UK Tax Bulletin

January 2020

FIELD COURT TAX CHAMBERS

Contents January 2020

Current Rates..The latest rates of inflation and interest

Crypto Assets …………........……... Where are these assets located for CGT and IHT

Transactions in Securities …………………………...The motive defence explained

CGT: Payment date………………………...……...... New filing and payment dates

CGT: Losses on Off-Plan Property………..…The rights to the properties are assets

Penalties: Automatic Notices……………..…Automatically issued notices are valid

Entrepreneurs Relief……………………………………..The meaning of substantial

Latest Rates of Inflation and Interest

The following are the latest rates:

Current Rates	
Retail Price Index: December 2019 November 2019	291.9 291.0
Inflation Rate: December 2019 November 2019	2.2% 2..2%
Indexation factor from March 1982: Frozen at December 2017	 2.501

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 3.25% from 21st August 2018

There is one exception: Quarterly instalments of corporation tax bear interest at only 1.75% from 13th August 2018

Repayment supplement

Interest on overpaid tax is payable at the same rate from 21st August 2018

The formula is Bank base rate minus 1% but with an overriding minimum of 0.5% which applies at the present time.

Except IHT where the rate is 0.50%

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%

Crypto assets

I mentioned in the November Bulletin that HMRC had published details about how crypto assets are to be treated for the purposes of income tax and capital gains tax. They have now provided further information about their views on where crypto assets should be located which is relevant for capital gains tax and inheritance tax.

No news yet about how HMRC can find out about them in the absence of voluntary disclosure by the taxpayer, but I am sure that will be forthcoming in due course.

The approach adopted by HMRC is that crypto assets will be treated as located in the UK if the beneficial owner is resident in the UK. So, no protection for non doms.

They say that this treatment will apply only to exchange tokens and not to other types of crypto assets (don't ask).

This is all a bit difficult because there is no law on the subject – these are just the views of HMRC. The best they can say is that a residence basis most accurately fits the majority of transactions. They might be right – but maybe not. It is going to be interesting when a dispute arises.

This looks like an excessively pragmatic conclusion. The crypto asset is obviously not actually in the UK (goodness knows where it is – although clearly not here) but the person who possesses the access code is in the UK so he is therefore taxable on this UK situs asset. Um.?

I wonder if this reasoning applies to my safety deposit box in Switzerland where (confidentially, just between us) I secrete items of staggering value. I carry the key on my person – or I memorise the number. If I am resident in the UK does that mean the contents of the safety deposit box is a UK asset? I don't think so.

Transactions in Securities

One of the difficulties involved in claiming relief or undertaking a transaction is that you are sometimes faced with a motive test – that is to say, the relief you are claiming, or the tax treatment you are expecting, will be denied if its main purpose was the avoidance of tax.

Unfortunately, not all the motive tests are the same (why on earth not, would be a very good question) and although they do not all have the same meaning, there is a broad theme – there must be an intention to avoid tax.

Nowhere is this more important than in the Transactions in Securities legislation in section 682 et seq Income Tax Act 2007 which can effectively turn a capital receipt on which the tax might be 10% (or maybe zero) into an income receipt chargeable to income tax at somewhat higher rates.

Section 684 provides that these provisions will not apply if:

> "the main purpose or one of the main purposes of the transaction in securities … is to obtain an income tax advantage"

The application of this motive test was examined in the recent case of *Assem Allam v HMRC TC 7532*. Dr Allam sold some shares in a company to another company under his control. This is the paradigm case of a transaction in securities. The issue was whether the main purpose or one of the main purposes of the transaction was to obtain an income tax advantage. Dr Allam was able to persuade the Tribunal that it was not.

Of course, the conclusion was inevitably special to its facts, but some of the arguments before the Tribunal are of much wider application.

A central element of the arguments of HMRC was that Dr Allam could have structured his transaction in a way which would have given rise to more tax – therefore he must have had the obtaining of an income tax advantage as one of his main purposes.

This is a horrific argument. Any course of action necessarily involves the rejection of all other alternative courses of action and their consequences (consciously or otherwise). I could have flown to Paris this morning instead of coming to work and I therefore avoided the air passenger duty on the flight. Should I therefore be charged the tax which I have avoided? And what about that new Porsche that I did not buy and the £25000 tax which would have arisen on the purchase. Or what about the 100 new Porsches I did not buy ….

This is obviously bonkers, but it is not a new argument – and the argument does not get any better by being repeated. Anyway, the Tribunal rejected it – which is helpful because it clearly has a significance to other taxing provisions where a tax avoidance motive is relevant.

The Tribunal referred to the celebrated case of IRC v Brebner [1967] 2 AC 18 in which it was said:

> "When the question of carrying out a general commercial transaction, as this was, is reviewed, the fact that there are two ways of carrying it out – one by paying the maximum amount of tax the other paying no or much less tax – it would be quite wrong as a necessary consequence to draw the inference that in adopting the latter course one of the main objects is for the purposes of the section the avoidance of tax."

I had thought that the developments in the law relating to tax avoidance since 1967 had meant that Brebner had kind of got lost, so it is a comfort to see this principle confirmed.

CGT: Payment date

On 6th April 2020 the new rules come into force concerning the reporting and payment of capital gains tax on the disposal of UK residential property. Thereafter, a new online return must be filed together with a payment on account of the capital gains tax, within 30 days of completion. (This is all quite separate from the continuing obligations on non residents and the NRCGT returns).

This is going to involve some neat footwork to calculate the capital gains tax on time. There are special rules to deal with losses, and assumptions about the income levels likely in the current year. However, unlike the position with non residents, no new return will be required if there is no tax payable on the disposal.

HMRC have confirmed that these new rules only apply to gains arising on disposals after 5th April 2020. The relevant date for disposal will be the normal rule in Section 28 TCGA 1992 – that is the date of exchange of contracts where the contracts are unconditional or the date when a conditional contract becomes unconditional.

Disposals of UK residential property prior to the end of this tax year are to be disclosed in the 2019/20 self-assessment returns in the normal way.

I suppose we will get used to it – but I can see a whole new series of appeals to the FTT in respect of penalties arising under these new rules.

CGT: Losses on Off-Plan Property

A recent case hit the headlines regarding a loss made by Lord and Lady Lloyd-Webber who entered into contracts to buy two villas in a proposed development in Barbados. The developers got into difficulties and in the end, Lord and Lady Lloyd-Webber were unable to recover the amounts they had paid which amounted to approximately £6 million. (No information, or press comment, seems to be available in respect of other investors in this development who must similarly have lost significant amounts of money).

Lord and Lady Lloyd-Webber claimed this £6 million as a capital loss against their other capital gains but HMRC disallowed the loss on the grounds that the money was spent on an asset which was never acquired. The only asset that the taxpayers acquired were the rights under the contracts.

HMRC argued that the rights under the contracts were not assets for CGT purposes. This followed the decision of the Upper Tribunal in *Hardy v HMRC [2016] UKUT 0332* which held that the taxpayer did not acquire an asset when he paid a deposit to buy a property which was never acquired. However, during the course of the hearing both parties agreed that *Hardy* was wrongly decided.

The taxpayers argued that they were entitled to relief as they satisfied section 38 TCGA 1992; they incurred expenditure on the acquisition of the rights and those rights were an asset for capital gains tax purposes. When those rights were disposed of or became of negligible value, a loss on that asset crystallised.

However, HMRC argued that the payments were made to acquire an estate in land which was the ultimate subject matter of the contracts, and not for the purposes of acquiring the contractual rights as distinct assets.

The Tribunal concluded that although Lord and Lady Lloyd-Webber entered into the contracts with the intention of ultimately acquiring the completed villas, the payments under the contracts were for the acquisition of contractual rights, the only assets they actually acquired. They made a loss on those assets and accordingly, the losses were allowed.

This has been referred to as a triumph for common sense, but I would suggest that, more significantly, it is a triumph of a sound legal analysis.

FIELD COURT TAX CHAMBERS

Penalties: Automatic Notices

Last year there was a series of decisions by the First Tier Tribunal to the effect that notices sent out automatically by HMRC were invalid – for example notices to file tax returns under section 8 TMA 1970.

One such example was the case of *Craig Shaw TC 6547* which decided that notices sent to taxpayers automatically by computer without any human intervention, did not satisfy the requirements for a valid notice under section 8. It followed that any penalties for failing to comply with such a notice was also invalid.

Having regard to the sheer volume of tax returns and other notices which need to be sent to taxpayers by HMRC, this decision was likely to cause severe logistical difficulties. It must be acknowledged that HMRC really ought to be entitled to send these things out automatically as that is the most obvious thing to do. However, at the moment, it may not be convenient, and it may not be very efficient, but if that is the law, HMRC need to abide by it, however irksome it may be.

HMRC complained that making individual decisions on individual cases is impractical and resource intensive. Well yes, but complying with the law is often resource intensive which is a factor experienced daily by taxpayers - and HMRC is never very sympathetic when the taxpayer fails to comply with the law.

Fortunately for HMRC, they have the opportunity to get the law changed if they find it inconvenient and they announced a little while ago that the next Finance Bill will provide authority for large scale automated processes to serve certain statutory notices However, this may have been overtaken by the Upper Tribunal's decision in *HMRC v Rogers and Shaw* [2019] UKUT 0406 in which the Upper Tribunal decided that the notices were valid after all.

HMRC were unable to provide evidence to establish that a specific identified HMRC officer took the decision to send the section 8 notices, but the Upper Tribunal decided that section 8 does not require a specific officer to be identified. There was sufficient evidence that HMRC officers had decided that a taxpayer should receive a section 8 notice, leaving the implementation of that decision to administrative staff (and presumably to computers).

Entrepreneurs Relief

There seem to be conflicting views about whether entrepreneurs relief is going to survive the Budget on 11th March. It is extraordinary that when entrepreneurs' relief was introduced in 2008 it was said to be a Good Thing, achieving a sound and worthwhile purpose. It is now thought to be a very Bad Thing and should be abolished.

It is possible that the Chancellor will grasp an underlying truth that those benefitting from the relief will have created significant businesses and generated loads of jobs, with the consequential flow of tax to HMRC of corporation tax, income tax, PAYE and NIC as well as VAT. However, we shall see.

It is not as if entrepreneurs relief has been unchanged for years. It is constantly being tinkered with and it is increasingly difficult to be sure whether the conditions will be satisfied in any particular case.

One of the problem areas arises in connection with shares in a trading company. We know what a trading company is – but for this relief, a trading company has a special definition. It means a company which carries on trading activities and whose activities "do not include to a substantial extent, activities other than trading activities". Section 165A(3) TCGA 1992.

HMRC have published guidance suggesting that non-trading activities are "substantial" if they amount to 20% or more of the activities of the company. The meaning of "substantial" has recently been considered by the Tribunal in the case of *Allam v HMRC* TC 7532. Interestingly, HMRC acknowledged that this 20% was simply intended as a rule of thumb and not a strict limit or threshold.

This is very welcome because this is a matter which has exercised the minds of taxpayers and advisers for some time.

The Tribunal took the view that to breach the "substantial" test, it is not necessary for the non-trading activities to predominate – but equally, there is no sanction in the legislation for the application of a strict numerical threshold. Nor is it permissible to substitute other tests (like those suggested by HMRC) for the test provided by the legislation. In the view of the Tribunal, "to a substantial extent" means that the non trading activities must have a material or real importance in the context of the activities of the company as a whole.

In the case of *Allam*, the non-trading activities were of such a size that the Tribunal had little hesitation in deciding that they were substantial – without unfortunately providing any other guidelines which may help us in the future, in cases where the issue is more finely balanced. However, the formulation they did provide is clearly an improvement.

Peter Vaines
Field Court Tax Chambers
31st January 2020

Contact
Peter Vaines
Field Court Tax Chambers
3 Field Court
Gray's Inn
London WC1R 5EP
Tel: 020 3693 3700
pv@fieldtax.com
www.fieldtax.com