UK Tax Bulletin

February 2016

Field Court Tax Chambers

Introduction

Latest Rates of Inflation and Interest

The following are the current rates at February 2016

Current Rates	
Retail Price Index: January 2016	258.8
Inflation Rate: January 2016	1.3%
Indexation factor from March 1982:	
to January 2016	2.258
to December 2015	2.280

Interest on overdue tax

Interest on all unpaid tax is charged at the same rate.

The formula is Bank base rate plus 2.5% which gives a present rate of 3%.

There is one exception: Quarterly instalments of corporation tax bear interest at only 1.5%.

Repayment supplement

Interest on all overpaid tax is payable at the same rate.

The formula is Bank base rate minus 1% but with an overriding minimum of 0.5% which applies at the present time.

Official rate of interest

To 6 April 2014: 4%

To 6 April 2015: 3.25%

From 6 April 2015: 3%

Non Dom Taxation

The draft legislation for the new non-dom rules relating to Inheritance Tax was published late last year and HMRC have now issued the draft legislation in respect of income tax and capital gains tax.

The general idea is now well-known that non-domiciled individuals who become deemed domiciled in the UK under the new tests will be taxed in pretty much the same way as UK domiciled individuals. The new draft clause and draft schedule give effect to this intention. However, there are some complications.

Where a UK domiciled individual establishes a non-resident settlement in which he has an interest, an amount equal to the capital gains which are made by the trust is automatically taxed on him by reason of section 86 TCGA 1992; he is not subject to the s.87 capital payments regime. The same treatment is going apply to anybody who is deemed UK domiciled – but only in respect of any settlements established (during lifetime or on death) after 5th April 2017.

The rules relating to the location of foreign currency accounts are being similarly revised. For a person deemed domiciled in the UK, no relief will be available in respect of foreign currency accounts and the position will be exactly as it is for a UK domiciled individual.

There are also to be changes to the tests for determining the residence of a trust where the domicile of the settlor is relevant – and it is proposed that the rules for non-domiciled employees travel costs will in future correspond to those applicable to UK domiciled individuals.

Interestingly there is a relief for foreign chargeable gains accruing to an individual during a period of temporary non residence beginning before 8th July 2015. I am not sure of the thinking here, but I shall take it – and be appropriately grateful.

The transfer of assets abroad rules are being amended so that the individual who is deemed to be UK domiciled will be the same as an individual who is domiciled in the UK under the general law – that is to say the special remittance basis which is included within the transfer of assets abroad rules will no longer apply.

HMRC have made it tolerably clear that a settlor interested offshore trust established by an individual prior to becoming UK deemed domiciled will be protected so that the income and gains of the offshore trust will not automatically be taxed on the settlor. Only distributions will be charged to tax – but how (and at what rate) such tax will be chargeable remains a mystery. The latest announcement does not make it any clearer. They merely say that "these protections will be legislated in Finance Bill 2017". Stay tuned.

HMRC and Taxpayers

HMRC have taken the bold step of issuing a press release in an attempt to dispel some myths which have emerged in the media in recent months – not least about Google. I guess it may be helpful in limiting the amount of extraordinarily distorted reporting that has taken place – but I have my doubts. It goes on a bit but I thought that the following extracts were both interesting and important:

> a) The largest companies often pose big tax risks which is why we closely manage their compliance. Because of the tax at stake, their size and complexity, and the significant risks these businesses present to the Exchequer, this resource intensive approach is the most cost effective way of ensuring they pay the right amount of tax. At any given time, we have about two thirds of the UKs 800 largest businesses under investigation.
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> b) HMRC treat all taxpayers impartially. We apply the same approach to resolving all disputes, regardless of business size.
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> c) A definition of a permanent establishment is set by international treaty law. These rules are complex. Some media reports have suggested that HMRC did not look into Google's assertion that its Irish company did not have a permanent establishment in the UK.
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> d) It is wrong to suggest that HMRC does not take into account all relevant factors when making sure multinationals pay the tax due under the law. HMRC has taxed all of Googles profits chargeable to tax in the UK for the period in question at the full statutory rate of tax.
>
> e) Government Ministers are not informed of the progress of any tax enquiries and play no part in agreeing the amount of tax to be paid by any taxpayer. We only informed Ministers of the outcome of the Google enquiry after it was concluded and we only told them information that was in the public domain or what Google intended to make public.

These things badly need to be said – and all credit to HMRC for doing so.

Commercial Trades

The case of *Kevin Johnson v HMRC TC 4805* concerned a claim by Mr Johnson of a loss incurred in his business activities. It sounds a bit dull – but the case had some interesting features.

The published comments on this case have highlighted the parts of the decision which dealt with bartering but it seems to me there is a much more important issue to which I refer below. Anyway, the Tribunal went through the conventional analysis of how to define a trade adding that it is not limited to an activity in which money is received. They said that an activity of bartering is no less capable of being a trade than one in which barter is replaced by the exchange of money.

Mr Johnson became involved in tree surgery and undertook a number of assignments from November 2010. It seems that he was not paid for this work but he was able to take away for his own use several trailer loads of wood. Mr Johnson incurred various expenses including purchasing a chipper and a trailer.

The Tribunal found that in providing his services in return for the wood, Mr Johnson was providing his labour in return for a benefit and this was capable of being a trade.

The Tribunal went through the badges of trade and concluded that Mr Johnson was carrying on a trade and that the trade commenced in November 2010.

That sounded good for Mr Johnson but it was not the end of the matter because Section 66 ITA 2007 provides that relief for a trading loss is not available unless the trade is conducted on a commercial basis and with a view to the realisation of profits.

The Tribunal noted that in the first year 2010/11 the value of the wood received by Mr Johnson in return for his activities exceeded his expenditure. The Tribunal set out the net taxable profit and loss for 2010/11 showing the value of the income for the year at £1,500 and the allowable expenditure at £400. However, there was a further deduction – an investment allowance on the chipper and trailer of £5,000 which turned the profit of £1,100 into a loss of approximately £4,000.

Given that the profit or loss has to be calculated on generally accepted accounting principles one might wonder why the results of Mr Johnson's business was not a profit of £1,100 because the annual investment allowance is a capital allowance in respect of capital expenditure. That does not turn his profit into a loss – it merely means that he is entitled to capital allowances. It would seem that HMRC were concluding that because he made a loss claim, this must be the loss he made in his business – but that would surely be wrong. On generally accepted accounting principles the business made a profit; the loss which he claimed was entirely the result of his entitlement to capital allowances.

The Tribunal had another argument which was that although in the first year his activities were beginning to deliver benefits and a flow of work was starting, his later success could not be relied on. It was a time of relative economic uncertainty and Mr Johnson had said to HMRC that it was a marked achievement to have managed to establish a business. The Tribunal concluded that because Mr Johnson actually succeeded did not mean that it was objectively reasonable to suppose that he would succeed. Accordingly, he could not have expected to have made a profit and therefore his activity was not commercial.

Wow – that is really tough. I wonder what would have happened if Mr Johnson had disclaimed his capital allowances to defer the benefit of the allowances until a later year. Would the profit he made on his trading been tax free because it was not objectively reasonable for him to expect to make a profit? Er, possibly not.

Taxpayers' Charter

HMRC have issued a new taxpayers Charter. It has attracted some criticism which I feel is rather unjustified. It is regrettably expressed in rather dumbed down phrases – not even sentences – but the same sentiments are still there, largely as they were in 1986 when the first Charter was published.

There is a lot of stuff about being polite and helpful to taxpayers – but they could hardly say anything else. We can all have examples of cases where things have not happened in accordance with this Charter – but a charter is not going to mean that everything happens as it should, any more than a law against bank robberies means that people will never rob banks. It is just a mission statement setting out how HMRC think things ought to be. That seems fair enough and I think the Charter seems sufficiently clear for the purpose.

In my view the single most important (non) sentence in the Charter is:

> "*Respect you and treat you as honest*" (see what I mean about the sentences)

This is explained as meaning:

> "*We'll presume that you are telling us the truth, unless we have good reason to think otherwise.*"

Just think how many questions you have had from HMRC in which they want support or evidence that what the client is saying is correct. Some of these questions may be justified on the basis that the client might be mistaken about something – but most of the time the sub-text is that they are not prepared to believe the client without corroboration. I think that such lines of enquiry might be open to challenge on the basis of the Charter.

Share Trading

The taxation of individuals who engage in share dealing has for many years been reasonably clear – although the underlying reasoning may have been difficult to follow.

Determining when a person is carrying on a trade can sometimes be a problem, but when somebody buys and sells assets of the same type, hundreds of times, making profits and losses there is normally little doubt that he is carrying on a trade. And, unless the trade carried is not conducted on a commercial basis, (like Kevin Johnson above, perhaps), he will be taxed on the profits and allowed relief for his losses.

Except, when it comes to buying and selling shares. We know this from *Salt v Chamberlain* [1979] STC 750 where the court held that the hundreds of share deals undertaken by the taxpayer did not amount to a trade – the High Court explaining there was presumption that an individual engaged in speculative dealings in securities was not carrying on a trade. (It would have been a trade if it was carried on by a company – that is abundantly clear from such cases as *Lewis Emanuel & Sons Ltd v White* 42 TC 369 and *Cooper v C & J Clark Ltd [1982] STC 335*).

However, we now have the case of *Akhtar Ali v HMRC TC 4816* which has reviewed the whole thing. Mr Ali did some serious share dealing involving thousands of transactions, which had all the hallmarks of trading – except of course that they were transactions in shares. Having regard to *Salt v Chamberlain* which has been the unchallenged authority for over 30 years, it is no surprise that HMRC claimed that he was not trading.

The Tribunal said that the main reason for the decision *Salt v Chamberlain* was that the transactions were more in the nature of gambling. The Tribunal therefore had to consider the circumstances of Mr Ali and whether his activities were so close to gambling as to be excluded from the definition of a trade. They concluded that Mr Ali's activities, his business plan and his organised scheme of profit making, meant that he was carrying on a trade of share dealing.

HMRC then sought to argue that his trading was uncommercial so that the losses would be disqualified from relief by reason of s.66 ITA 2007.

However, the Tribunal took the view that Mr Ali conducted his activities in a commercial manner – they were not undertaken in a manner of an amateur or dilletante but by a serious trader seriously interested in profit.

(Coincidentally this very point appeared yet again in the very next reported case of *Rowbotham v HMRC* TC 4817 where the taxpayer was involved in a boat chartering business – and where the lack of a business plan and other indicia of a serious trader seriously interested in profit seemed to be lacking. It makes for an interesting comparison.)

Peter Vaines
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Contact
Peter Vaines
Field Court Tax Chambers
3 Field Court
Gray's Inn
London WC1R 5EP

Tel: 020 3693 3700
pv@fieldtax.com
www.fieldtax.com