Smith & Williamson

Tax update

A round-up of recent issues

9 July 2019

1. General

1.1 HMRC publishes 2019 departmental plan

HMRC's new departmental plan sets out updated objectives to reduce tax evasion.

HMRC has published an updated single departmental plan, setting out its 2019 objectives. These include investing £800m in additional work to tackle evasion and non-compliance, using new bulk data powers to make it harder for businesses to operate in the hidden economy, and raising £5bn in 2019/20 more than in 2015/16 by tackling tax avoidance, evasion and non-compliance. The plan also mentions tackling aggressive tax planning and imbalances in the tax system. It is not clear what these latter two terms are meant to cover that is not already covered by the previous ones.

www.taxjournal.com/articles/hmrc-publishes-departmental-plan-for-2019

2. Private client

2.1 HMRC succeeds in appeal on high income child benefit charge penalties

HMRC has won an appeal on failure to notify penalties for the high income child benefit charge (HICBC). The UT held that the taxpayer was liable for HICBC, so the discovery assessments were valid, and the penalties correct, despite the technical difference between HICBC and tax.

The taxpayer earned over £50,000, but did not inform HMRC that his wife was claiming child benefit, and that he was therefore subject to the HICBC. HMRC issued discovery assessments for three years, covering the HICBC and penalties for failure to notify. The taxpayer accepted the HICBC, but appealed the penalties.

The FTT had cancelled the penalties, holding that failure to notify penalties could only be issued where there was potential lost revenue (PLR) on a discovery assessment or self-assessment. The definition of PLR does not include HICBC, only tax, so there was no valid assessment. There was no PLR in a case of underpayment of HICBC. The penalties were therefore invalid.

The UT disagreed, stating that a valid assessment was not necessary for PLR to exist. The taxpayer was liable for HICBC, and it was not necessary to distinguish between this and tax. The penalties were upheld.

HMRC v Robertson [2019] UKUT 0202 (TCC)

www.bailii.org/uk/cases/UKUT/TCC/2019/202.html

2.2 Bonus cannot be time apportioned for tax

The FTT has rejected a taxpayer's contention that his bonus, paid at the end of a retention period, should be apportioned across that period. HMRC's view that it is taxable in the tax year of receipt only has been upheld.

The taxpayer's employer merged with a larger firm. As part of its retention strategy, it made bonus payments to staff. The bonuses were paid over a year after being announced, on condition that recipients had met certain conditions throughout the period, including being an active employee in good standing. The taxpayer argued that the bonus should therefore be time apportioned over the period, spanning three tax years. HMRC held that the bonus was taxable in the tax year of receipt.

The FTT rejected the taxpayer's appeal to the closure notice. Although his continued employment throughout the period was a requirement to receive the bonus, he only became entitled to it at the end of the period. The full amount was taxable in the last year.

Murphy v HMRC [2019] UKFTT 409 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2019/TC07224.html

2.3 FTT halves 'disproportionate' penalties

The FTT has upheld late filing penalties for a taxpayer who did not have a reasonable excuse. The penalties were halved, however, on the grounds that £4,800 of penalties was disproportionate in a case with only a nominal amount of tax at stake.

The taxpayer was told to complete returns for three tax years after failing to register when starting self-employment. He experienced some problems with the online system, but did not prove that he had a reasonable excuse for filing two returns extremely late. The FTT heard the appeal out of time due to the amount of penalties at stake (£4,800). For two of the three tax years there was no liability, and only a nominal amount in the third. There was no evidence before the FTT that the HMRC officer had considered special circumstances, which can include proportionality. The FTT decided that penalties of £4,800 were disproportionate, and halved them, commenting that a penalty at this level 'would send the wrong message to taxpayers'.

Walker v HMRC [2019] UKFTT 402 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2019/TC07217.html

2.4 Litigation costs not allowed as expense on sale

A minority shareholder who litigated against a majority shareholder to be treated fairly as a shareholder has been denied a CGT deduction for the litigation costs. The FTT decided that this action for fair treatment as a shareholder did not fall within the allowable category of defence of title.

The taxpayer held shares in a British Virgin Islands (BVI) company. He entered into litigation with the majority shareholder as he felt that he was being treated unfairly as a minority shareholder. The litigation was settled out of court on the morning of the hearing in his favour, and he sold the shares at a good price as part of the settlement.

The taxpayer argued that the litigation was necessary to preserve his title to the shares, and should therefore be an allowable expense. HMRC considered that the expenditure was not wholly and exclusively incurred for this purpose as several measures were sought in the litigation, such as restitution of profits. The case was for fair treatment as a shareholder, not solely in defence of title.

Gray v HMRC [2019] UKFTT 393 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2019/TC07208.html

2.5 Partner subject to penalties on partner payment notices

The FTT has upheld late payment penalties for partner payment notices (PPNs) issued during settlement discussions. The partner did not wish to pay amounts demanded in the PPNs before HMRC had clarified whether or not he would be refunded if the partnership won in its litigation with HMRC, but this was not a reasonable excuse for late payment.

The taxpayer was issued with PPNs, followed by penalties for their late payment. He appealed the penalties, contending that he had been in ongoing settlement discussions with HMRC, and had been assured that no penalties would be payable while they were ongoing. His case was related to HMRC's ongoing litigation against the partnership. He had asked for clarification, which was not given, on what would happen if HMRC lost that case after he had settled the tax claim against him before he made payment.

The FTT took the simple approach, upholding the penalties as he had been issued with PPNs and not paid them by the due date shown. It was made clear to him that he needed to make the payments on time, and failing to pay whilst waiting for clarification from HMRC was not a reasonable excuse.

Pau v HMRC [2019] UKFTT 392 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2019/TC07207.html

3. Trusts, estates and IHT

3.1 Office of Tax Simplification reports on IHT

The Office of Tax Simplification (OTS) has published its recommendations for simplifying IHT. Key areas covered include lifetime gifting, agricultural and business property relief, and the interaction with CGT.

The OTS has published the second part of its report on IHT. The first part, published in November 2018, dealt with administrative aspects. This 103 page report looks at making IHT simpler, more intuitive and easier to operate. It makes recommendations for the Government to consider in three key areas: lifetime gifts, the interaction of CGT and IHT, and agricultural and business property relief (APR and BPR). Recommendations have also been made in other areas such as pre-owned asset tax.

The recommendations are summarised on pages 13-14 of the report, and include:

- removing the CGT uplift on death where a relief or exemption from IHT applies, such as the spouse exemption or BPR/APR. The recipient would instead be treated as acquiring the asset at historic base cost;
- reducing the 7 year period for IHT to 5 years while abolishing taper relief;
- replacing the current gift exemptions with an overall personal gifts allowance;
- reforming the exemption for normal expenditure out of income;
- considering whether or not the level of trading activity for BPR should be increased; and
- aligning the IHT treatment of furnished holiday lets with income tax and CGT treatment.

The OTS has not made any recommendations in this report on the residence nil rate band on the basis that it is still relatively new. It has instead made suggestions for the Government to consider when reviewing this area of policy. This will be a disappointment for the many who think this relief is overly complicated.

www.gov.uk/government/publications/ots-inheritance-tax-review-simplifying-the-design-of-the-tax

https://blog.step.org/2019/07/05/ots-inheritance-tax-review-second-report-a-welcome-start-but-could-go-further/

4. PAYE and employment

4.1 FTT finds different IR35 treatment for two engagements

Two engagements by a doctor have been examined by the FTT, which found that one was caught by the IR35 regime but the other was not. The different tax treatments resulted from differences in the doctor's right to substitute another worker, the termination period and the obligation on the hospital to provide work.

The taxpayer was a personal service company that engaged with hospitals to provide the services of the company's owner as a locum doctor. HMRC made determinations in relation to two of these engagements on the basis that they fell within the IR35 legislation. Under these rules, a hypothetical contract is constructed between the worker and the engaging employer, reflecting the actual arrangements. If that hypothetical contact would have been a contract for employment, the personal service company is liable for IT and NICs on the payments made by the hospital. These laws have since been amended to place the liability on the employer.

The FTT analysed the agreements between the hospitals and the taxpayer and constructed the hypothetical contracts. It found that one engagement was a contract of employment but the other was not. The distinction arose because of three differences in the contracts. The contract that was not caught by IR35 allowed the doctor the right to substitute another person to complete the work, allowed only one day's notice on termination, and placed no obligation on the hospital to provide work. In contrast, the other contract allowed one week's notice of termination and did impose an obligation on the hospital to provide work and on the doctor to personally perform it.

George Mantides Ltd v HMRC [2019] UKFTT 387 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2019/TC07202.html

4.2 Divers' employment income incapable of being a trade carried on by a partnership

In two very similar cases, the FTT has found that income received by the mixed gas divers was employment income. IT was not capable of being trading income carried on by a partnership. Although such income is deemed to be trading income, that deeming provision only extends to a deemed sole trade, not to deemed trading income of a partnership of which the diver is a partner.

The two divers claimed to operate their work as partnerships, each with his spouse who performed administrative tasks. The income from the diving assignments was split between the partners in each partnership, thus lowering the overall rate of tax paid. These arrangements had been in place for several years before HMRC opened enquiries and determined that the income entirely belonged to the diver.

The FTT found first that the deeming provision that operates to treat the employment income of a diver as trading income does not extend to allowing that income to be treated as the trading income of a partnership. Second, it found that the arrangements for both divers were employment contracts rather than self-employment. The argument that the underlying arrangements were in fact trades, not deemed trades consequently did not stand. Finally, it was held that the employments were between the divers and the employers, not the partnerships and the employers. There were therefore no circumstances in which the employments could be regarded as giving rise to income attributable to the partnerships. The appeals were both dismissed.

Joseph Puttnam v HMRC [2019] UKFTT 389 (TC): *www.bailii.org/uk/cases/UKFTT/TC/2019/TC07204.html*

David Green v HMRC [2019] UKFTT 390 (TC): *www.bailii.org/uk/cases/UKFTT/TC/2019/TC07205.html*

5. Business tax

5.1 No legislative anti-avoidance purpose in group capital gains case

The FTT ruled in favour of a taxpayer that undertook a complex restructuring exercise to avoid directly acquiring a group of companies with brought-forward capital losses. Relief for capital gains would have been restricted if the group had been acquired directly, so the acquisition was carried out in such a way as to satisfy an exemption in the legislation. The FTT allowed the appeal on the basis that this reconstruction qualified for the exemption, even under a purposive interpretation of the law.

The transaction involved two groups of companies: one with significant unrealised capital gains (the gains group) and the other with significant brought-forward capital losses (the loss group). The gains group wished to acquire the loss group to mitigate the CT on its chargeable gains by electing to treat the gains as arising in the loss group. This relief would, however, be denied under the CGT pre-entry loss rules if the gains group directly acquired the loss group. The shareholders of the gains group therefore undertook a complex restructuring exercise such that the loss group was acquired by a new holding company. The new holding company subsequently acquired the gains group, and then transferred the loss group to the gains group. The final position was the same as what would have resulted from a direct acquisition of the loss group by the gains group. The acquisition steps, however, were designed to satisfy the specific criteria in the CGT legislation. Provided that this subsection was satisfied, the losses could be transferred within the final structure.

HMRC argued that those criteria were not met when the legislation it was read with a purposive interpretation. The FTT examined the meaning of the two relevant phrases in the legislation in light of Parliament's purpose. 'Immediately after' was held to mean at or almost at the very moment after an event. 'Had assets' was held not to include scenarios in which a company did not own an asset but would in the future own those assets pursuant to a series of preordained transactions. It also found that these provisions did not have a broad anti-avoidance purpose; the purpose was to limit the use of losses in specific circumstances only. The appeal was therefore upheld.

ANO (No.1) Limited v HMRC [2019] UKFTT 406 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2019/TC07221.html

5.2 CIOT issues advice on reclassifying vans

In a recent case, some vans have been reclassified as cars for employee benefit purposes, resulting in a significantly greater tax charge. The CIOT has published a note for advisers concerned that the decision will affect their clients.

In response to the *Payne* UT case, the CIOT technical team have published a note for members concerned about reporting of employee benefits. The case narrowed the definition of a van, reclassifying some vehicles as cars. The employee benefit tax charges are lower on vans than cars provided to employees, so the reclassification could result in tax liabilities for earlier years.

Tax advisers and employers are advised to consider the characteristics of vans provided to employees to check whether or not they meet the new requirements. If a van is reclassified as a car, a disclosure may be necessary for prior years. The case is likely to go to the CA, so cannot be regarded as final at this stage, but clients should be ready to make corrections, if needed.

www.tax.org.uk/policy-technical/technical-news/car-or-van-%E2%80%93-benefit-kind-issues-crew-cab-panel-vans

HMRC v Payne & Ors [2019] UKUT 90 (TCC)

www.bailii.org/uk/cases/UKUT/TCC/2019/90.html

5.3 LLP enquiries made under IT provisions found to be invalid

The FTT has upheld an appeal against closure notices that were issued to two Limited Liability Partnerships. The enquiries had been opened under IT provisions, and the FTT found that a Limited Liability Partnership is treated as a company for the purposes of tax administration provisions.

HMRC had opened enquiries into two Limited Liability Partnerships (the LLPs) under an IT tax administration provision. The subsequent closure notices concluded that neither of the LLPs was carrying on business with a view to a profit. The income tax deeming provision therefore did not apply. This deems an LLP to be a partnership for tax purposes if it is carrying on a business with a view to a profit. Where this condition is not met, as in this case, the default position applies. The LLP is then treated as the body corporate it is in fact is, which must submit a CT return.

The LLPs therefore argued that the enquiries were not valid because they were opened under IT provisions rather than CT provisions.

The FTT examined the treatment of LLPs under UK tax law and found that LLPs are always treated as companies for the purposes of tax administration laws. This is the correct approach whether or not an LLP is deemed to be partnership or a company for the purposes of calculating and paying tax. The enquiries should therefore have been opened under the CT administrative provisions. The appeal was allowed and the closure notices held to be invalid.

Inverclyde Property Renovation LLP and another v HMRC [2019] UKFTT 408 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2019/TC07223.html

6. VAT

6.1 UT upholds the decision that VAT is due on free wine

The UT has ruled that VAT due on the 'free' wine offered under a promotion by Marks & Spencer. The ruling in Kuwait Petroleum did not apply because there was no timing difference between when payment was made and when the wine was received. There was a direct link between the provision of the wine and the consideration paid by the customer, so VAT is due on the wine element.

The taxpayer, Marks & Spencer PLC (M&S), offered a promotion where a customer could purchase three food items for £10 and receive a free bottle of wine. In April 2018, the FTT ruled that the £10 should be apportioned between the food and wine for VAT purposes, such that VAT was to be accounted for on the wine. M&S appealed the decision on the basis that, in line with *Kuwait Petroleum* [1999] STC 488, promotional items could be given for nil consideration and therefore no VAT would be due.

The UT held that the *Kuwait Petroleum* ruling could not be applied in this case as there was a fundamental timing difference. In *Kuwait Petroleum*, the customers would receive promotional items at a later date, whereas M&S customers would obtain the wine at the same time as the other foods items when they made payment. The UT ruled that there was a direct link between the provision of the goods and the consideration received: the wine would not have been provided if the customer had not paid the £10. An element of VAT was due on the wine; no VAT was due on the food items since they were zero rated. The appeal was dismissed.

Marks and Spencer PLC v HMRC [2019] UKUT 182 (TCC):

www.bailii.org/uk/cases/UKUT/TCC/2019/182.html

Kuwait Petroleum [1999] STC 488:

http://curia.europa.eu/juris/showPdf.jsf?docid=101340&doclang=en

7. Tax publications and webinars

7.1 Briefing Notes published

The following Briefing Notes have been published

- *Taxation and national insurance on coming to the UK*
- *Taxation on leaving the UK*

7.2 Webinars

The following client webinars are coming up over the next few months.

- 10 July 2019: *Key tax considerations for M&A*
- 23 July 2019: *Planning for the future*

https://smithandwilliamson.com/en/events/

8. And finally

8.1 Rhetorical (de)vices

HMRC has updated its Single Departmental Plan for 2019. The objectives include the cryptically-worded aim to '*Raise an additional £5bn a year on 2015 to 2016 by 2019 to 2020 by tackling tax avoidance and aggressive tax planning, evasion and non-compliance, and by addressing imbalances in the tax system'*. Tax evasion and non-compliance are concepts with which we are familiar, and are obviously not going to be tolerated. Tax avoidance is a well-documented subject, and we are only repeating ourselves when we say that what was once a term used to describe otherwise legal tax planning has been so misused that it has now come to mean almost the same thing as tax evasion. But it is the reference to tackling 'aggressive tax planning' that particularly concerns us. What is aggressive tax planning? If it is illegal, why has a new phrase been invented for what is simply tax evasion? If it is legal, and not avoidance, why is HMRC tackling it? And what exactly are these imbalances in the tax system?

This continued erosion of legitimate behaviour by using loaded rhetoric to invent new supposed wrongdoings cannot be left unnoticed. According to HMRC's own figures, the revenue lost to tax avoidance in 2017-18 was £4.6bn less than that attributed to failure to take reasonable care.

Surely HMRC's resources would anyway be better spent addressing that issue?

HMRC Single Departmental Plan: *www.gov.uk/government/publications/hm-revenue-and-customs-single-departmental-plan/hm-revenue-and-customs-single-departmental-plan--2*

Measuring Tax Gaps 2019 edition: *www.gov.uk/government/statistics/measuring-tax-gaps*

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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