

Tax update

A round-up of recent issues

7 August 2018

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1. General

1.1 UK/Cyprus double tax treaty

A new UK/Cyprus double tax treaty entered into force on 18 July 2018.

The new treaty replaces the existing one and is applicable from:

- 1 January 2019 in respect of withholding tax paid in both the UK and Cyprus;

- 1 January 2019 in respect of all other taxes in Cyprus;
- 1 April 2019 in respect of UK corporation tax; and
- 6 April 2019 for UK income tax and CGT.

There are also articles regarding mutual agreement procedures and exchange of information and these will apply from 18 July 2018.

www.gov.uk/government/publications/cyprus-tax-treaties

1.2 Follower notices and APNs

The HC has dismissed a judicial review in a lead case for 342 claimants involving follower notices and Accelerated Payment Notices (APNs). The scheme involved was similar to the Huitson case involving the Isle of Man/UK double tax treaty.

The taxpayer, Ms Broomfield, was the lead case for the other 341 claimants. The taxpayers participated in a scheme in which they each set up a trust in the Isle of Man. The taxpayers were the beneficiaries of the trusts and provided services to a partnership of which the trustees of their individual trusts were a partner. The trustees made payments to the taxpayers as beneficiaries and they claimed the payments were exempt from UK tax under the Isle of Man/UK double tax treaty.

A similar scheme was defeated in the case *Huitson v HMRC* [2015] UKFTT 448 (TC) and HMRC issued follower notices and APNs.

The taxpayers disputed the follower notices and APNs on two grounds:

1. They did not agree with the decision in *Huitson*.
2. The follower notices and APNs were invalid as they did not:
 - correctly state the number of days on the APNs for making representations or on the follower notices for taking corrective action;
 - describe the correct corrective action; and
 - two of the claimants contended their follower notices were issued late.

The HC dismissed the arguments on the following basis:

- the decision in *Huitson* was correct and if applied to this case would satisfy the conditions for the follower notice;
- while HMRC accepted that a number of the taxpayers may not have been given the exact timing allowed for making representations and taking corrective action, the HC found this did not make the notices invalid. The judge also commented 'I would not have granted any remedy in relation to any of the follower notices or APNs....None of the claimants has suggested in any of the evidence that they have suffered any injustice'; and
- the follower notices do set out the corrective action to be taken in line with the requirements.

The HC did however agree that two of the claimant's follower notices and APNs were invalid as they were sent to incorrect addresses and therefore issued late.

The judges commented on the complexity of the case that 'The parties recognise that the relevant provisions of the 2014 Act are complex and not necessarily easy to interpret'.

Following the decision, HMRC wrote to the claimants to confirm it would not issue a penalty if the claimants withdraw their arguments and agree in writing not to seek further judicial review.

Broomfield and others v HMRC [2018] EWHC 1966 (Admin)

www.bailii.org/ew/cases/EWHC/Admin/2018/1966.html

1.3 Follower notices and APNs: Eclipse

The HC has dismissed a second judicial review case involving 10 claimants and their follower notices and Accelerated Payment Notices (APNs). The scheme involved was similar to the Eclipse 35 case, involving the claim for tax relief on interest paid on a loan to participate in a partnership.

The taxpayer, Mr Locke, was the lead case for the other 9 claimants. The taxpayers participated in a scheme similar that in the *Eclipse 35* case (*Eclipse Film Partners No. 35 LLP v HMRC* [2015] EWCA (Civ 95)). The scheme involved borrowing a large amount in order to invest in a partnership and interest relief was sought on the interest paid. In this case the taxpayer invested £29,700,000, of which £28,920,692 was borrowed.

The *Eclipse* case failed on the basis it was held the business was not carrying on a trade and the interest relief was therefore not allowable. The taxpayers contended that their case was not the same as the *Eclipse 35* case, as it did not analyse whether or not the purchased share in the partnership arose from the borrowed monies. The HC disagreed and agreed the facts of this case were 'materially' similar to *Eclipse 35* and held the follower and APNs were valid.

Locke v HMRC [2018] EWHC 1967 (Admin)

www.bailii.org/ew/cases/EWHC/Admin/2018/1967.html

1.4 Increase in tax take from the very wealthy

It has been reported that the additional amount of tax that HMRC has collected through investigations in to what The Times calls 'super rich' taxpayers has increased by 29%.

The additional tax collected through such investigations, on top of what these taxpayers already declare on their returns, is stated as £1.2 billion in the 2017/18 tax year.

www.thetimes.co.uk/edition/money/taxman-reaps-an-extra-300-million-from-the-super-rich-dpjgjp329

1.5 HMRC publishes 'warning' on requirement to correct

HMRC has published a note 'urging UK taxpayers to come forward and declare any foreign income or profits on offshore assets before 30 September to avoid higher tax penalties'.

The Requirement To Correct legislation requires those with undeclared UK tax liabilities that involve offshore matters or transfers relating to IT, CGT or IHT for the relevant periods to disclose those to HMRC on or before 30 September 2018.

HMRC notes that 'over 17,000 people have already contacted HMRC to notify the department about tax due from sources of foreign income, such as their holiday homes and overseas properties.'

www.gov.uk/government/news/hmrc-warns-its-time-to-declare-offshore-assets?utm_source=c48ad8c2-65df-47c2-a7de-2975d7ad8426&utm_medium=email&utm_campaign=govuk-notifications&utm_content=immediate

1.6 HMRC late payment interest rate to rise following the Bank of England rate rise

The late payment interest rate will rise to 0.75% in line with the Bank of England rate rise.

The changes will apply from:

- 13 August 2018 for quarterly instalment payments; and
- 21 August 2018 for non-quarterly instalment payments.

www.gov.uk/government/news/hmrc-late-payment-interest-rates-to-be-revised-after-bank-of-england-rate-rise

2. Private client

2.1 Tax avoidance schemes: accelerated payments

On 31 July 2018, HMRC updated its list of those avoidance scheme reference numbers (SRNs) whose users may be issued with an accelerated payment notice (APN).

HMRC confirms that this list is under continual review to ensure that only current and newly disclosed schemes whose users may receive an APN are included. The next update of the list is due to be published in October 2018.

- New scheme reference numbers added are: 33146661, 44135382, 44231922, 52103880, 79590926, 95845964.
- No scheme reference numbers have been removed.

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/729844/Reviewed_Tax_Avoidance_Scheme_Ref_Numbers_July_2018.pdf

3. PAYE and employment

3.1 Spotlight 44 on disguised remuneration schemes affected by the loan charge

HMRC has issued a further Spotlight on disguised remuneration schemes, emphasising the advantages of settling and outlining possible settlement terms, particularly for those on lower incomes.

The Spotlight refers to schemes where, broadly, remuneration has been replaced by a third party loan arrangement. The Spotlight makes the entirely pragmatic point that settling up with HMRC under the published settlement opportunity is likely to be less expensive than any charge to income tax and NIC under the loan charge legislation that has effect in April 2019. This legislation is a game changer for these arrangements because it has the effect of treating such loans as employee remuneration without further ado. The question for the taxpayer is now likely to be, more, which way to pay is cheaper, rather than, does the scheme work? As previously reported at article 3.3 of our Update of 24 July this year, HMRC will agree to instalment plans of up to five years for those on income of up to £50,000. The opportunity for settlement extends to contractor loan schemes.

www.gov.uk/guidance/disguised-remuneration-schemes-affected-by-the-loan-charge-spotlight-44

3.2 Contractor calculator calls CEST tool unreliable following substantial research

The website Contractor Calculator undertook a 14 month investigation into the reliability of HMRC's Check Employment Status for Tax (CEST) tool. Following a Freedom Of Information request, it analysed 24 key employment status cases against the CEST tool. It found that the CEST tool gave the correct answer in only 14 out of the 24 cases.

Following a Freedom Of Information request, Contractor Calculator analysed 24 key employment status cases against the CEST tool. HMRC had previously said the CEST tool had provided incorrect outcomes for only 2 of the 24 cases. Contractor Calculator re-analysed the cases and found that in only 14 out of the 24 cases the CEST tool gave the correct answer. It called the tool 'hopelessly unreliable'.

www.contractorcalculator.co.uk/cest_exposed_hopelessly_unreliable_hmrCs_foi_543610_news.aspx

4. Business tax

4.1 Late payment interest charged on late applications of treaty clearance

A recent case heard at the CJEU could have a potential impact on the equivalent position in the UK. The case concerned late payment interest charged following late application of treaty clearance in respect of withholding tax (WHT) charged on interest paid on a loan to an overseas lender.

The case concerned a Bulgarian company that paid interest to three companies in other EU member states. It did not deduct WHT on the basis it qualified under the double tax treaties with each country. It did so, however, *before* it had received the necessary treaty clearance. In practice, in the UK and Bulgaria this can be done by concession, but HMRC (or equivalent) has the right to charge late payment interest and possibly penalties.

The Bulgarian company contested the late payment interest and the CJEU found for the taxpayer on the basis it was contrary to the right of freedom to provide services and could not be justified as necessary to ensure the collection of tax.

The case may therefore be relevant to such challenges made in the UK against HMRC.

TTL Eood v Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' [2018] CJEC C-553/16
<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:62016CJ0553>

4.2 Distributions in a winding up: HMRC updates its manuals

HMRC has updated its guidance on the TAAR for distributions in a winding up.

HMRC has updated its manual at CT36340. This section deals with the Targeted Anti-Avoidance Rule (TAAR), which seeks to prevent individuals converting what would otherwise be a dividend into a capital payment on the winding up of a company.

Several new paragraphs have been inserted that clarify:

- a decision not to make an income distribution prior to winding up will not of itself satisfy the condition;
- it is for the taxpayer to self-assess and decide for himself that tax avoidance is not the main purpose. It is then for HMRC to prove the decision was not reasonable;
- The condition is applied by reference to the intentions at the time of winding up but HMRC will look at all evidence including events that occur after winding up; and
- the position regarding situations where owners remain within the business but as an employee.

Minor amendments have also been made to CTM36330 so that the wording mirrors the legislation.

www.gov.uk/hmrc-internal-manuals/company-taxation-manual/ctm36340

5. VAT

5.1 Supplies of the services of temporary workers by employment bureaux

The CA has agreed with HMRC that the supply of temporary workers by an employment bureau does not amount to introductory services, but that the temporary workers' services are made through the employment bureau.

The appellant, Adecco UK Limited and Others ('Adecco'), was an employment bureau supplying clients with temporary staff ('temps'). Adecco invoiced its clients the amount payable to the temp, being the temporary staff remuneration plus a commission for introductory services.

Based on the FTT decision of *Reed Employment Limited* [2011] UKFTT 200 (TC), Adecco considered its supplies to be that of introductory services. Adecco maintained that it was the temps that were making

supplies of the underlying services to Adecco's clients and therefore considered only the commission element of its fees should be subject to VAT.

HMRC, on the other hand, argued that the services of the temps were supplied by and through Adecco and therefore the totality of what was paid by the client to Adecco including temp remuneration should be subject to VAT.

The CA, like the FTT and UT, ruled in favour of HMRC. In coming to the decision, the CA considered the contractual arrangements between Adecco, the temps and clients. Some of the key factors influencing the conclusion were:

- there were no direct contracts between the temps and clients;
- the contracts required the temps' services to be made 'through Adecco';
- Adecco paid temps on its own behalf, rather than as agent for the clients; and
- Adecco did not 'drop out of the picture' once the temp had been introduced to the client.

The CA also held that *Reed Employment* was wrongly decided.

This case highlights the VAT complexities of tri-partite arrangements. If you have any questions regarding existing or prospective tri-partite arrangements, please contact a member of our VAT team.

Adecco UK Limited v HMRC [2018] EWCA Civ 1794

www.matrixlaw.co.uk/wp-content/uploads/2018/07/Adecco-UK-Ltd-Ors-v-Commissioners-for-HMRC-2018-EWCA-Civ-1794.pdf

5.2 HMRC publish draft update to Specified Supplies Order legislation

HMRC has published draft measures to amend the VAT (Input Tax) (Specified Supplies) Order 1999, a key part of the VAT legislation for insurance and financial intermediaries. The SSO allows input VAT recovery for supplies that would be exempt services in the UK, where the intermediary's customer is located outside the EU.

The stated aim of the amendment is to counteract 'offshore looping'. A recent FTT case illustrates the area of concern: a UK broker provided insurance intermediary services to a non-EU insurer who in turn insured UK retail customers. The SSO allowed the UK broker to recover VAT on associated costs as its supplies were to a customer located outside of the EU. HMRC's proposed measures will restrict this entitlement to services where the end user of the insurance or financial service is outside the EU.

Although this updated legislation is designed to counter arrangements that HMRC regards as avoidance, it could, if left unamended, have significant unintended consequences for other financial intermediaries. If a business provides intermediary services to recipients located outside of the EU, it may have no way of proving that the end user is also outside the EU and its input VAT recovery may therefore be affected by these changes.

Please speak to a member of our VAT team to discuss if this will impact your business.

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/727149/Draft_legislation_-_Amendment_of_the_VAT_Input_Tax_Specified_Supplies_Order_1999.pdf

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/727152/Draft_explanatory_memorandum_-_amendment_of_the_VAT_Input_Tax_Specified_Supplies_Order_1999.pdf

5.3 VAT prepayment rule

The SC has dismissed an appeal against a VAT prepayment as a condition of an appeal going forward. The taxpayer claimed that the prepayment of VAT required to appeal its VAT assessment constituted a breach of the EU principle of equivalence. The SC disagreed.

The SC agreed with the previous reasons given by the CA.

The taxpayer, its Totel Ltd, had challenged the previous conclusions of the CA. It argued that because appeals against assessments of income tax, CGT and SDLT did not require a prepayment, the fact that appeals against VAT assessments did require such payment was an example of unfavourable treatment against VAT tax and, thus, a breach of the EU principle of equivalence law.

The EU principle of equivalence law requires that the procedural rules of member states applicable to claims based on EU law are no less favourable than those governing similar domestic claims.

This law required the presence of a true comparator, which the taxpayer could not demonstrate. The SC ruled that whilst the prepayment requirement for a VAT reassessment could arguably be deemed as a less favourable treatment in comparison with another 'similar' domestic type of tax, this appeal fell short because no domestic tax constituted a true comparator to VAT.

Totel Ltd V HMRC [2018] UKSC 44

www.bailii.org/uk/cases/UKSC/2018/44.html

5.4 Making Tax Digital for VAT

HMRC release VAT Notice 700/22 which provides additional detail to help taxpayers understand how VAT records must be kept and returns submitted from April 2019.

HMRC has published its much anticipated VAT Notice on Making Tax Digital (MTD) for VAT as well as listing software suppliers that it is working with on MTD. The list of software suppliers will be updated on an ongoing basis as more providers go through the testing phase with HMRC.

The Notice does not contain any surprises, but adds further detail around the digital records businesses must keep and ways to record transactions digitally in certain circumstances. It provides further examples of when the VAT compliance process must contain digital links. There is still some uncertainty for those businesses with more complex VAT issues, such as partial exemption and other adjustments.

MTD will be mandatory for all VAT registered businesses with taxable turnover above the VAT registration threshold (currently £85,000) from April 2019. HMRC has confirmed that other taxes will follow at a later date but not before April 2020 at the earliest.

Under MTD, taxpayers will need to make sure that they store VAT records digitally, are able to submit VAT returns electronically via an Application Program Interface ('API') and have a digital link from source data to VAT return submission.

www.gov.uk/government/publications/vat-notice-70022-making-tax-digital-for-vat

www.gov.uk/government/publications/software-suppliers-supporting-making-tax-digital-for-vat

6. And finally

Nice

Forrest Gump once said: 'Life is like a box of chocolates. You never know what you're gonna get.' Of course, he really meant VAT. Actually, VAT and chocolate are generally interchangeable for And finally, both being invariably delicious, and mysteriously addictive.

The VAT box this week, *Kinnerton Confectionery Limited v HMRC* is indeed true confectionery and not cooking chocolate. Does that matter? Well, apparently it does. For those of us who are true chocoholics that's a distinction without a difference - just let us at the bar. This case, though, is one to nibble slowly, savouring each mouthful. Was a chocolate bar standard rate confectionery or zero rated cooking chocolate? If that isn't a silly enough question, the poor court then looked at how it was 'held out for sale'. The size of the bar mattered. Packaging mattered. Placement in the store mattered. The taxpayer magnificently argued that, wait for it, it mattered if the chocolate was broken up. Of course, if it had been, we all know that the calories would have leaked out, but so what?

It was just chocolate; we almost said plain chocolate. Only VAT could have cooked up, or is it confectioned? This fantasy world of nice distinctions. Spare a thought too for a heroic judge Anne Redston. All those different sorts of chocolate in evidence and no tasting, just to check.

<http://financeandtax.decisions.tribunals.gov.uk//judgmentfiles/j10510/TC06548.pdf>

Glossary				
Organisations		Courts	Taxes etc	
ATT - Association of Tax Technicians	ICAEW - The Institute of Chartered Accountants in England and Wales	CA - Court of Appeal	ATED - Annual Tax on Enveloped Dwellings	NIC - National Insurance Contribution
CIOT - Chartered Institute of Taxation	ICAS - The Institute of Chartered Accountants of Scotland	CJEU - Court of Justice of the European Union	CGT - Capital Gains Tax	PAYE - Pay As You Earn
EU - European Union	OECD - Organisation for Economic Co-operation and Development	FTT - First-tier Tribunal	CT - Corporation Tax	R&D - Research & Development
EC - European Commission	OTS - Office of Tax Simplification	HC - High Court	IHT - Inheritance Tax	SDLT - Stamp Duty Land Tax
HMRC - HM Revenue & Customs		SC - Supreme Court	IT - Income Tax	VAT - Value Added Tax
HMT - HM Treasury		UT - Upper Tribunal		

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