UK Tax Bulletin

December 2017

Field Court Tax Chambers

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Latest Rates of Inflation and Interest

The following are the current rates at November 2017

Current Rates	
Retail Price Index: November 2017	275.8
Inflation Rate: November 2017	3.9%
Indexation factor from March 1982:	
to October 2017	2.465
to November 2017	2.472

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% from 21st November 2017

There is one exception: Quarterly instalments of corporation tax bear interest at only 1.25% - but this was increased to 1.50% from 13th November 2017

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%

Partners Expenses

For those who are interested in this subject, I regret to say that the Court of Appeal have upheld the decision of the Upper Tribunal in favour of HMRC in the case of *Vaines v HMRC [2017] EWCA*. The decision will be published soon.

I am often critical of the conduct of HMRC, so it is only right that I should say that throughout this the case, everybody at (and representing) HMRC behaved impeccably and I have the highest praise for everybody involved.

It is a pity about the result. HMRC were never able to understand that my arguments were completely right and theirs were completely wrong. It's a mystery. But I suppose you can't have everything.

The reports of this case in the past have not always been accurate, so it may be helpful for me to explain the issues briefly.

A payment was made, not to discharge any debt or obligation, but to cause a disputed claim to go way. It was made by the taxpayer for the preservation of his trade or profession. A deduction was therefore claimed from his professional income on the authority of *McKnight v Sheppard (1999) UKHL 6.*

However, in order for the taxpayer to claim a deduction, we all know that the expenditure must be laid out for the purposes of the taxpayer's trade or profession. HMRC argued (and the Court agreed) that a partner in a professional firm does not carrying on a trade or profession himself. The trade is carried on by the partners collectively and not by the partner himself – so if he is not carrying on a trade, he obviously cannot have a deduction, even for the clearest business expenditure.

I will not trouble to set out all my arguments because despite my success in the First Tier Tribunal, the arguments were not accepted by the Court of Appeal (and therefore must be wrong). However, it is interesting to note that the Office of Tax Simplification recommended changes in the system of partnership taxation which will deal with this issue and that should be coming along soon – in fact, very soon.

Finance Bill 2018

It doesn't stop. If you were hoping for a bit of a rest after the Finance (No 2) Act 2017 was enacted on 16th November, you are going to be disappointed. The Finance Bill 2018 was published on 1st December.

This Bill includes a whole load of new provisions some of which deal with:

- the taxation of partnerships, including the determination of the amount of profit of each partner for tax purposes. (Well, that did not take long.)

- preventing the washing out of the income and gains of offshore trusts so that distributions or benefits to non residents do not reduce the pool of income and gains able to be taxed on UK residents.

- the relief from SDLT for first time buyers on properties up to £500,000.

- the freezing of indexation relief in calculating a company's chargeable gains at December 2017. Assets acquired from 1 January 2018 will not attract any indexation relief.

- further provisions to strengthen the charge to tax on loans from EBTs which remain outstanding at 6th April 2019.

Penalties

It may be remembered that I went off on one earlier in the year following the case of *Kaczmarczyk v HMRC TC 5744* when HMRC claimed that they could send tax returns to people who had no UK tax liabilities and impose serious penalties for not submitting them. The Tribunal upheld their view – and the penalties.

Mr Kaczmarczyk was resident in the UK but I am aware from personal experience that HMRC believe they are entitled to send tax returns to non residents with no income chargeable to UK tax and to impose penalties just the same. (This would seem to include the entire population of the Yemen, Peru, Brazil and so on).

I suggested that this was perhaps a questionable view (I think "bonkers" was the shorthand) and that that there must surely be another interpretation.

With this in mind I read the recent case of *Jiminez v FTT and HMRC [2017] EWHC 2585* (Admin) where Charles J held that a Schedule 36 information notice issued to a person resident in Dubai was unlawful because it was issued to a person outside the jurisdiction.

It is interesting to compare the reasoning here with the reasoning in the recent charity case of *Routier* (which was explained in detail in October). In that case, HMRC sought to deny tax reliefs for overseas charities on the grounds that had no way of obtaining information about the charity. And here they are arguing that they are entitled to issue information notices under Schedule 36 to people overseas. We deserve better than this.

His Lordship explained some general rules about territoriality – broadly, that (unless the contrary is expressly enacted or plainly implied) there is a presumption that Parliament does not enact statutes to operate on its subjects beyond the territorial limits of the UK.

There seems to be no reason why this analysis should not apply equally to section 8 TMA 1970 in connection with tax returns, which would avoid the absurdity referred to above. Let us hope so.

It must be acknowledged that HMRC have a genuine interest in identifying UK tax liabilities of persons who are not in the jurisdiction, and they need information to assist them. However, a Schedule 36 notice is not the way to do it.

Requirement to Correct: Reliance on Advisors

The Finance (No 2) Act 2017 has enacted the provisions relating to the Requirement to Correct and makes serious inroads to the defence of reasonable excuse where the taxpayer is relying on a professional advisor. This will almost certainly require offshore arrangements to be reviewed, if a penalty is to be avoided.

This new obligation applies in respect of undeclared offshore income and gains for years up to 2016/17. There is an opportunity to come clean before 1 October 2018 and accept a reduced penalty – and failure to do so exposes the taxpayer to eye watering penalties of up to 200% of the tax (plus the tax and the interest of course). This dovetails with the Worldwide Disclosure Facility which runs out on 30th September 2018.

A penalty of 200% of the tax may seem excessive, and possibly be capable of being struck down as disproportionate, but I would doubt it. The failure to declare offshore income deliberately in order to evade tax is a crime, deserving of a serious penalty – much more so if the defaulter has repeatedly ignored warnings and opportunities to disclose the income and gains which have previously been concealed.

However, the penalties will not arise where the taxpayer has a reasonable excuse. One such excuse (which I have mentioned many times before) is that he was acting on professional advice. This excuse has been refined a bit – but it is still generally a good one, even if the advice was wrong. Not any more – at least not for this purpose.

For reliance on professional advice to be a defence to these penalties, the advice must be given by a professional advisor who:

- is an independent advisor with appropriate tax expertise
- has no connection with the arrangements which did not work
- did not participate in the arrangements himself
- did not facilitate the involvement of the taxpayer in the arrangements
- advised the specific taxpayer (not somebody else, or generically)
- took proper account of the specific taxpayer's individual circumstances

It would therefore be a wise precaution to ensure that advice relating to the disclosure of offshore arrangements are reviewed by an appropriate expert who has no connection with the arrangements. That would not protect the taxpayer from the tax (or interest) if the arrangements do not work as intended – but it could save him from the 200% penalty.

GAAR Panel Opinion

The GAAR Panel have published their opinion on a new case which has been referred to them by HMRC. I fear that it may prove to be of considerable importance.

In very broad terms the taxpayer managed to get £500,000 out of his company without it being chargeable to tax as a benefit in kind, as a loan to a participator or as a dividend.

The GAAR Panel concluded that entering into these arrangements was not a reasonable course of action thereby giving HMRC grounds for seeking to counteract the tax advantage.

One unsatisfactory feature of opinions by the GAAR Panel is that in the GAAR Guidance they make a big thing about the importance of the Taxpayers Safeguard being the double reasonableness test: "*the arrangements cannot reasonably be regarded as a reasonable course of action*" and that this test exists specifically to set a high threshold.

It is a pity therefore that when it comes to the GAAR Panel, they do not have to apply this high threshold. They merely have to decide whether the arrangements are a reasonable course of action. As the Guidance is supposed to be taken into account in reaching the relevant conclusions, one might ask why the Panel are not obliged to honour the express taxpayers safeguard.

I would respectfully suggest that the Opinion in the (anonymous) case is a bit short on analysis. They look at the principles of the legislation and conclude that the principle was to charge tax on benefits received by a participator in a close company. That is surely a little too broad. There are three different ways in which the legislation imposes a charge to tax on benefits to participators. It is reasonable (to say the least) that if your arrangements do not fall within the scope of this detailed legislation, then they were not intended to be taxed.

The GAAR legislation provides an answer here which is that the taxpayer is not permitted to exploit shortcomings in the legislation. Indeed, the Guidance says that one of the basic purposes of the GAAR is to deter or counteract the deliberate exploitation of shortcomings in the legislation. It was therefore interesting to read the following passage in the Opinion:

> "*We do not consider there to be a shortcoming in any of the three separate sets of rules charging tax on benefits conferred by close companies*"

This sounds like the taxpayer was in the clear – but unfortunately not. The thrust of the Opinion seems to be that if he could have received this money in a different way which would have given him a (huge) liability to tax, like a dividend, he should pay tax on that basis. It does not matter that he followed the legislation which said it was not taxable – nor that he did not exploit any shortcoming in the legislation.

The legislation and the Guidance are pretty clear about the meaning of "exploit" in this context; it is deliberately to take advantage of loopholes and shortcomings in the legislation. The Panel seem to have extended the meaning of "exploit "so that it no longer merely applies to loopholes or shortcomings in the legislation – it means that you have "exploited the fact" that the legislation was not designed to tax your transaction. This would seem to cover absolutely everything.

It may be wondered what protection or safeguard now exists for the taxpayer. Obeying the law does not protect him – even if it was designed to do so. Following the Guidance does not protect him either. (I scan the horizon daily for sight of the Four Horsemen.)

However, we can winge all we like, but if this is the law – and it is how the State is going to extract tax from its citizens - it is important to be aware of it.

An Opinion of the GAAR Panel is not binding but it will be a brave (or seriously aggrieved) taxpayer who will be prepared to challenge it.

However, as the penalties for doing something that the GAAR Panel considers to be unreasonable are now 60% of the tax (and the advisors involved may also have to pay a penalty equal to the amount of their fees), it might not be long before a vigorous challenge will arise.

Spring Statement

It may be remembered that we used to have a Budget in the spring - and later in the year there was an Autumn Statement.

Mr Hammond decided to do away with all that and said that we will only have only one major fiscal event each year and it will be in the Autumn.

So I read with interest that we are going to have a Spring Statement on 13th March 2018.

Yes - we used to have a Spring Budget and an Autumn Statement. Now we have a completely different system of having an Autumn Budget and a Spring Statement. I don't want to be rude, particularly during the season of goodwill, but …………

Happy Christmas

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22nd December 2017

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