UK Tax Bulletin

September 2012

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Latest Rates of Inflation and Interest

The following are the current rates at September 2012

Current Rates	September 2012
Retail Price Index: August 2012	243.0
Inflation Rate: August 2012	2.9%
Indexation factor from March 1982: to April 1998 to July 2012 to August 2012	 1.047 2.047 (not yet published)

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

From 6 April 2010: 4%

SQUIRE SANDERS

Finance Bill 2013

The Treasury have announced that a draft Finance Bill 2013 will be published on 11 December. They have been consulting on 35 subjects since the Budget in March. As we are particularly waiting for further details on a number of these subjects – not least the latest on the Annual Charge and other impositions relating to UK residential properties of more than £2 million, and the final version of the Statutory Residence Test – this could be interesting.

Delivery by Post

The Tribunal case of *Browns CTP Limited v HMRC TC 2244* sounds seriously boring. It concerns a penalty for late payment of PAYE which is enough to put anybody off, but it raises some interesting points. I hasten to add that my attention was drawn to this case because, sad as I may be, I try not to spend all the hours of darkness reading tax cases about PAYE penalties - and worse, finding them interesting.

Anyway, what happened was that *Browns CTP Limited* was late in paying its PAYE. Payments of PAYE are usually due on the 19th of the month and it was the company's practice to send a cheque on the 18th (or earlier if the due date fell on a Sunday). The cheques did not always arrive on the due date and HMRC charged a penalty. The question was whether the company had a reasonable excuse for late payment. In other words was it reasonable for the company to expect the letter to be delivered to HMRC the following day.

The offer and acceptance rules for the formation of a contract do not apply in these circumstances so payment cannot be regarded as having been made at the time of posting. The PAYE Regulations specifically refer to payments of PAYE being made by cheque and it is certainly implicit that the cheques would be sent to HMRC by post. However, Finance Act 2009 Schedule 56(16)(2)(b) which relate to penalties, provides that:

> "*Where [the taxpayer] relies on any other person to do anything, that is not a reasonable excuse unless [the taxpayer] took reasonable care to avoid the failure.*"

One might therefore conclude that if the taxpayer is relying on the postal service to deliver his cheque on time, he is out of luck because that would be reliance on a third party. However, the HMRC Manuals provide:

> "*If paying by post, your cheque payment must be posted early enough to reach HMRC no later than the 19th of the month. To allow for possible postal delays, for which we are not responsible, please allow at least three working days for the payment to reach us.*"

I think this means that to satisfy the requirements for reasonable care, the taxpayer has to do more than just address the letter correctly and affix the right stamp - he also has to post it 3 working days before the due date. But why? Where does this 3 days come from?

One might look at the Interpretation Act 1978. This says that in connection with service by post, service is deemed to be effected at the time in which a properly addressed letter would be delivered in the ordinary course of post. That does not get us very far except to move to a consideration of "*the ordinary course of* post".

Interestingly however, HMRC accepted in *Browns CTP Limited* that the ordinary course of first class post is delivery next day, excluding Sundays.

So if you send a cheque the day before and HMRC accept that you can reasonably expect it to be delivered in the ordinary course of post on the due day you would think that you would have a reasonable excuse if it does not arrive in time for reasons totally outside your control. Wrong. This would be unreasonable and you must be penalised.

It is extraordinary that despite going to all the trouble of taking the taxpayer to the Tribunal over this matter, HMRC did not address the Tribunal on any authorities or guidance in relation to this postal issue. It was therefore left to the Tribunal to do their own researches and come to their own conclusions.

They said it is necessary to identify the reasonable expectation of the taxpayer when sending payment. If he has a reasonable expectation that the payment will be received on or before the due date then he will have a reasonable excuse for non payment if it is not received. HMRC did not suggest any specific factors which would make reliance on next day delivery unreasonable.

The Tribunal said that if HMRC did not consider it reasonable to rely on next day delivery by first class post they should publicise that view in terms and the reasons for it. HMRC may well say that that is exactly what they have done by publishing a clear statement in the Manuals that the taxpayer should leave three working days. However, they give no reasons for this statement - which is hardly surprising if they acknowledge that next day delivery can be expected.

To make matters worse, and the stance of HMRC even less acceptable, cheques sent in payment of VAT one working day prior to the due date, are accepted by HMRC as posted in time. (*Halstead Motor Co v HMRC : 1995*).

At least for the moment the position is clear in respect of first class post - next day delivery can be expected and will be regarded as a reasonable excuse even if it does not arrive.

Stepping back and looking at the matter from a wider and perhaps more sensible perspective, one might ask what on earth is going on here. HMRC rightly say that postal delays are not their responsibility but they are certainly not the responsibility of the taxpayer. For HMRC to penalise people who act properly, reasonably and in good faith is something I would have thought they would do well to avoid.

Reasonable Excuse

It has been pretty well established in recent years that where an error has arisen in connection with a taxpayer’s affairs but the taxpayer has relied on the advice of a professional adviser, this does not represent negligence on the part of the taxpayer. The case of *Rowland SpC 548* sets out the position clearly and this is supported by the HMRC Manuals.

In the recent case of *Waseem Shakoor v HMRC TC 2208*, the Tribunal confirmed the general principle that if the advice of a professional is negligently provided, that negligence is not to be imputed to the taxpayer. The question is whether the taxpayer was negligent. He cannot be principally or vicariously liable for the negligence of his professional adviser.

However, there are limits – this is not a get out of jail free card.

In Waseem Shakoor, the issue involved the sale of a property which the taxpayer treated as exempt on the advice of his accountant. The Tribunal considered that the advice by the accountant was so obviously wrong that the taxpayer ought to have called for further explanation. It defied belief that he did not seek an explanation from his accountant to enquire why, or on what basis any exemption could be claimed. The Tribunal suggested that Mr Shakoor shut his eyes to what was or what ought reasonably to have been seen as incorrect advice and these were not circumstances in which he could therefore claim any protection.

Interest Paid

The case of *Garrett Paul Curran v HMRC TC 2194* provides an interesting review of the meaning of interest and its deductibility for tax purposes. The facts were comparatively straight forward. Mr Curran took out a loan for 30 years. He was naturally obliged to pay interest on this loan but the opportunity arose for him to pay the interest earlier than originally agreed at a discount to reflect early payment.

HMRC claimed that what Mr Curran paid was not interest – it was a payment in lieu of interest and therefore was a capital payment.

In a long judgment, the Tribunal examined the nature of interest, observing that there is no real statutory definition (only a circular definition as being "annual or yearly interest and interest other than annual interest). However, there are authorities of enormous weight to the effect that interest is a payment for the use of money or a payment received for the deprivation of money by reference to the period of deprivation.

It is not unusual to find debt and interest described in many different ways, wrapped up in instruments providing for discounts or premiums with a view to avoiding the payment (and receipt) of interest. HMRC are pretty alert to identifying receipts which have the character of payments for the use of money and charging them to tax as interest.

However, on the basis of this case, all those complications in re-categorising interest would be completely unnecessary. All that would be needed is for the taxpayer to pay the interest in advance and HMRC would have accepted it was a capital payment and not interest. Somehow I don't think so.

The Tribunal did not think so either. There was no doubt on the facts or the law that this was plainly a payment of interest and it is a surprise that HMRC argued to the contrary. Indeed you only have to consider the likely response had the taxpayer claimed that this was not a payment of interest but a capital payment (which would obviously not be taxable).

HMRC clearly did not want this payment treated as interest but even if it were interest, they did not want to allow a tax deduction for it. They sought to invoke Section 787 Taxes Act 1988 which denies relief:

> "*In respect of any payment of interest if a scheme has been effected or arrangements have been made (whether before or after the time when the payment is made) such that the sole or main benefit that might be expected to accrue to that person from the transaction under which the interest is paid was the obtaining of a reduction in tax liability by means of a deduction computing profits or gains or deduction or set off against income or total profits.*"

This provision is now found in Section 809ZG Income Tax Act 2007 but it says substantially the same thing. It is a powerful weapon for HMRC as it provides an objective test about whether "*the sole or main benefit that might be expected to accrue*" is a tax deduction. This is contrary to the normal test for deduction which relates to the subjective purpose of a taxpayer in incurring the expenditure.

It is mildly surprising that this formulation is not more widely used in the anti avoidance legislation. It is much more usual to see the phrase "*the purpose or one of the main purposes for which the transaction or transactions were effected*" which is the subjective test applicable to most anti avoidance provisions. This is particularly the case as the objective test goes back a long way, at least to the Finance Act 1944.

Although Mr Curran received tax relief for the interest sooner than he would otherwise have done, the Tribunal also took into account the non tax benefits to him of the early payment. Although the precise reasoning is a little difficult to follow, the Tribunal concluded that tax relief was not the sole or main benefit which might have been expected to accrue to Mr Curran – the non tax benefit outweighed the benefit of the interest relief and the anti avoidance section was not engaged.

Stamp Duty Land Tax - Sub Sales

An arrangement exploiting the sub sale relief has been successfully challenged by HMRC in the case of *Vardy Properties v HMRC TC 2242*. However the reasons for their success are comparatively unusual - and instructive.

It is perhaps unnecessary for me to get into all the details (it was a scheme after all) but a crucial (and successful) part of HMRC's argument is that one of the important steps in the arrangement, being a distribution in specie of the relevant property was unlawful as a matter of company law. A dividend had been declared involving a distribution of the property in specie but the terms of Section 270 Companies Act 1985 had not been satisfied thereby rendering the distribution unlawful. The inevitable effect of that conclusion was that the parent held the property on a constructive trust for the unlimited company and never had an entitlement to call for a conveyance of the property at any time - a crucial requirement for the sub sale relief.

In many ways, this looks a bit tough. No one can blame HMRC for insisting that all the transactions were lawful - indeed it is absolutely right for them to do so. It just highlights the need to consider all relevant areas of law when considering the tax analysis - after all, the tax consequences merely follow a proper legal analysis of the transactions.

The reason I say this looks a bit tough is that Section 270 sets out the various matters one needs to consider in determining whether a distribution may lawfully be made, such as profits, losses, assets, liabilities, provisions, share capital and reserves. However, in a case such as this where the company was formed specifically for the purpose, it could perhaps be said that the directors knew perfectly well all about the company, its profits, assets and liabilities without needing to go through a checklist. However the Tribunal considered that Section 270 required the production of an identifiable and contemporaneous single document which recorded the necessary details.

(I should not overlook to mention that there was a second line of argument which would have enabled HMRC to succeed anyway. The Tribunal found that the parent company did not acquire the property for no chargeable consideration but had provided the full consideration for the purchase.)

One cannot help thinking that with only a very slight variation in the facts, these arrangements may well have succeeded - although that may be a tad optimistic in the current climate.

Another sub sale case is presently under appeal to the Upper Tribunal (*DV3 RS Limited Partnership v HMRC*) and more information on this subject is likely to be forthcoming soon.

Restricted Securities

UBS has won a significant victory in the Upper Tribunal, regarding the issue of restricted securities for employees in a way which enabled the profit on the disposal to be regarded as capital gains, taxable at only 10% (by reason of taper relief) - and rather less tax for those employees who were not domiciled in the UK.

HMRC hit the arrangements head on. They said that the employees were entitled to bonuses before the shares were issued to them, they were not restricted securities, the arrangements were a sham and failing that, Ramsay applied to enable everything to be reconstructed as the simple provision of a fully taxable bonus in the UK.

The facts were desperately complicated and not of wide interest - except for the fact that the taxpayer succeeded on all counts (unlike the joined case of DB Group Services (UK) Ltd which went down on a technical issue over the meaning of control in Section 416 TA 1988). The Tribunal concluded that HMRC's arguments on Ramsay went beyond permissible limits, that the arrangements were real and not a sham and that the shares really were restricted securities. All of those issues were extensively analysed - and are well worth a read as they have an application way beyond the facts of this case.

However, having regard to the importance and sensitivity of the subject matter this case must surely go further.

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30 September 2012

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