Smith & Williamson

Tax update

A round-up of recent issues

8 September 2020

1. Private client

1.1 HC refuses to rectify error resulting in tax of £215,000 on charitable donation

The HC has refused to allow a taxpayer to rectify an error on his return, which resulted in a £215,000 tax bill on his charitable donation of £800,000. He had entered the wrong figure for the carry back claim and so the claim was denied completely. He became liable for the full amount of the gift aid claim, as in the tax year the donation was made he had not paid enough tax to cover it. The HC found that it did not have jurisdiction to rectify a tax return.

The taxpayer made a gift aid donation of £800,000 in 2017/18. Under the carry back rules, he intended to claim relief on his 2016/17 tax return, but erroneously used a figure of £400,000. He had entered that

figure into his software when planning to make a £400,000 donation, and had forgotten to change it when he decided to increase the donation. HMRC does not allow carry back figures to be amended after the return is submitted, and does not permit partial carry back claims, so the entire donation of £800,000 fell into 2017/18.

In 2017/18, he had not paid enough tax to cover the gift aid reclaim by the charity, and after investigations by HMRC he became liable to pay approximately £215,000 so in tax, interest, and penalties for carelessness, including the full gift aid reclaim of £200,000. He would have derived no financial benefit in his 2016/17 return by making the increased claim on it.

He applied to the HC to rectify his original tax return, as he felt that this was a disproportionate outcome. The HC found that the tax return was not a unilateral instrument, so it did not have power to rectify it. It also found that it should not circumvent the tax tribunals, so did not have jurisdiction to amend a return. If it had had that power it would not have exercised it, as the error was caused by the taxpayer's carelessness.

Webster, Re [2020] EWHC 2275 (Ch)

www.bailii.org/ew/cases/EWHC/Ch/2020/2275.html

1.2 FTT rules on voting rights for entrepreneurs' relief

The FTT has found that shares that did not have voting rights under the articles of association did not constitute shares in a personal company for the purposes of entrepreneurs' relief.

The taxpayer disposed of his shareholding of 'B' shares. Under the articles of association, the holders of B shares were not entitled to receive notice of, attend or vote at any of the general meetings. The taxpayer claimed entrepreneurs' relief on the disposal of the shares, and included a note on his tax return stating that the rights attached to the B shares were incorrectly stated. HMRC refused the claim for relief.

The FTT held that the articles of association left no room for any doubt as to their construction and expressly prohibited B shareholders from voting at the general meetings. The taxpayer's claim that the majority shareholder would have agreed to amend the articles was irrelevant, as the articles had not been updated to reflect this. There was also no evidence that the B shareholders had voted or were eligible to vote at any general meetings. The FTT agreed that entrepreneurs' relief (as it was then known) was therefore not available.

Guy Holland-Bosworth v HMRC [2020] UKFTT 331 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2020/TC07811.html

2. Trusts, estates and IHT

2.1 HMRC Trusts and Estates Newsletter

The latest edition of the HMRC Trusts and Estates Newsletter has been published, and includes information about changes to the Trust Registration Service (TRS) and various reminders.

Points raised include:

- the current version of the TRS will be replaced with a new online form on 23 September. Any partially completed registrations will be lost, and will have to be restarted on the new form;
- a request for volunteers to test the changes that will be made to the TRS as a result of the fifth EU Anti-Money Laundering Directive;
- a reminder that details on the TRS should now be updated, and declarations should be made if nothing has changed, by the normal self-assessment deadline of 31 January for 2019/20 changes;
- reminders on trust changes in the Finance Bill, such as to offshore trusts and excluded property; and
- the facility to submit IHT returns by Dropbox is being withdrawn, and can only be used on request if an individual cannot submit the return by post.

www.gov.uk/government/publications/hm-revenue-and-customs-trusts-and-estates-newsletters/hmrc-trusts-and-estates-newsletter-august-2020

3. PAYE and employment

3.1 GAAR Panel rules against contrived reward scheme

The GAAR Panel has issued two further opinions on artificial arrangements designed to deliver a tax-free return for a director shareholder while obtaining a corporate tax deduction, using an independent fund manager and a specially designed trust. The Panel found these arrangements were effectively tax abusive remuneration arrangements.

The arrangement was used by a company with a sole employee and shareholder (the Individual) who provided his services as a consultant. The arrangement involved entering into a token loan arrangement with a third party that managed a trust. The trust was designed to include as beneficiaries both the manager company and those who had provided funds to the manager company, thus making the Individual a beneficiary of the trust as well, because of the token loan arrangement.

The manager entered into a substantial loan with the Individual and subsequently the company contributed an amount to the trust that was broadly equivalent to the value of the loan plus fees.

Unsurprisingly, the Panel found that these arrangements were contrived and abusive. They held that the arrangement was designed to circumvent the disguised remuneration rules and the employment benefit contribution rules.

HMRC has subsequently followed this ruling up with a Spotlight (see article 4.2 below).

www.gov.uk/government/publications/gaar-advisory-panel-opinion-of-7-april-2020-rewards-in-the-form-of-loans-for-employees-including-contributions-to-a-trust

3.2 HMRC commissioned report on tax advantaged share schemes

A new report on tax advantaged share schemes (TASS) has found that employers and employees generally viewed such schemes positively and perceived them to have continue relevance. The results highlighted a need for greater awareness of each of the schemes.

The research showed that TASS positively impacted employee engagement, and were important for recruiting talented staff. Both employers and employees felt that increasing the awareness of TASS was the key to boosting participation.

The report found that junior employees were less likely to participate in TASS than their senior colleagues. Some employers and employees suggested that TASS uptake would be improved by a relaxation to the eligibility criteria and the features of the schemes. The cost of introducing TASS acted as a barrier for small companies when compared to other forms of employee benefits that are less expensive to introduce.

The three main schemes, Company Share Option Plans, Share Incentive Plans and Enterprise Management Incentive schemes were all viewed as attractive and flexible. The required holding periods,where they applied, however, acted as a deterrent for some employees. Interviewees viewed Save as You Earn schemes less favourably owing to lack of interest on savings, lack of bonus rates and the perceived inflexibility of the scheme.

www.gov.uk/government/publications/tax-advantaged-share-schemes-research

3.3 UT overturns FTT ruling on date right to acquire shares arose

The UT has found that an employment related share option conferred the right to acquire securities at the date of grant, before the taxpayer became non-resident. It agreed with the FTT that some restricted shares he had also been granted were acquired by reason of his employment, as a share for share exchange before the restrictions were lifted did not break the link.

The taxpayer was employed by a company in Bermuda. In 2001, he was granted share options by reason of his employment. These vested in three tranches and he exercised them later. The FTT found that he had acquired the right to acquire securities when the shares vested. It also determined the date he became non-UK resident, which was before the third tranche vested. He was therefore liable to UK tax on exercise of the first two tranches of the options, though by then he was non-resident. HMRC appealed this point, arguing that the right to acquire securities arose on grant of the options, when he was UK resident, so all three tranches were subject to UK tax.

HMRC contended that a right to acquire securities arose when the options were awarded, as the legislation governing share options relied on the date of grant, not on the date the options became unconditional. The FTT had chosen the vesting date, as the vesting of the options was conditional on the taxpayer's continued employment. The taxpayer contended that the right to acquire the shares did not exist until it became unconditional. The UT overturned the FTT decision, finding on an analysis of the scheme documentation that the grant of the option was the date on which the right was acquired, so all three tranches were subject to UK tax.

The taxpayer was also granted restricted shares, in 2002. These were subject to a share for share exchange before restrictions were lifted in 2005. The FTT found that he acquired these as a director or employee, so they were subject to IT. He appealed this element of the decision, contending that he acquired them as a shareholder, as when they were exchanged all shareholders were granted shares in the new company, whether or not they were employees. The UT dismissed this appeal, agreeing with the FTT that the share for share exchange did not break the link between the acquisition of the shares and his employment.

Charman v HMRC [2020] UKUT 253 (TCC)

www.bailii.org/uk/cases/UKUT/TCC/2020/253.html

4. Business tax

4.1 CA upholds UT decision on permanent establishments

The CA has agreed with the UT that the permanent establishment (PE) provisions of the UK/Ireland Double Taxation Agreement (DTA) are correctly implemented in UK domestic law. It held that the provisions could be given effect in many different ways, including in the way set out in UK law.

The taxpayers were two Irish banks that had PEs in the UK. Under UK tax law, PEs are allocated a notional amount of free capital in line with the amount of capital they would have had if they were independent entities. HMRC believed that the notional capital allocated to the PEs was too low, and therefore made Capital Attribution Tax Adjustments in the tax returns. These adjustments disallowed some tax relief for interest expenses. The taxpayers argued that such adjustments were precluded by the UK/Ireland DTA. In their view, the actual capital position of the PEs had to be used for tax purposes.

The CA upheld the decision of the UT. Although the correct starting point is the actual capital attributed to the PE, an adjustment should be made if it does not reflect the position that would have been if the PE was in fact a separate and independent entity. The UK provisions relied on by HMRC are not the only way to implement this approach, but they are consistent with the DTA.

Irish Bank Resolution Corporation Ltd (in special liquidation) and another v HMRC [2020] EWCA Civ 1128

www.bailii.org/ew/cases/EWCA/Civ/2020/1128.html

4.2 HMRC Spotlight 56 on disguised remuneration

HMRC follows up on the General Anti-Abuse Rule (GAAR) Advisory Panel's warning on the use of further tax avoidance arrangements that remunerate company directors of owner managed companies through the use of loans made through a remuneration trust as outlined in the Panel's Opinion of 7 April 2020.

HMRC has issued Spotlight 56 to highlight and follow up on the consequences of the GAAR Panel's opinions, see Article 3.1 above, regarding such arrangements.

www.gov.uk/guidance/disguised-remuneration-tax-avoidance-by-owner-managed-companies-using-remuneration-trusts-spotlight-56

5. VAT

5.1 New consultation on VAT groups

HMT has called for evidence on the effect of VAT grouping. The consultation is intended to inform future policy direction, though the consultation document does not provide any specific proposed measures.

The call for evidence focuses on the establishment provisions of VAT grouping, compulsory VAT grouping, and the eligibility criteria for limited partnerships. HMT notes that the financial services industry is likely to be particularly interested in this consultation. It will close on 20 November 2020.

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/913002/2008268_VAT_Grouping_Call_for_evidence.pdf

6. Tax publications and webinars

6.1 Tax publications

The following Tax publications have been published

- *Strategic land: the challenge of multiple owners*
- *Strategic Land - Land Pooling Trusts*
- *Strategic Land – when is it sold?*

7. And finally

7.1 Tangling with the GAAR Panel

For the first time, we may be uncomfortable with a GAAR Panel ruling (see Article 3.1 above). Not, indeed, over the general conclusion that the arrangement was contrived and artificial, but over the Panel's conclusion that the arrangement was a disguised remuneration one.

Admittedly, we haven't seen the papers, but no matter; for your thoughts, here is a possible alternative analysis. The case involved an owner manager and his one man business. Like many such taxpayers, his only interest will probably have been in just getting cash out of the company and into his hands with a minimum of tax loss on the way. He would have been pretty indifferent how it was technically done. He had previously basically done this through dividends. He couldn't just borrow the cash out of the company because of the loans to participators rules and, anyway, such a loan doesn't generate a corporate tax deduction.

Along comes a scheme provider who says it has solved both of these issues. The cash can come out structured as a tax-free loan but with a CT deduction. That's all the Individual would have wanted to hear. 'Where do I sign?'

Of course, the arrangement is every bit as GAAR prone as it ever was. Just possibly, though, the Panel shoehorning the arrangement into one that was to replace a supposed salary was, well, a bit contrived and artificial.

www.gov.uk/government/publications/gaar-advisory-panel-opinion-of-7-april-2020-rewards-in-the-form-of-loans-for-employees-including-contributions-to-a-trust

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	RS – Revenue Scotland	SC – Supreme Court	IT – Income Tax	VAT – Value Added Tax
HMT – HM Treasury		UT – Upper Tribunal		