SQUIRE SANDERS HAMMONDS | LEGAL COUNSEL WORLDWIDE

UNITED KINGDOM TAX BULLETIN

Squire, Sanders Hammonds

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CURRENT RATES	October 2011
Indexation	
Retail price index: September 2011	236.1
Inflation rate: September 2011	5.2%
Indexation factor from March 1982:	
to April 1998	1.047
to September 2011	(not yet published)
to August 2011	1.972

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%

Robert Gaines-Cooper : Supreme Court Judgment

The Supreme Court handed down their judgment in the case of Mr Gaines-Cooper on 19 October. It may be remembered that Mr Gaines-Cooper was seeking a judicial review of HMRC's refusal to regard him as non UK resident in accordance with their established practice in IR20. HMRC acknowledged that if Mr Gaines-Cooper satisfied the terms of IR20 they would be bound to honour it and treat him as not resident nor ordinarily resident. The Supreme Court decided that he did not do so.

The leading judgment was that of Lord Wilson which contained some interesting features.

Lord Wilson confirmed that to become non resident it is not necessary to sever your family and social ties. He made it absolutely clear that the test set out by the Court of Appeal is wrong – that severance of such ties is too strong a word. A distinct break is required and this only encompasses a substantial loosening of social and family ties. He pointed out that as a taxpayer is permitted to make limited visits to the UK, this clearly foreshadows the continued existence of family and social ties in a loosened form.

Whilst this is extremely helpful, because the idea of severing family and social ties was obviously excessive, we are no nearer clarity with a test that says you must "loosen" such ties. It would have helped to have some indication about the extent to which loosening is necessary.

Lord Wilson emphasised the need for a distinct break both for the strict legal position and for IR20. He suggests that a distinct break is an appropriate description for the necessary degree of change in the pattern of an individual's life if his settled or usual abode in the UK is to cease. A distinct break requires a multi factorial enquiry i.e. you need to look at all the facts. He was not impressed by the fact that the whole concept of distinct break does not and never has featured in IR20. In his judgment HMRC were right to say that leaving the UK requires a distinct break and therefore the meaning of IR20 corresponds with the general law. However, this leaves open the question that if IR20 corresponds with the general law, what is the point of IR20?

There are passages in Lord Wilson's judgment which may seem a little harsh. He criticises Mr Gaines-Cooper for not seeking advice from a tax office still less a ruling on residence when he left the UK. Mr Gaines-Cooper was advised by his father who was a tax officer with the Inland Revenue; he submitted all the relevant forms and responded to appropriate enquiries from HMRC. Some may think it would be reasonable to conclude that having made a claim to non residence in such circumstances, and having dealt with the reasonable enquiries from HMRC on the matter, if HMRC had any issue with his residence they would have said so – not wait for 20 years before contacting him again. For Mr Gaines-Cooper to be required to chase them is an obligation that some may feel is unreasonable.

The most important part of the judgment is the analysis of the key paragraphs of IR20. These are the paragraphs which say that HMRC will treat you as non resident if you leave the UK for the purposes of full time work abroad, or for a settled purpose or permanently or indefinitely for a period of more than 3 years. Providing you do not make visits to the UK of more than 90 days each year, you will be regarded as non resident.

Lord Wilson explains that you have to be extremely rigorous in your examination of IR20.

The taxpayer must understand that he was required to do more than take up residence abroad. This is a reference to the possibility that a person may be dually resident so he may become resident in another country without necessarily ceasing to be resident in the UK. This is clear from paragraph 1.4. However the taxpayer might have difficulty reaching this conclusion when reading paragraph 2 because it does not say HMRC will treat you as resident in the other country (leaving open the possibility that you may remain resident in the UK as well) – it says HMRC will treat you as being non resident, thereby excluding the possibility that you would be remaining resident in the UK.

The next point for the taxpayer to appreciate in paragraph 2 is that any subsequent returns to the UK are required to be no more than "visits". This is a reference to the day count test and the taxpayer must understand that when paragraph 2 talks about visits to the UK not exceeding 90 days, the word "visit" is very significant – it means that the periods of presence in the UK must have the character of a visitor. The significance of this term may have been missed by many people and that bears particularly harshly on the lay taxpayer.

The taxpayer must also understand that it is essential for him to relinquish his "usual residence in the UK". He should know this because of paragraph 2.1 of IR20 which says that you remain resident if you usually live in this country and only go abroad for short periods – for example on holiday or business trips. However, the taxpayer reading paragraph 2.1 will recognise that he is not going on holiday or on short business trips; he is leaving the UK to live somewhere else. It would be easy for him to draw the conclusion that paragraph 2.1 has no relevance to his circumstances. However, this would be an error. It is relevant – or at least part of it is; the bit referring to where you usually live.

Lord Wilson says that the ordinarily sophisticated taxpayer will surely have concluded that these general requirements demanded a multi factorial evaluation of his circumstances. Not all taxpayers may have readily reached that conclusion – but they know now. However, it is interesting that this multi factorial evaluation of the circumstances does not apply in the case of leaving the UK for full time work abroad. In those circumstances, no further enquiry is required – the full time employment is enough. It may be thought difficult for the ordinarily sophisticated taxpayer to understand why a multi factorial evaluation of his circumstances is required in some circumstances surrounding his departure but not others.

Interestingly, and disappointingly, Lord Wilson reveals that in the event that his analysis is wrong, IR20 would be so unclear as to communicate to its readers nothing to which legal effect could be given.

Whilst this judgment will be a severe disappointment to those involved and to taxpayers generally, the Supreme Court has spoken. This is the law and just like the batsman who wishes to challenge the umpire's decision, the response is the same: look in the scorebook. Nevertheless, although this may be the law, there will be a feeling of unease regarding the conclusion. As far as residence issues are concerned this may be short lived because we will soon have a statutory residence test, but the approach to HMRC statements has a much wider application.

IR20 is one of hundreds of statements of practice operated by HMRC and it is clear from Lord Wilson's judgment that they must be subject to the most rigorous examination. Furthermore, you would be unwise not to seek confirmation from HMRC that you have not missed any shade of meaning. To think that you can read a statement of practice which is in apparently clear terms and reach a conclusion (which you and your advisers consider is the only conclusion on the wording) would be seriously irresponsible now.

Discovery Assessments

I am always on the look out for cases which involve discovery assessments because the opportunity for HMRC to raise assessments out of time is obviously very important indeed. It will be remembered that the decision in *Langham v Veltema* gave HMRC pretty much unrestricted power to raise assessments without regard to the enquiry window. However the principles in that case have gradually been eroded in recent years to allow the taxpayer a reasonable degree of protection from discovery assessments out of time which was indeed one of the cornerstones of the self assessment system.

The recent case of *Admirals Locums v HMRC TC1416* was concerned with a loss relief claim made by a doctor who had been suspended from the GMC with the effect that he was unable to work as a doctor for a considerable period. He claimed for a loss in the trade during the period that he was trying to have his registration as a medical practitioner restored but he was not carrying on any trade during the period of his suspension and could not therefore have incurred a trading loss during those periods. For several years after he had ceased work he continued to claim loss relief in the trade and had disclosed his circumstances to HMRC. Although HMRC had not disallowed his claims in the past, that did not mean they were precluded from doing so once they realised their error.

However, having done so, they wanted to go back beyond the enquiry window on the basis of discovery but their application was denied by the Tribunal on the grounds that there had not been anything "newly arising" or "newly appeared" to them. The Tribunal observed that the main fact relied on by HMRC is that the taxpayer had no trade in the years in question. However this is something that the taxpayer had

made clear in the information provided to HMRC. Therefore there was no discovery because the relevant officer could have been reasonably expected on the basis of the information made available to him at the relevant time to be aware of this situation. It followed that there was no fraud or negligence on behalf of the Appellant allowing any further opportunity for discovery.

Whilst there was little or no merit in the taxpayers claim (he was not carrying on a trade, he was not entitled to loss relief and had relied too heavily on the fact that HMRC had not challenged him before) the fact remains that HMRC should have taken action within the specified time limit. If a taxpayer had failed to act in that way HMRC would have no sympathy so it is difficult to suggest that the rules should not apply equally to them.

Negligible Value : CGT

Section 24 Taxation of Chargeable Gains Act 1992 allows loss relief to be claimed on an asset which has become of negligible value even though the asset has not been disposed of. There is no definition of negligible value and therefore a degree of uncertainty about what it means, so the recent Tribunal case of Barker v HMRC TC 1487 may be helpful.

The Tribunal said that negligible value for this purpose means that the asset is worth next to nothing (but not nil). However that does not really take us much further. The best we previously had was a CCAB statement in 1971 which said that for Capital Gains Tax purposes, small could be defined as 5% and negligible would be considerably less.

However, this percentage formula has been rejected by the Tribunal who say that it is an absolute test, without regard to the previous value of the asset. So a £10 million asset which is now only worth £10,000 may well be negligible in comparison, but £10,000 is not negligible in absolute terms. That is helpful clarification bit it does not move us forward very much.

A more helpful way of approaching this matter emerged from the Tribunal – that the issue should be determined by reference, not to abstract calculations of market value, but simply whether the asset could sensibly have been sold. If for some reason (as in the case of Barker) on the balance of probabilities the shares were unsaleable on the relevant particular date then they would be regarded as of negligible value.

That gives us something to work on. It must be better than “next to nothing” which is just a phrase which will mean different things to different people. At least a sensible professional judgment can be made as to whether something is saleable.

A negligible value claim can be more valuable than it appears because it is not merely a means of establishing a capital loss. If the subject matter is shares in an unquoted trading company for which the taxpayer had subscribed, it is possible to obtain an income tax deduction under Section 133 Income Tax Act 2007 gaining relief at 50% which is obviously much better.

Foreign Properties

HMRC have announced the establishment of a new team to identify individuals who own land and property abroad. It sounds a bit intrusive but it is really no more than common sense. If you have bought a property abroad, HMRC will always want to enquire where you got the money if such a purchase would be inconsistent with their knowledge of your financial resources. Furthermore, a foreign property may give rise to rental income and there may be foreign bank accounts which could be the source of income or capital gains.

However, HMRC make it sound much more sinister with their references to a newly formed team who will use “new and innovative risk assessment techniques" and "sophisticated data mining techniques". Maybe they are just trying to get their message across.

Self Employed Substitutes

HMRC has had mixed results before the Courts on the distinction between employment and self-employment. One of the relevant factors in determining the status is the requirement for personal service. If the element of personal service is lacking there can be no contract of employment – and a right of substitution can therefore be very important because the ability to send somebody else to do the work is inconsistent with an employment relationship. However, the mere inclusion of a right of substitution has often been found inadequate – an example if the right was, in practical terms, unlikely ever to be exercised. Other issues such as the possible need to obtain the clients consent just complicates the position.

The issue recently rose in the context of agency workers and the effect of a right of substitution was analysed closely by the Upper Tribunal in Talentcore v HMRC UK UT 423. The conclusion was that if the worker had complete freedom to arrange for a substitute if he wished, even if did not actually do so, this represented an unfettered right of substitution which was inconsistent with a contract of employment.

I am afraid I have never been convinced by all this. It seems to me that where a genuine right of substitution exists there can be no employment. Even where a right of substitution does not exist the position can be no more than neutral and the relationship needs to be determined on other grounds. For example if I engage a famous pianist to play a piece of music at a concert, he can’t just send somebody

else on the grounds that they will both play the same notes. This is not acceptable, but to suggest that the inability to send the substitute makes him my employee is clearly going too far.

HMRC Advice : CAP 1

Having regard to the above, it is a coincidence that HMRC have now published CAP1 setting out the circumstances in which non-business taxpayers can obtain advice from HMRC on their interpretation of recent tax legislation. This is not the complete answer of course as it is restricted only to legislation passed in the last four years – although they do say they will give a view on earlier legislation where the subject or circumstances are not covered in their published guidance.

HMRC will respond in respect of a transaction which has already been undertaken or one which is proposed but they do expect you to have considered the published guidance first. If they consider that there is no genuine point of uncertainty, they will explain why and identify the relevant guidance.

They will not respond in respect of transactions which they feel are for the purpose of avoiding tax or simply to give tax planning advice or to approve a tax planning product.

You may not agree with their view and you can ignore it if you wish, but you do need to be careful that an appropriate disclosure is made in your Tax Return. You will by then have been made aware of HMRC taking a contrary view and it could be regarded as careless conduct to disregard it without explaining why – assuming of course that HMRC are found to be correct.

Peter Vaines
Squire, Sanders & Dempsey (UK) LLP
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Contact:

Peter Vaines
+44.20.7655.1780
peter.vaines@ssd.com

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