UK Tax Bulletin

March 2016

FIELD COURT TAX CHAMBERS

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Latest Rates of Inflation and Interest

The following are the current rates at March 2016

Current Rates	
Retail Price Index: February 2016	260.0
Inflation Rate: February 2016	1.3%
Indexation factor from March 1982: to January 2016 to February 2016	 2.258 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%

Budget: March 2016

There has been lots written about the Budget in the last two weeks – and you will be relieved that I am not going to add to it, at least not very much. However, one or two points did catch my eye.

There was only a single paragraph on the taxation of non doms – but just you wait; all those new rules have not gone away. They are all going to be in the Finance Bill next year as planned. Sand there was a surprise - see further below.

Entrepreneurs' Relief is a seriously valuable relief, but goodness me – the Chancellor cannot resist fiddling with it. Last year's changes are being abolished or revised this year because they we so ill-considered, and you can bet that this year's changes will need to be changed in due course. Why can't he just leave it alone. It worked – it did not need fixing. I fear that it has now been made so complicated that it will be a prime candidate for "simplification".

However, there is a nice (although not so new) Investors Relief providing a similar 10% rate of capital gains tax for investments of up to £10 million in unlisted shares in trading companies which are held for 3 years.

The Chancellor is even more obsessed with UK residential property, what with the swingeing SDLT charges (and surcharge), the ATED, the non-residents capital gains tax charge and the proposed inheritance tax hit. If that is not bad enough the reduced rate of capital gains tax will not apply to UK residential property. I fear he will not stop until this particular golden goose (or cash cow – or whatever metaphor you like) has been strangled to death. He may not like house prices going up – but he will like it even less when they go down.

Non Dom Taxation

There was practically nothing in the Budget regarding the taxation of non-doms – but there is plenty to look forward to later in the year – and in 2017.

However, there was a little something buried away in the Budget papers - just a single paragraph which contained the following sentence:

> *"Budget 2016 confirms that non-doms who become deemed domiciled in April 2017 can treat the cost base of their non-UK based assets as being the market value of that asset of 6th April 2017".*

This looks extremely helpful – I hope they mean it.

It may give the non dom an interesting choice. He could do nothing with his foreign assets and they will be rebased for CGT but they will then form part of his estate for IHT after April 2017 although perhaps protected by the spouse exemption. Or he can put them into a trust and get both a CGT uplift and IHT protection as settled excluded property – and a possibly a further income tax advantage going forward.

One of the important areas of uncertainty surrounds what is to happen to offshore trusts established by a person who subsequently becomes deemed domiciled by being resident in the UK for at least 15 years. The idea is that the offshore structure will be ring fenced and not subject to any tax unless and until distributions or benefits are made from the structure.

In principle that sounds fair enough except that unfortunately, nobody knows how those distributions are going to be taxed – as income, as capital or maybe neither but subject to a flat rate (although this seems to be increasingly unlikely). And what if the structure contains UK source income. At the moment, the UK non-dom settlor cannot claim the remittance basis in respect of UK source income which would be taxable on him anyway. However, HMRC say that the new rules for taxing offshore trusts of deemed doms will be apply "without reference to the income or gains arising in the offshore structure". No distinction between UK and foreign income there and that seems clear. But in discussions with the professional bodies, HMRC talk about a possible double charge in respect of UK source income distributed from the trust which has already been taxed on the settlor. This would suggest exactly the opposite conclusion. I think the answer is a resounding: Dunno.

We are told that we are going to get further information on this topic – but the only date which has been mentioned is December 2016. Stay tuned.

Non Residents CGT

One of the tedious features of the introduction of the Non-Residents Capital Gains Tax on the disposal of UK residential property is the reporting requirement.

We are all getting to grips with the idea that non-residents now pay Capital Gains Tax on the disposal of UK residential property but HMRC went rather overboard with the reporting obligations. There was a requirement to file a return in respect of every disposal even when there was no gain – which was pretty likely in respect of disposals made in 2015 because it is only the increase in value from April 2015 which is taxable.

A report of the disposal had to be made within 30 days of the conveyance unless the non-resident was already registered for self-assessment in which case he put it on his tax return in the normal way.

Earlier this month HMRC issued a statement to the effect that a tax return in respect of the disposal of a UK residential property by a non-resident will be optional (how quaint – making tax returns optional) where there is:

> *"a disposal of residential property on or after 6th April 2015 for no gain or loss - or the grant of a lease for no premium to an unconnected person in a bargain at arm's length".*

It is possible that this is intended to cover disposals which are treated by specific legislation as being transferred for consideration giving rise to neither a gain nor a loss – for example, a transfer between spouses or an intra group transfer – but I see no reason why these words should be interpreted so strictly. A disposal "for no gain or loss" can reasonably be interpreted as covering the situation where the sale price on the disposal was equal to the value in April 2015. I imagine that there are quite a lot of those.

Fortunately, this relaxation is backdated to 6th April 2015 so that anybody who has not filed a return for a disposal giving rise to no gain or loss will not face any penalties as a result of their failure to do so.

Non Monetary Benefits

I was interested to read in the Budget papers about the new rules for traders having to bring into account non-monetary items as trading receipts. It was interesting because I thought that was the positon anyway and I am having difficulty understanding why we suddenly need pages of new legislation on this subject.

The new rules provide that when calculating the profits of a trade in accordance with section 28 ITTOIA 2005 (and section 49 CTA 2009):

> *"an amount equal to the value of the money's worth is to be brought into account as a trading receipt if, had the transaction involved money, that amount would have been brought into account".*

Well yes. Surely that was always the position? That is what the court said in *Gold Coast Selection Trust Ltd v Humphrey* [1948] 30 TC 209. (Indeed, it may be remembered last month in the case of *Kevin Johnson*, the Tribunal confirmed that a bartering transaction gave rise to trading income.)

The HMRC Manuals indicate that they think so too: (see BIM 40051). Anyway I suppose there is no harm in putting the matter being doubt – but as they are always going on about the pressure on Parliamentary time, I wonder why they bothered with this. Maybe I am missing something here and that some devious tax scheme is being caught by these new rules, which has passed me by.

This is entirely different from the position where the trader receives a benefit which is not convertible into money (such as the provision of a non transferable holiday from a supplier or customer). Such a benefit does not represent money or money's worth and does not have to be brought into account as a trading receipt. There is nothing in the proposed new rules to affect this principle.

Entrepreneurs' Relief

The strict rules which apply for Entrepreneurs' Relief were illustrated this month by the case of *Castledine v HMRC* TC 4930.

One of the tests for Entrepreneurs' Relief is that the taxpayer must hold at least 5% of the ordinary share capital of the company – and Mr Castledine did so. However, for good commercial reasons to do with the management, the company created a few deferred shares. These shares had no rights to dividend, no votes and no realistic rights to participate in a winding up – well not until the other shareholders had received more that £20,000 trillion. Unfortunately, Mr Castledine did not have any of these deferred shares (and was not actually entitled to have any) and if they were treated as ordinary share capital, the issue of these shares caused his shareholding to fall marginally below 5%.

For the purposes of Entrepreneurs' Relief, a company's shares are ordinary share capital unless they only have a right to a dividend at a fixed rate but have no other right to share in the company's profits. Mr Castledine said, come on, you cannot count these shares – they are totally devoid of any rights to anything and cannot be regarded as share capital at all.

The Tribunal agreed with HMRC that the definition of ordinary share capital in section 989 Income Tax Act 2007 was clear; this definition has been in the tax legislation since 1938 and there was no doubt that deferred shares fell within the wording – so bad luck.

The taxpayer did not think that this conclusion fitted very well with the stamp duty case of *Arrowtown*. In that case the company issued some deferred shares for the purpose of bolstering the ordinary share capital to enable them to satisfy the tests for group relief. The Court said that the shares were issued simply for the purpose of claiming the stamp duty relief and should be disregarded.

Mr Castledine argued that the deferred shares in his case should be disregarded too – they were no more commercial than the shares in *Arrowtown*. It did not seem right that the issue of absolutely worthless deferred shares were disregarded in *Arrowtown* with the effect that the taxpayer was denied relief – and that in Castledine the issue of absolutely worthless deferred shares were not disregarded, with the effect that the taxpayer was denied relief.

The distinction may be that the shares in *Castledine* were issued for a genuine commercial purpose but there was no commercial purpose in *Arrowtown*. That sounds like a reason - except that the courts have specifically said that just because the shares were issued for a tax avoidance purpose, that is not a reason for them to be disregarded.

I wonder what would have happened if Mr Castledine had noticed that the issue of the deferred shares might cause this problem, and had subscribed for a handful of deferred shares for the sole tax purpose of restoring his 5% holding and his claim for Entrepreneurs' Relief. Might it have been suggested that the deferred shares which took him below the threshold should be treated as ordinary share capital but the deferred shares which enabled him the satisfy the test should be disregarded?

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