UK Tax Bulletin

July 2017

FIELD COURT TAX CHAMBERS

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Latest Rates of Inflation and Interest

The following are the current rates at June 2017

Current Rates	
Retail Price Index: June 2017	272.3
Inflation Rate: June 2017	3.5%
Indexation factor from March 1982: to June 2017 to May 2017	 2.428 2.420

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 2.75% from 23rd August 2016

There is one exception: Quarterly instalments of corporation tax bear interest at only 1.25% from 16th August 2016

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 6th April 2014: 4%

To 6th April 2015: 3.25%

To 6th April 2017: 3%

From 6th April 2017: 2.5%

Summer Finance Bill ?

Before Parliament rose for the summer recess, HMRC announced that the Summer Finance Bill will be introduced … in the autumn. Of course. They insist that there have been no policy changes and the provisions which were originally in the March Finance Bill will be included in the next Finance Bill.

HMRC also confirmed that the measures which had been announced as applying from 6th April 2017 will operate from that date and everybody should assume that they will apply as originally announced. And to be helpful, HMRC have issued some updated draft legislation.

The new draft clauses are virtually the same as the ones we had before – although they have confirmed that the cleansing of mixed funds provisions will also apply to pre-April 2008 accounts. This relief is getting increasingly complicated, but nobody will mind about that because it is such a valuable opportunity.

There is no reference to any relief or relaxation for those blameless taxpayers who have been caught up in all this chaos. However, it is said that "technical adjustments and additions to the versions contained in the March Bill will be made on introduction to ensure that they function as intended". Maybe this is code for saying that some kind of relief will be introduced - not least for those who have died in the meantime. Let us hope that the absence of any reference to *fairness* is not significant.

There are however numerous measures for which no updated legislation has been provided (one notable example being the proposed penalty for "enablers") but there is clearly an expectation that they will all be brought into the Finance (No 2) Bill when it is introduced in the autumn.

Unless of course they decide to have another General Election.

Employee Benefit Trusts

The decision of the Supreme Court in the case of *Rangers Football Club RFC 2012 Plc (in liquidation) v AG for Scotland [2017] UK SC 45* has now been published.

It may be remembered that (in broad terms) Rangers established an employee trust for the benefit of their players and other employees; payments were made to the EBT which subsequently made loans to the players. It was argued by Rangers that the loans did not represent earnings in the hands of the players, and therefore they were not subject to income tax and NIC, because they had no legal right to receive the payment. The FTT agreed, and so did the Upper Tribunal – but the Court of Session and now the Supreme Court have found in favour of HMRC.

The arguments have been the subject of considerable debate and uncertainty but this is no longer a matter of debate – it is the law. It is therefore idle to argue with the decision – any more than arguing with speed limits as you drive along the road. However, what is important is to identify what this decision means as far as other taxpayers are concerned.

Although there are suggestions that HMRC will seek to issue Follower Notices on the back of this decision, it is not at all clear (at least to me) that this case is of such wide application. However, section 204 FA 2014 enables HMRC to issue a Follower Notice (which is like an APN) if they are of the opinion that there is a judicial ruling which is relevant to the arrangements – and I guess that will be their view. The taxpayer would seem to have no defence (or redress) if their view is wrong.

Of course, everything changed in April 2011 when Part 7A ITEPA 2003 came into force but the loans in this case predated that legislation and the judgment is therefore relevant to the general principles.

The decision of the Court of Session was that the payments to the trustees were made at the direction of the footballers and this was central to the Supreme Court decision as well. The payments to the EBT were therefore taxable when they were made. Section 62 ITEPA 2003 does not require the remuneration to be received by the employee – payments made to a third party are equally taxable. (I thought that was always the case). So maybe there is no new principle here – but merely a question whether in fact the employee did redirect part of his earnings to the trustees of the EBT.

For that reason, this case might prove to be of rather more limited application than has been suggested. There will be many cases where payments have been made to a third party such as an EBT without necessarily the knowledge or consent of the employee, and without any assurance (or knowledge) that the employee might benefit from the EBT. It is difficult to say that a payment is made at somebody's direction if they did not know about it, consent to it, or benefit from it – at least until something else happened.

It is interesting to compare this analysis to the way in which benefits in kind are taxed If a payment is made by the employer to a third party, say for the provision of a car for the benefit of the employee, the amount paid is not taxed as earnings; the employee is subject to tax under the benefits code.

We know that the benefits code only applies to the extent that the benefit is not otherwise chargeable to tax as earnings. So why would the payment to the third party for the provision of a motor car not be taxable as earnings instead of as a benefit in kind. It is difficult to see why it should be treated differently from a payment to an EBT.

There must be a distinction, and therefore a limit on how far the reasoning in Rangers goes, because otherwise it would destroy the entire benefits code. Perhaps the difference arises from the facts of the case. If in fact the employees redirected their earnings to the EBT they were taxable the moment they were paid to the EBT. If we remove the redirection, maybe we are back to the benefits code.

I see a difficulty arising as a result of all this. There were lots of EBTs set up before 2011 and the view of HMRC was that the original payments to the EBTs were not earnings - but any payments out of the EBT after 2011 were chargeable under Part 7A. That was their published view and may be said to represent the prevailing view at the time. However, HMRC have now changed their stance and have successfully argued that the payments to the EBT were earnings and PAYE should have be applied. But they are out of time now. And if the payments to the EBT were earnings at the time, they cannot be charged to tax when they are paid out. That was a specific conclusion of the Court of Session.

This is clearly a most important case and it will be interesting to see just how far it goes when all the flurry has died down - and where it leaves the new provisions in FA 2017 which are intended to bring all outstanding loans into charge to tax on 5th April 2019. (I cannot resist the feeling that we could end up with a *Mansworth v Jelley* situation here).

Business Property Relief

Everybody will be familiar with Business Property Relief under section 105 IHTA 1984 which can represent an effective exemption from inheritance tax. There are terms and conditions which apply of course and in particular the relief will not apply if the business:

> *"consists wholly or mainly of one or more of the following, that is to say, dealing in securities stocks or shares, land or buildings or making or holding investments."*

Things are not looking good when it comes to the business of letting property. The Tribunals have consistently decided that the letting of property is a business which consists wholly or mainly in the making or holding of investments, no matter how extensive the services provided. There will be many taxpayers (and advisers) who take the perfectly reasonable view that they are carrying on a bona fide business and are not merely making or holding of investments. However, this is now a seriously uphill struggle.

The recent case of the *Executors of Marjorie Ross v HMRC TC 5959* seems almost to conclude the issue. Mrs Ross was a partner in a partnership which operated some holiday cottages; the cottages were let and loads of services were provided to the guests. The Tribunal acknowledged that a high level of services was provided to guests and these services were more extensive that those considered in any previous decision. This sounds encouraging.

However, it was irrelevant because in the view of the Tribunal the relief would not be available "however high the standard of services which were provided and whatever the level of expenditure incurred on those services".

The Tribunal denied relief on the grounds that the business of the partnership consisted mainly of investment in property. The fact that the business was run on sound business lines and with much effort, was not relevant.

I thought it would be significant that the Tribunal (and HMRC) accepted that the business was operated in partnership. The mere ownership of properties jointly is not a partnership under the Partnership Act 1890, so they must have been carrying on a genuine business – but that did not make any difference either.

Accounting Standards

The recent case of *Ball UK Holdings Ltd v HMRC TC 5920* highlights (or exposes) what may be an uncomfortable truth – that accounting standards are matters to be determined by lawyers and not by accountants.

The case concerned whether the company's accounts were in accordance with Generally Accepted Accounting Practice. The details do not really matter – at least not here. However, the principle is important because this is a statutory requirement for tax purposes under section 46 CTA 2009. FRS23 was the appropriate accounting standard and the company believed that their accounts were prepared in accordance of FRS23 and therefore complied with UK GAAP. HMRC said they did not.

The company had good grounds for their belief. PwC said so, Deloitte prepared a report which supported that view and there were two expert witnesses from KPMG on their side. You would have thought they were on pretty safe ground. Dream on.

The Tribunal did not agree with any of these accountants. They said that "no accountant could reasonably have read FRS23 in that manner" which was an interesting point of view having regard to the wealth of highly experienced accountants who clearly did so.

The Tribunal went on to say that although a number of expert accountants had read FRS23 in that way(!), that did not mean it was in accordance with UK GAAP; they were all wrong.

It is difficult not to have sympathy for the taxpayer. They got some of the most prestigious accountants in the land to confirm that their accounts were prepared in accordance with UK GAAP, but their expert knowledge and experience was rejected by HMRC - and by the Tribunal.

It is of course right that when a dispute occurs, even on matters of accountancy, it is the courts which are the ultimate forum for adjudication. However, it is quite something when professional expertise on this scale is dismissed so comprehensively.

Criminal Finances Act 2017

The Criminal Finances Act 2017 was enacted on 27th April 2017 but the provisions do not come into force until 30th September 2017. It is a bit peripheral (I hope) but so serious that it deserves detailed consideration.

The Act creates new criminal offences for companies and partnerships (not individuals) who fail to prevent their staff from facilitating tax evasion.

The new criminal offence applies to corporations and partnerships who fail to prevent their associated persons (generally, their employees and agents – but also subsidiaries) from deliberately assisting tax evasion. It applies to UK tax evasion where UK taxes are criminally evaded and to foreign tax evasion where the conduct is criminal in the overseas jurisdiction and also in the UK. However, the conduct must have occurred in the UK and the relevant body must be incorporated in the UK, carry on business in the UK or the relevant associated person must be operating from the UK.

The conduct must be dishonest and deliberate. HMRC confirm that ignorance or negligence will not be enough to give rise to the offence.

This is said to be a strict liability offence (which is odd because the Act also provides a defence). It can give rise to an unlimited fine and enables the seizure and forfeiture of proceeds of crime.

Because this is a crime, HMRC has the full range of criminal procedures available to it, including notices under the Serious Organised Crime and Police Act 2005 – where the failure to answer questions is a criminal offence. This can be used to obtain information from people who are not under suspicion but have access to information desired by HMRC.

There are three stages which give rise to the offence:

Stage 1 – the taxpayer must criminally evade tax whether in the UK or overseas.

Stage 2 – the evasion must be criminally facilitated by the relevant body.

Stage 3 – the relevant body must have failed to prevent its associated person from criminally facilitating the evasion.

The offence is subject to a defence of reasonable prevention procedures. If the company can prove that it had in place reasonable prevention procedures designed to prevent its associated persons from facilitating tax evasion offences, it will be in the clear.

HMRC have published draft guidance on what they consider to be reasonable prevention procedures which are as follows:

1. Risk assessment
2. Proportionality of risk based prevention procedures
3. Top level commitment by senior management
4. Due diligence of the associates
5. Communication and training
6. Monitoring and review – and making improvements.

Nobody reading this Bulletin will be remotely involved in tax evasion – nor in advising others to evade tax. However, you might have a rogue employee (or employees) who perhaps view things differently and need to be prevented from doing so – which is where the procedures come in.

The Criminal Finances Act 2017 also provides an opportunity for the relevant authorities (which includes the NCA, HMRC, the DPP and the SFO) to obtain an Unexplained Wealth Order from the High Court to require those suspected of serious crime or corruption to explain their sources of wealth. (I thought HMRC were well able to do that anyway).

An order may be sought where there are reasonable grounds to suspect a Politically Exposed Person or a person who has been involved in serious crime (which includes money laundering) has property of more than £50,000 which cannot be explained by known sources.

This includes having control over the property, being a trustee of the property or a beneficiary or potential beneficiary of a trust with the property and also includes a wide class of connected person. The recipient has 60 days to explain, or HMRC or any of the other authorities can seek to "recover" it – in addition to other penalties such as a spell behind bars.

I wonder what they will do about those PEPS who have diplomatic or other immunity. And what happens if there is a difference of opinion regarding the adequacy of the explanation? Penalty first – trial later?

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