FIELD COURT TAX CHAMBERS

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Latest Rates of Inflation and Interest

The following are the current rates at June 2016

Current Rates	
Retail Price Index: May 2016	262.1
Inflation Rate: May 2016	1.4%
Indexation factor from March 1982:	
to May 2016	2.299
to April 2016	2.290

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%

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Non Dom Taxation

An area of widespread concern in connection with the non dom rules proposed for next year is that UK residential property will no longer be protected from inheritance tax if it is held by an offshore company.

At the present time, where a foreign domiciled individual holds shares in an offshore company, the shares are foreign assets and therefore excluded property for inheritance tax purposes, even though the company may contain valuable UK property. It is proposed that this protection will disappear on 6th April 2017. It is not clear how this protection will be denied – whether there will be a tracing provision to treat the UK property as being owned by the shareholder or whether the shares in the company will cease to qualify as excluded property – but we get the general idea.

This is going to be a very serious matter for the enormous number of overseas property investors who have been buying UK properties in offshore companies (frequently off-plan, as part of a package) for decades. They escape the ATED charge because of the commercial letting but they will not escape the Non Residents Capital Gains Tax charge. And now they will be exposed to inheritance tax. They can complain all they like about HMRC moving the goal posts but it won't do them any good.

Trustees are in a particularly difficult position. The trustees of a trust in (say) Hong Kong or Singapore may have an interest in a company which owns a UK property. They need to know that on 6th April 2017 they will be exposed to the ten year charge. One way or another, they will cease to be holding excluded property and will be treated as holding UK property which will be chargeable to inheritance tax at 6% on each tenth anniversary. Furthermore, if they were to make a distribution of the property out of the trust between ten year anniversaries, there would be an exit charge calculated on a proportionate basis.

This is not an intuitive charge – no trustee in a distant land would ever guess that such a charge would arise. It will come about by various deeming provisions under the UK rules and it is quite possible that the trustees would have no idea about it. What is worse, it may be imminent because the ten year charge would not arise after ten years – it arises by reference to the date the settlement was established. So a trust established in August 2007 may have a ten year charge in August 2017. I expect this may be an unwelcome surprise.

The trustees may be in even greater difficulty. They may be the shareholder of a holding company of a substantial international group – and way down amongst the various subsidiaries there may be a BVI company which has a UK residential property investment. The trustees may not be aware of the existence of this property; after all it would not be a decision for them whether a distant subsidiary invested in UK property – but they will be the ones who would be liable for the tax.

An even more difficult situation for trustees arises if the settlor becomes a returning non dom – that is a person who was born in the UK, with a UK domicile of origin and who had acquired a foreign domicile of choice but subsequently becomes UK resident. In these circumstances, after the first year, if the settlor is a beneficiary, he is likely to become fully chargeable to inheritance tax on the whole of the assets of the trust by reason of his reservation of benefit; none of the settled property will qualify as excluded property under the new rules. This liability will fall on the trustees – in addition to the ten year charge. The trustees would do well to stay aware of the movements of the settlor – and better still, confiscate his passport – if they want to avoid some serious liabilities.

Assuming that HMRC does not have a serious pang of conscience and decide that these rules really go a bit too far, this is an area where serious consideration needs to be given before next April so that any liabilities can be eliminated as far as possible.

I have said before that when the Treasury starts seeking to tax the foreign assets of foreign resident and foreign domiciled individuals (I think there are about 1 billion people in China who fall into that category) they will truly have gone mad. This looks like it is getting close.

Brexit Alert: Could it be possible that the Chancellor will decide that he has rather more pressing priorities than filling up the Finance Bill 2017 with all this? We can dream.

Termination Payments

Having regard to the insecure nature of an employment in the field of Association Football and the sometimes generous levels of remuneration, it is perhaps a surprise that tax cases involving termination payments for footballers do not arise more often.

There is of course the celebrated case of *Shilton v Wilmshurst* 64 TC 78 in which a termination payment was held to be chargeable to income tax but that was some time ago. Similar issues recently arose in the case of *Tottenham Hotspur Ltd v HMRC* TC5143 where a payment to a player in connection with the termination of his contract came under scrutiny. The club argued that the first £30,000 of the payment was tax free by reason of s.403 ITEPA 2003. However, it is perhaps the sign of the times that the income tax issue was much less important than the NIC liability.

As far as income tax is concerned, the question was whether the payment was "an emolument from the employment" and for NIC, whether it was "a profit derived from an employment".

The outcome of the case depended mainly on the Contract Law analysis and the arguments centred on whether the player received his payment pursuant to the terms of the contract, or whether it was a payment for compensation for breach of contract.

Where a payment (such as a termination payment, or a payment in lieu of notice) arises within the terms of the contract, it is always taxable as it is part of the rewards from the contract itself. HMRC argued that because the contract contained an express provision that it could be terminated by mutual consent, any such termination and resultant payment would therefore be taxable. The taxpayer claimed that it was a payment by way of compensation arising from a breach of the contract.

The Tribunal did not agree with either of the parties. They did not consider that the club was in breach of contract even though the club threatened to leave the player out of the squad and off the bench for two years. This did not involve a breach (or anticipatory breach) as there was no implied term that he should be considered for selection. Neither did the Tribunal consider that the provision for termination by mutual consent was relevant either. They made the keen observation that a contract can always be terminated or varied by mutual consent. Therefore, a clause permitting the parties to terminate the contract by mutual consent adds nothing to the rights of the parties.

There were various ways in which the club could have terminated the player's contract early but none of these circumstances applied. What happened was that the parties reached an agreement for the contract to be terminated and a sum was paid in consideration. The Tribunal held that a payment made as part of a mutual agreement to terminate an employment is not a payment "from the employment".

This was enough to cause the payment to fall outside the penalty area of NIC – and to secure the £30,000 exemption, although the balance of the payment was chargeable to income tax as earnings.

Discovery Assessments I

Two cases were recently released within days of each other on the subject of discovery assessments – one in the First Tier Tribunal, *Simon Miesegaes v HMRC* TC 5129 and another in the Upper Tribunal in *Pattullo v HMRC* [2016] UKUT 0270.

Both these cases dealt with the conventional arguments regarding what is a discovery – but a comparatively new concept was floated in both cases. That is the proposition that a discovery may become stale and therefore unable to support a discovery assessment if it is made after too long a delay.

Before dealing with that point (and without getting involved too deeply in the facts of these cases), it was interesting to note that in *Miesegaes* the Tribunal gave some consideration to what the hypothetical officer was expected to know, acknowledging that he is expected to understand the law as it relates to the facts disclosed by the taxpayer. However, I was

surprised to read their conclusion that if the matter was complex, even a full disclosure of the facts may not be enough.

This is very disturbing. I know I am always banging on about the absurdity which has enveloped the law on discovery assessments – and that the taxpayer can never satisfy the conditions because they have been interpreted and refined to such a degree of fantasy that makes it quite impossible for him to do so - but this seems to be yet another example. The idea that full disclosure of all the facts may not be enough to protect the taxpayer is surely going too far.

What on earth is the taxpayer supposed to do? It must be possible for him to be able to protect himself – nobody would suggest that Parliament intended to deny him any protection. It is no answer for HMRC to say "the law is too complex for us to allow you any protection." Who made the law complex for goodness sake.

Quite apart from anything else this seems to fly in the face of the very foundation of the discovery assessment rules explained by Park J in *Langham v Veltema*:

> "[Self Assessment] imposed new burdens on taxpayers by requiring them to submit fuller tax returns than had previously been required …. The new burdens were balanced by new protections for taxpayers who conscientiously comply with the system, in particular by new and tighter time limits on the power of the Revenue to make further tax assessments".

Until there is a sensible review of this subject, the most enormous care is necessary when looking at what needs to be disclosed (and by whom).

Discovery Assessments II

The other interesting issue arising from these cases is the argument that if HMRC make a discovery but wait too long before raising their discovery assessment, they should be debarred from doing so. Obviously they have to raise their discovery assessment within the relevant statutory time period – but the suggestion is that sometime before the expiry of the statutory time limit, HMRC could run out of time on the basis of staleness.

The First Tier Tribunal in *Miesegaes* said in clear terms that there is no concept of staleness of a discovery. A discovery can take place at any time, even before the enquiry window has closed, and the only time limitation for the making of the discovery assessment is the statutory time limit contained in section 34 TMA 1970.

However, the Upper Tribunal in *Pattullo* took rather a different view. They said that there is a need for the discovery to be acted upon while it remains fresh and this is something which arises from the natural meaning of s.29(1). The Upper Tribunal said in particular:

> "It would, to my mind, be absurd to contemplate that having made a discovery of the sort specified in s.29(1) HMRC could in effect just sit on it and do nothing for a number of years before making an assessment just before the end of the limitation period specified in s.34."

It is a pity that the Upper Tribunal provided no further guidance on this point. Indeed, the judge went on to say:

> "I do not think it would be helpful to try to define the possible circumstances in which a discovery would lose its freshness and be incapable of being used to justify making an assessment."

I would respectfully disagree. I think it would have been extremely helpful (and of great interest to taxpayers) if the Upper Tribunal had tried to define the circumstances in which a discovery would fatally lose its freshness.

As it happens, the discovery in *Pattullo* had not in fact become stale by the time the discovery assessment was made, so that the issue did not have to be taken further. Having regard to this clear conflict (and the uncertainty which now exists over the concept of staleness), this issue is bound to arise again before too long.

Residence

My inbox indicates that, after the momentous events of last week, some people are thinking that it may be preferable to avoid becoming UK resident and are studying the Statutory Residence Test (and counting their days) very carefully.

It would be wise not to get the day count wrong because a person who inadvertently becomes UK resident may find himself a bit stuck; it is miles more difficult to lose UK residence than it is to become resident here.

A person who comes to the UK as an *arriver* with only two UK ties (perhaps he has a place to live and he is working here for more than 40 days), will not be resident unless he spends more than 120 days here. So if he spends 110 days here, he will not be resident – so that's fine. Well, not quite. In the following year, he will have a third UK tie because he would have been here for more than 90 days in the previous year. Accordingly, his day count limit would go down from 120 to 90.

If he were to overlook this point and spend more than 90 days in the second year, he will become resident. He will not be able to correct the position by making sure he is in the UK for less than 90 days in the following year because he will then be a *leaver* and subject to the less generous day count table. Accordingly, he would not cease to be UK resident unless he is here for less than 46 days. This could make life a bit difficult.

What is worse, he would be subject to the deeming rule because he would have been resident in one of the last three years and will have three UK ties, so some of the days in which he is in the UK will be counted, even if he is not here at midnight. This will make the UK even more like Hotel California.

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