could be used to store gas at high pressure merely meant that they were very good at performing their premises-like storage function

The FTT went on to consider the restrictions of the items listed as structures, assets and works in CAA 2001, s 22 which are prevented from qualifying for allowances as plant and machinery, unless specified elsewhere in the legislation. In summary, the tribunal concluded that allowances were also prohibited by s 22. In reaching this conclusion, it had to consider whether the cavities were 'in use for the purposes of an undertaking for the extraction, production, processing or distribution of gas' (under list B, item 7(b) at s 22). The tribunal decided that an 'undertaking' in this context meant a task or action, rather than an entity (such as a company or partnership).

In its view, the task or action was to store gas and not to extract, produce, process or distribute it. So this exemption did not help the companies.

In considering whether allowances were prohibited by s 22, the tribunal also gave consideration to the meaning of 'the alteration of land for the purposes only of installing plant or machinery', which would provide an exemption from the statutory restrictions (per item 22 at list C, CAA 2001, s 23 which sets out items unaffected by s 22). There was no disagreement that the land was being altered. However, the tribunal took issue with the conclusion of last year's First-tier Tribunal decision in SSE Generation (TC6618) as to the meaning of 'install'. In this instance, the tribunal held that install carries the implication that something that already exists is put in place. In this case, the leaching and de-brining activities created a cavity suitable for gas storage, but did not install such a cavity. So this exemption, too, was of no help to the appellant companies.

The tribunal supported the long-held HMRC view that the relieving provisions of list C (in s 23) cannot be applied to other assets by analogy (based on function) except in particular circumstances that are made clear in the list. So list C must be seen as complete in its own right, and it is not possible to argue that another asset is saved by list C because it has the same function as one that is specifically included. Thus, because the tribunal determined that the cavities were not in fact storage tanks (which are included at item 28 of list C), it was not possible to argue that the cavities were exempted from statutory restriction by analogy to such tanks.

*Adapted by Joanne Houghton from "Recent FTT definition of plant" in Taxation, 19 August 2019*

*Cheshire Cavity Storage 1 Ltd and EDF Energy (Gas Storage Hoe House) Ltd v HMRC [2019] UKFTT 0498*

## **Capital allowances on a building**

The *Urenco* case involves a specific construction in the nuclear industry business but provides some useful discussion about what is a building for capital allowance purposes.

The buildings formed part of a facility which deconverted the bi-product of a uranium enrichment process (known as Tails) into a product which could be stored more easily. What was in dispute was whether various structures at the site functioned within the trade as plant and qualified for capital allowances rather than being buildings which were the setting within which the trade was carried on. The assets in question operated as safety structures as the product being dealt with, the Tails, was very hazardous.

*Urenco* submitted that although the buildings did not do the deconversion of the Tails they did provide an essential function in the processing of the Tails in much the same way as containers would which had been accepted as being plant.

The FTT noted that the trade was to deconvert Tails and store the end result at the facility and in this respect the buildings were part of the setting in which this trade was carried on. In contrast to *Wangaratta Woollen Mills*, an Australian case, where a dyehouse structure was treated as part of the overall dyeing process, in this situation the process could be carried on without the safety structures being in place. Although the regulatory environment would not allow this to happen the FTT stated that the regulatory environment was not relevant to whether an asset performs a function in the trade.

The FTT went on to state that there had to be some other function performed by the structures in the trade and not just a safety function. Therefore, the only items which were considered to operate as plant were in the kiln and condenser facilities and various plinths in the buildings as these provided necessary support for items of plant and ensured they were in the correct position and height to be used in the processing function. However, the FTT then concluded that these items could not qualify as plant as the structures were buildings within the meaning of CAA 2001, s 21.

Lastly the Tribunal dealt with whether any items were plant by virtue of being within CAA 2001, s 23, specifically items 1 and 4 and item 22. The FTT took the view that the meaning of 'plant or equipment' in the excluded items listed means the expenditure on the cost of these items and not the costs of installing such plant and equipment. If a piece of plant or equipment is incorporated into a building, then the cost of its installation is part of the provision of the building and not the provision of the plant and equipment.

Item 22 of s 23 excludes items which are on the alteration of land for the purpose only of installing plant and machinery and the FTT concluded that this was not the case here as the items in dispute were not solely constructed for the purpose of installing plant and machinery, they were also built to protect operatives, the public and to provide premises to house the equipment.

Therefore none of the items qualified for capital allowances as they were all buildings and not saved by being included within CAA 2001, s 23.

*Urenco Chemplants Ltd and Urenco UK Ltd v HMRC [2019] UKFTT 522*

*Contributed by Joanne Houghton*

## **Rollover relief**

The case of Oriel Developments Ltd related to a discovery assessment but also made important points on rollover relief. Oriel carries on a business of letting and developing business units. Oriel disposed of a piece of land under compulsory purchase and put a provisional rollover relief claim in its tax computation for the year to 31 August 2010. In 2012 the company reinvested all the proceeds of sale into the construction and erection of two industrial workspaces on land that the company already owned. The company claimed rollover relief on compulsory purchase under TCGA 1992, s 247 and understood that this superseded the provisional claim.

The issue in question was whether the reinvestment was applied in acquiring other land where other land is defined as 'the new land' (TCGA 1992, 247(1)(c)).

HMRC raised an enquiry into the company's tax return to 31 August 2010 and concluded this by stating they did not agree that the rollover claim was valid because new land cannot include the cost of buildings or additions to buildings on land that is already owned. HMRC made an amendment to the return in 2015 that was appealed and a statutory review requested. The review period was extended in order to allow the case of HMRC v Benham (Specialist Cars) Ltd [2017] UKUT 389 (TCC) to be decided in the Upper Tribunal. This case was released in October 2017 and determined that an amendment was not appropriate in a case such as this.

Therefore HMRC raised a discovery assessment in May 2018 that was noted as being based on a discovery in May 2018. The FTT found that the discovery assessment was stale because the only discovery in 2018 was that HMRC had adopted the wrong mechanism for dealing with the invalid claim to rollover relief, the information on the rollover claim was the same as it was in 2015.

Although this decision decided the case in favour of Oriel, the FTT went on to look at the rollover relief point. They noted that to describe the construction of buildings on existing land as falling within the phrase 'acquiring...land' would run counter to the general approach in the legislation and to established principles of land law. In the view of the tribunal, the construction of buildings on land already owned enhances the existing interest the owner has in the land they already own, there is not an acquisition of a new interest in the land. The FTT felt that this was supported by TCGA 1992, s 248 which includes within the definition of a dwelling house the land which the house is situated on. Therefore if HMRC had succeeded on the discovery assessment issue they would have succeeded on the rollover point.

*Oriel Developments Ltd v HMRC [2019] UKFTT 503*

*Contributed by Joanne Houghton*

## **Legal proceedings against a borrower**

*Summary – The company was not entitled to input tax recovery on the legal costs as they related to an exempt supply.*

Newmafruit Farms Limited is a fruit farming and packaging business based in Kent. In January 2018, the company submitted to HMRC a Notification of Errors in VAT Returns form in respect of periods 03/15 to 01/17.

The company had lent accumulated profits on a short-term basis to unconnected third parties to earn interest. Subsequently, following legal proceedings, the company was able to partially recover the loan capital but was unable to recover any interest.

Initially, the company had not claimed any input tax relating to the professional services undertaken in connection with those legal proceedings but in February 2018, they submitted a Notification of Errors in VAT Returns form in respect of period 11/17.

HMRC rejected the claim for input tax, on the ground that the company had not shown how the input tax claimed was directly linked to its other taxable supplies.

HMRC's review decision concluded that the claimed input tax was not recoverable because the legal fees incurred were linked to an exempt supply (the making of loans). It concluded also that in any event, the legal fees were not a general overhead of the company's business and were not linked to any taxable supply made by the company.

Newmafruit Farms Limited appealed.

## *Decision*

The First Tier Tribunal agreed with HMRC and concluded that:

“a lender’s costs of bringing legal proceedings against a borrower for breach of a loan agreement is a cost component of the supply of the loan itself.”

This meant that there was a direct and immediate link between the legal fees and an exempt supply, so input tax could not be claimed.

The appeal was dismissed.

*Newmafruit Farms Limited v HMRC (TC07254)*

## **Salary sacrifice for travel and subsistence**

*Summary – The First Tier Tribunal erred in law when concluding that Pertemps Ltd made a supply of services to certain employees but they were correct when concluding that the company was not carrying on any economic activity.*

Pertemps Ltd provides permanent and temporary workers to clients, although in this case we are only concerned with those employees who were working on temporary assignments for Pertemps Ltd’s clients.

These employees were given the choice of being paid a salary, out of which they would have to meet any travel and subsistence expenses, or participating in the Mobile Advantage Plan (MAP) under which they would be paid their travel and subsistence expenses but receive a reduced salary. The amount of the reduction was equal to the amount of the expenses payment plus a fixed amount that was, at different times, 50p or £1 per shift.

The advantage conferred by using the MAP was that the expenses were reimbursed free of tax and national insurance contributions so that, even after the payment of the MAP fixed amount, the employees were better off. Pertemps Ltd also benefitted as it did not pay Class 1 NICs in relation to those employees using the MAP.

HMRC took the view that the MAP involved a taxable supply of services by Pertemps Ltd to its participating employees. The payment for these services was the fixed fee of £1 or 50p and that Pertemps Ltd was liable to account for VAT on those amounts. Accordingly, HMRC assessed Pertemps Ltd for VAT of £715,918 in two assessments covering periods 07/09 to 07/14. There were further assessments standing behind these appeals.

Pertemps Ltd appealed to the First Tier Tribunal who concluded that Pertemps Ltd did supply services to the employees but that the supply was not within the scope of VAT because the operation of the MAP was not an economic activity for VAT purposes and allowed the appeal. The Tribunal also held that, if there had been a supply, it would have been exempt.

HMRC appealed against the First Tier Tribunal’s decision.

## *Decision*

The Upper Tribunal agreed with the First Tier Tribunal that Pertemps Ltd was not carrying on an economic activity when it operated the salary sacrifice scheme. The Upper Tribunal concluded that the economic reality was that Pertemps Ltd offered its employees two methods of being remunerated in its employment contract, each of which had slightly different tax consequences. As a result, Pertemps Ltd agreed to pay slightly different salaries. The Upper Tribunal did not regard that arrangement as showing that there was any service supplied by the employer even where an employee chooses the method that provides a greater weekly or monthly take home amount but a lower salary element.

However, the Upper Tribunal concluded that the First Tier Tribunal had erred in law when it held that Pertemps Ltd provided any service to participating employees and, therefore, there was no supply of services for VAT purposes. The company was merely ensuring that it met the legal requirements for processing pay under PAYE legislation for which ever of the two options the employees selected.

The Upper Tribunal could not see that Pertemps Ltd had supplied anything at all which might be regarded as a service to the employees.

HMRC's appeal was dismissed.

*HMRC v Pertemps Ltd [2019] UKUT 0234 (TCC)*

## **Book or stationery?**

*Summary – The planner sold by the taxpayer was correctly classed as a zero-rated book and so the assessments to tax and penalties should be withdrawn.*

Thorsteinn Gardarsson resides and operates his business from Iceland. He is an Amazon market place trader and began selling his product into the UK on 26 July 2013.

On 19 July 2017, as part of a routine check on what are known as non-established taxable persons, HMRC began an enquiry into his VAT registration status and concluded that the Action Day Planner that he was selling was not a book but was unused stationery falling outside the eligibility to be zero rated and thereby subject to VAT at the standard rate. It was a diary, not a book.

HMRC believed that he should have been VAT registered in the UK from when he started trading and so they issued an assessment for the long first prescribed accounting period 26 July 2013 to 30 June 2017, when he actually registered, for the sum of £158,024.77. A late notification penalty of £33,188.98 and an inaccuracy penalty of £1,915.43 were also issued.

Thorsteinn Gardarsson described the Action Day Planner as a time management tool developed to teach and instruct people time management skills. The first 16 pages of the planner contained text setting out a narrative of the ethos for effective time management. The remainder of the planner was taken up with 52 double page planners. The layout followed the methodology advocated in the first 16 pages with space to set out “tasks to execute” “delegation and teamwork” a column for each day of a week and “goals/projects I am going to work on this week”. Thorsteinn Gardarsson submitted that the planner was a zero rated book and not a standard rated diary.

### *Decision*

The First Tier Tribunal considered that within the ordinary meaning of the word book is any item with the physical characteristic of a book (i.e. as a minimum covers, pages, text and/or illustration) which has as its main function informing/educating or recreational enjoyment.

The Tribunal took the view that the section at the start of the planner was educational and set out both the theory and a guide for the practical application of effective time management and prioritisation skills. They commented that had there been a single example of the weekly page inviting readers to photocopy and complete the template they believed that HMRC would not have even questioned the liability of the planner.

The Tribunal concluded that the main function of the planner was to teach the user how to better or more effectively manage time and that it was correctly classed as a book and should therefore be subject to VAT at the zero-rate. As a consequence the taxpayer was not liable to the assessment raised by HMRC.

The Tribunal went on to consider the issue of registration stating that where a non-established person meets conditions A – D as set out in Schedule 1A VATA 1994, there is a liability to be registered for VAT with no turnover threshold unless, at the request of that person, HMRC consider it fit to exempt that person from the liability to be registered. On that basis, and with no request for exemption from registration, the correct VAT registration date was 26 July 2013.

The Tribunal stated that they have no power to require that HMRC exercise their discretion to exempt the taxpayer from registration. They merely observed that on the basis of the conclusion reached as to the liability of ADP the taxpayer met the requirements for exemption subject to a formal request being made.

They concluded by stating that failure to register as required under Schedule 1A strictly renders the taxpayer liable to a penalty for failure to comply with an obligation specified in Schedule 41 Finance Act 2008. However, the penalty payable is a tax geared penalty and, with no tax due, the penalty in this case was therefore nil.

*Thorsteinn Gardarsson T/A Action Day A Islandi v HMRC (TC07255)*