UK Tax Bulletin

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Latest Rates of Inflation and Interest

The following are the current rates at April 2016

Current Rates	
Retail Price Index: February 2016	261.1
Inflation Rate: February 2016	1.6%
Indexation factor from March 1982: to March 2016 to February 2016	 Not yet announced 2.273

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%

Field Court Tax Chambers

Panama Papers

I was going to leave this alone but all this business about the Panama Papers is driving me bonkers. Everybody is getting themselves worked up about the tax issues relating to funds deposited in Panama – but these revelations have got very little to do with tax. It is very unlikely that this money is put there to escape tax (such people are hardly likely to have been paying tax anyway), but to conceal the proceeds of crime, money laundering and corruption - on a biblical scale. Indeed, in the published list of people who had money in Panama, there is a whole section entitled "Organised Crime".

It never ceases to amaze me how in some countries, a perfectly ordinary person can be elected to high office and before very long is able to accumulate untold millions (or billions) of pounds without anybody really getting too fussed about it. And they obviously need to put it somewhere beyond the reach of the political opponent who will be along shortly.

Of course there will be some people who have deposited money in Panama for the purpose of evading tax and numerous tax authorities will now be having a field day. However, it is interesting that the focus has not been on those who have been hiding the proceeds of crime or corruption - but on people who have put their funds in Panama and have made the necessary disclosures to the tax authorities and paid all the proper taxes.

There are some serious issues to be addressed here because the Panama Papers clearly reveal something very bad – and being able to uncover the proceeds of crime and tax evasion (which of course is the same thing) so that those responsible can be brought to account is extremely important, even if we have to overlook the uncomfortable truth that the information was only made available by a criminal act. But for good to come out of this we must surely look in the right direction and not be distracted by manufactured quest for transparency which is little more than voyeurism or envy.

There is a clear case for transparency for funds kept in places like Panama – but that transparency should extend to the tax authorities (in connection with tax evasion) or to the security forces or the police, in connection with money laundering or the proceeds of crime. There is absolutely no case for anybody to have access to other people's personal affairs (and bank accounts) just because they are interested – or they think other people may be interested. If I want to install a camera in my neighbour's bedroom or bathroom, why should I be prevented from doing so? My neighbour may want privacy but that is too bad; I am interested and believe in transparency so I am entitled to invade her privacy. How can that possibly be right? I have no legitimate interest in anybody else's private financial or other affairs for which they are entitled to confidentiality.

I remember that there was once a right to privacy enshrined in Article 8 of the European Convention on Human Rights (and in the Human Rights Act 1996) and that this was generally thought to be a GOOD THING. Not any more it seems.

I think somebody is having a laugh with all these calls for transparency. Have you ever tried to help your elderly mother with her bank account? Not a chance; the bank will not speak to you. Data Protection Act they say. We cannot give you any information about her account. If you want the details you have to look in Wikipedia. I think the lunatics are clearly now running this asylum.

And now they are calling for politicians to disclose their tax returns. This is even more of a giraffe. If a politician has misappropriated £10bn and is hiding it in Panama, not even a moron in a hurry would think that the solution to such wrongs is for him to publish his tax returns. Or maybe they think the details will be in Box 73G: *Bribes and Proceeds of Crime: Please insert total received during the year.*

There is a much more important implication here. Of course we know that officers of HMRC are beyond reproach and all information provided to them is confidential and will remain so. We grow up knowing that and we can be confident that there is no risk in providing all relevant details of our financial affairs to HMRC. However, not all countries have this privilege. In some countries, such information is sold or leaked to organised (or not so organised) crime enabling them to cherry-pick the wealthiest citizens for fraud, theft, extortion or whatever else. Is it any surprise that people who have been brought up knowing that details of their wealth becoming widely known puts their family at a severe risk, will be a tad reluctant to agree to all this disclosure? The reality of the risk of having your child kidnapped will always trump any high minded ideas about transparency.

There is clearly a very serious issue here but the concern should be with bringing to account those who have broken the law. It is perverse for somebody to be vilified because he has some connection with Panamanian funds, but there is not the slightest suggestion of any wrong doing. We should be concentrating on pursuing those who have been involved in criminal activity (including tax evasion) rather than hounding people who have not.

Restricted Securities

In the recent case of *UBS and DB v HMRC* [2016] UKSC 13, the Supreme Court struck down a scheme involving restricted securities which was designed to avoid the payment of Income Tax on employees' bonuses. The issues were inevitably complex and one important element was the meaning of "restricted securities" in section 423 ITEPA 2003, about which the Supreme Court said:

> "Applying section 423 to the facts, viewed from a commercially realistic perspective, it follows that the condition to which the UBS shares were subject should be disregarded with the consequence that the shares are not "restricted securities" within the meaning of that section."

This followed a good deal of analysis of the Ramsay doctrine and a purposive construction of section 423. Their Lordships concluded that the introduction of commercially irrelevant conditions whose only purpose was the obtaining of the exemption, should be disregarded.

The conclusion is interesting and it would be nice if it could work the other way round. I recall the position of poor Mr Finn (see *Finn v HMRC TC 3555*) who was denied EIS relief on some shares because he was not an original subscriber to the Memorandum of Association when the company was formed, an interpretation which meant that on a reorganisation, there was a condition for EIS relief which in reality could never be satisfied.

The Tribunal made reference to this interpretation making absolutely no sense, and that it was inconceivable to have been what Parliament intended.

In the light of the Supreme Court judgment, a taxpayer in a similar position might be able to say that if the construction makes no sense, has no commercial relevance and could not be what Parliament intended, a purposive construction should be available to assist the taxpayer. Or using the words of the Supreme Court, an appropriate purposive construction could be adopted to interpret the legislation in the light of the transaction that took place.

Maybe HMRC would agree to adopt such an approach. Or maybe they wouldn't.

Share Valuation (1)

The Supreme Court also provided some authoritative guidance on the issues to be considered when valuing restricted shares because having regard to their decision on the substantive issue, it was necessary to consider the value on which the employees should be taxed. Their Lordships decided that when valuing the shares, the conditions which must be disregarded in determining whether or not the shares were restricted securities, should not be disregarded for the purposes of assessing the value of the shares, because ordinary taxation principles require the tax to be based on their true value.

At first sight it would seem a bit odd for the restrictions attaching to these shares to be disregarded - so they are not restricted securities – but then for the employees to be taxed on the basis that they are restricted securities.

One might welcome this approach as clearly it is to the taxpayer's advantage. In reality, the shares were subject to restrictions, even if the restrictions had to be disregarded, and if the employees were to be chargeable to tax on a value which did not correspond with what they actually received, that would be a bit tough. However, a tough result does not usually stand in the way of anything – particularly in the context of a tax avoidance scheme. More importantly perhaps, what we are looking at here is the proper

construction of the statute – and that is something which should be undertaken without regard to who would benefit.

The answer would appear to be that the shares received by the employees had a value based on the actual terms on which they were issued; and that is the value on which they should be charged to tax. They may have been called restricted securities but the label does not matter. However, when it comes to section 423, there is a specific definition of restricted securities which applies for the purposes of the section - and the shares did not fall within that definition because, properly construed, the statute was not intended to apply to them.

Nevertheless, it is welcome that the taxpayers were able to be taxed only on the value they actually received and the idea that the valuation of the shares could be calculated on a different basis might prove useful in other circumstances.

Share Valuation (2)

Another share valuation point arose in a rather different context. In the case of *John Lewis v HMRC TC 5029*, Mr Lewis subscribed £100,000 for some shares in a trading company called iFind Media Limited. The question was whether he was entitled to a deduction under section 131 ITA 2007 when the company went bust – which it did, rather unfortunately, only two months after he subscribed for the shares.

HMRC not surprisingly suggested that the value of his shares at the date of his subscription was zero and therefore no loss arose. However, (and it shows how important contemporaneous evidence can be) although the company was in serious difficulties, there was a third party purchaser who was prepared to acquire a 51% stake for £75,000. This was a genuine offer and there were serious negotiations about how much the purchaser should pay and what percentage of the shares he should acquire. The prospective purchaser was adamant that he was prepared to pay £75,000 for 51% - and that was it. Anyway, for one reason or another, this never happened (mainly because the existing shareholders did not want to give up control) and the prospective purchaser went away. There was no alternative source of funds and the company went down shortly thereafter.

The Tribunal were impressed with this evidence and concluded that the shares were not valueless at the date of the subscription; they were clearly worth something and they therefore had to determine what that value was. Interestingly, they concluded that if £75,000 was the value of a 51% holding, then a 49% holding (which would have been what Mr Lewis was left with) would be worth somewhat less as it would be a minority holding. The Tribunal suggested that the 51% holding should benefit from a control premium of 10% so that a 49% holding would be worth £67,500 - and they knocked off another £7500 for uncertainties and ended up at £60,000. That was the measure of Mr Lewis's relief.

HMRC (and others) may be surprised at this conclusion and feel that a 51% shareholding is worth rather more than 10% greater than a 49% holding. Anyway, it may come in handy in a case where one is looking for a high value for a minority shareholding.

More difficult perhaps is the premise upon which this is based. Just because a purchaser was prepared to pay £75,000 for a 51% holding, this does not mean that the shares subscribed for by Mr Lewis was a 49% shareholding. It was not. He subscribed for a 99.9% shareholding. Accordingly, it could be said that if a 51% shareholding is worth £75,000, and assuming (for illustrative purposes only) a 25% discount from a pro rata value for a 51% holding, a 100% holding would be worth approximately £200,000 – assuming of course the £75,000 was injected.

The reasoning of the purchaser would seem to be that he valued the company at about £125,000 - so when he puts in his £75,000 it would then be worth £200,000. He would have 51% of the shares which on a pro rata basis would be worth £102,000 and after a 25% discount that comes to about £75,000.

On these grounds, one might argue that the starting point for the value of the 99.9% holding subscribed for by Mr Lewis would be something approaching £125,000 before any appropriate discounts are applied.

Mixed Partnerships

HMRC have recently announced a change in their practice regarding mixed partnerships and the application of the incorporation relief under s.162 TCGA 1992 where a business is transferred as a going concern to a company in exchange for shares. This new practice will operate from 30th April 2016.

The issue is not entirely straightforward as it refers to the situation where there is a mixed partnership (that is one which includes individuals and corporate members) and the business is transferred as a going concern to one of the existing corporate members in exchange for shares.

Hitherto, HMRC have accepted that relief under s.162 is available but they have now changed their mind. They explain that to satisfy the conditions of s.162 it is necessary for the whole of the assets of the business to be transferred to the company - but that in the context of a mixed partnership, this condition cannot be satisfied.

Section 59A(1) TCGA 1992 provides that any dealings by the LLP are treated as dealings by the members of the LLP. HMRC interpret this as meaning that where there is the transfer of the business of an LLP to an existing corporate member, s.162 cannot apply because the whole of the assets of the business would not be transferred. Some of the assets of the business would be treated as already owned by the corporate member.

The reasoning for this conclusion is derived from the Statement of Practice D12 which says that on a disposal of an asset by a partnership, each partner will be treated as disposing of

his fractional share of the asset.

One might have thought that the authority for such a change of view by HMRC should be rather more than "it does not accord with our Statement of Practice" which invests rather more authority to their Statement of Practice than may be appropriate. However, HMRC are not saying this is what the law is; they are merely saying that they are changing their practice which is obviously something they are perfectly entitled to do.

New DOTAS Hallmark

The new Financial Products hallmark for DOTAS is going to make your eyes water.

There are many people who are not involved in any kind of tax scheme, merely undertaking conventional tax planning techniques to which HMRC happily (well, almost happily) accept. All these marketed tax schemes with premium fees, confidentiality and transactions of byzantine complexity, were things dealt with by other people. However, they may need to think again.

DOTAS applies to notifiable arrangements with one of the prescribed hallmarks which might be expected to enable a person to obtain a tax advantage. The new financial product hallmark brings an enormous number of transactions within its scope.

The new hallmark is one that contains at least one specified financial product (which includes a loan or a share) and it would be reasonable to expect an informed observer to conclude that the arrangements might be expected to give rise to a tax advantage (or contain contrived or abnormal steps).

The "informed observer" is a concept which seems to be exclusively applicable to DOTAS. We used to have the man on the Clapham omnibus, then we had the moron in a hurry, more recently we had the intelligent businessman. Goodness knows what characteristics the informed observer is supposed to have. (I think the Office of Tax Simplification could do something useful here.)

Anyway, this new hallmark is unbelievably wide. It obviously includes arranging for a corporate bond (perhaps on a bona fide sale of a company) to be either a qualifying corporate bond or a non QCB depending upon the particular requirements – which of course will be tax driven. It will be specifically drafted for that purpose and include a term (such as a non-sterling redemption clause) and will be bang in the middle of this new hallmark.

How about arrangements to ensure that you have 5% of a company's shares (rather than 4%) or that you have a modest employment so that you qualify for Entrepreneurs Relief. A share is a financial product and there is at least one term which will be specifically included to ensure that the relief (and therefore the tax advantage) is obtained. End of.

And what about employee shares under the Employee Share Scheme. An ESS scheme has

to be deliberately drafted to include all the necessary conditions for the purpose of qualifying for the relief. That is clearly dead in the water.

This is obviously ridiculous. HRMC clearly realise that the provisions are too wide and specifically go out of their way to say that investing under the EIS or in a self-invested pension plan or an ISA will be excluded. But for the legislation to be so wide that these things are included in the first place just emphasises the unacceptable scope of these new provisions.

However, instead of making the legislation sensible they compound the absurdity by providing such things with a specific exemption. But they can't give an exemption for everything – not unless somebody does a lot of work and gives them a very long list, thereby adding to the absurdity - so there will be a whole load of completely benign commercial transactions which will be caught.

And of course if you have a notifiable arrangement under DOTAS you are liable for an Accelerated Payment Notice. An APN means that you have to pay tax up front, before any tax liability has been established – and worse, before HMRC have even considered the position at all. This is not an attractive prospect.

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