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UK Tax Bulletin

October 2013

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Introduction

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Latest Rates of Inflation and Interest

The following are the current rates at October 2013

Current Rates	October 2013
Retail Price Index: September 2013	251.9
Inflation Rate: September 2013	3.2%
Indexation factor from March 1982:	
to April 1998	1.047
to August 2013	Not yet published
to September 2013	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

Since 6 April 2010: 4%

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Annual Tax on Enveloped Dwellings

Today is the deadline for the payment of the Annual Tax on Enveloped Dwellings which applies mainly to companies owning UK properties worth more than £2million. Even if there is no tax to pay, you still had to send in a form at the beginning of this month if you are claiming one of the reliefs – for example, because the property is commercially let or is to be developed.

HMRC say that one of the policy objectives of the ATED is to encourage people to de-envelope their expensive properties presumably to avoid having to pay the tax. However, they are at the same time very anxious to stop people from avoiding the tax. So we have some new DOTAS regulations coming into force on 4 November for this enveloped charge. If anybody promotes an arrangement (containing the relevant hallmarks) whereby the liability to the charge is avoided or reduced by a transfer of the property, you have to make a notification to HMRC – unless it is one of the following four excluded arrangements:

1. The transfer is on such terms as would reasonably be expected to be agreed between unconnected persons.

2. The parties are members of the same group of companies.

3. The transfer is a distribution and the transferee is an individual or trustee who thereupon owns the property

4. The transfer constitutes a settlement.

An arrangement for this purpose is any scheme, transaction or series of transactions; that is going to cover most things - although I dare say there are transfers which come about otherwise than by reason of a transaction. However, whether it could also escape being a scheme is another matter.

There is an arguably more serious obstacle. The new rules provide that if the UK property is sold by an offshore company, the company is liable to capital gains tax at 28% but only on the increase in value since April 2013. That might not be such a big deal - but it does not wipe out the gain up to April 2013 which is still able to be attributed to (and taxed on) the UK resident shareholders under Section 13 TCGA 1992. That might be rather worse than the ATED charge.

There is also a bit of an issue about how the tax is paid. Typically the company which owns the property will have no other assets (and certainly no cash) so somebody else has to pay the tax. A payment by the occupier is not recommended because that could easily be a chargeable transfer for inheritance tax purposes. Indeed, if there is a trust involved in the structure, he could thereby become a settlor of that trust. Accordingly, somebody might prefer to provide money to the company by way of loan, or by additional share capital. That could be ok but it might mess up the shareholding and control issues relating to the company which could have seriously adverse effects.

This gets more and more complicated – and we have only just started.

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Health and Wellbeing Tax Plan

I just love the way they do this. HMRC have issued a statement called "The Health and Wellbeing Tax Plan". No carbs, no alcohol and lots of fresh fruit and down goes your tax liability. I don't think so. What it really means is that if you are a professional therapist (physical, alternative, or other – don't ask) and you have not disclosed all your income, HMRC will be after you in a big way. I suppose if you have not properly dealt with your tax affairs, it will be seriously bad for your financial wellbeing because HMRC will charge a penalty which will make your eyes water.

They do not quite put it that way. They say that they want to help those not paying the correct amount of tax, and to offer them the opportunity to do so.

Under this new disclosure plan the health professionals must come clean by 31 December 2013 and pay up by April 2014 if they are to receive sympathetic treatment by HMRC. Otherwise, the penalties will be heavy. There is also the prospect of prosecution and ending up on the published list of tax defaulters.

There is a new feature in this disclosure facility which is that the taxpayer is asked to suggest the appropriate penalty themselves. This will be interesting. The statement makes it clear that a penalty of at least 10% is expected, although they do acknowledge that no penalty at all may be appropriate in some circumstances – for example if the taxpayer has not been careless. However, it may not be easy to get HMRC to agree.

The statement includes a table which sets out a range of suggested penalties that HMRC have in mind in various circumstances. This includes no penalty in respect of the period from 6 April 2008 to 5 April 2012 where the taxpayer has sent HMRC a tax return showing less tax payable than the correct amount because they had been careless. I do not understand why such carelessness should be free of penalty but never mind.

HMRC also make it clear that if the taxpayer could have made the disclosure under any of the previous disclosure opportunities, they will find it hard to accept that the failures were not deliberate which means that the penalty is bound to be higher.

Costs

The case of *Roden v HMRC TC2911* sounds good but I fear it may have a sting in its tail. The taxpayer won his case before the First Tier Tribunal and sought costs against HMRC.

In general, no costs are awarded at the First Tier Tribunal unless the case is designated as complex – but even then the taxpayer can opt out of the costs regime. However, the Tribunal has power to award costs if one of the parties has acted unreasonably in bringing, defending or conducting the proceedings.

The Appellant's argued that HMRC should not have defended the appeal because their arguments were unsustainable. They therefore acted unreasonably and should pay costs.

The Tribunal said that if HMRC knew that their argument had no reasonable prospect of success they

would be acting unreasonably. In this case, taking into account HMRC's resources, they ought to have known that their arguments had no reasonable prospect of success so they were ordered to pay the taxpayers costs.

The Tribunal said that although there is nothing wrong in principle in taking novel points of law unsupported by authority, in this case HMRC acted unreasonably in defending the appeal based on a novel point of law which they ought to have known had no reasonable prospect of success.

Whilst rejoicing in the success of the taxpayer, I fear this may prove not be such a great result after all. When I think of all those penalty cases (which dominate the case reports) some of which are completely hopeless, there must be a real risk that they will be affected by this case. Nobody goes to the Tribunal to appeal against a penalty of a few pounds without a real sense of grievance and to be lumbered with costs as well would simply add to the feeling of injustice.

Although it must be a good thing for hopeless cases to be discouraged by the risk of costs, there is also the serious risk of this principle being extended to discourage those who do have a reasonable case – or at least believe in their arguments - but still lose. The weight of costs would of course bear much more heavily on the unrepresented citizen who seeks redress before the courts, than it would on HMRC.

Residence Guidance Note

HMRC have published a new Guidance Note on Residence, Domicile and the Remittance Basis entitled RDR1 (October 2013). It is a replacement for HMRC 6 (which replaced IR20) and explains HMRC views on the new statutory residence test, domicile and how the remittance basis operates. It applies to the year 2013/14 and subsequent years.

It is not anything like as detailed as the Guidance Note RDR3 on the SRT but it's obviously helpful to know the view of HMRC on these difficult topics. However, HMRC seem desperate to avoid any possibility of being bound by the guidance that it is hedged around with so many caveats that one wonders what purpose it is supposed to serve. It must surely be a waste of time and money to issue guidance to taxpayers and tell them they cannot rely on it.

Tax Valuations

Last month's Bulletin contained an item about personal goodwill and a successful challenge in the Employment Appeal Tribunal to HMRC's argument that goodwill attributable to the personal skills of a proprietor of a business cannot be transferred – for example to a company on incorporation of the business. There have been some other developments in this area in the last few weeks.

There are numerous arguments going on with HMRC about the valuation of goodwill and it is understood that a special team has been set up by HMRC to consider the position. It seems that their consideration may have come to an end. HMRC have issued a notice recognising that the sub-division of goodwill into categories such as inherent goodwill, adherent goodwill and free goodwill is not helpful particularly in the context of trade related properties. They have now published a detailed note setting out their view of the matter. Crucially, HMRC now accept that if a business is sold as a going concern the sale may include some element of goodwill. One might wonder why this had ever been doubted –

but there you are.

The note prepared by HMRC sets out their views about how goodwill should be valued where a business is carried on from a freehold or a leasehold property - although their views will no doubt be the subject of vigorous debate in due course.

HMRC acknowledge that their review of this matter has caused a considerable backlog of cases but they confirm that this backlog will now be addressed – and of course this will be on the basis of the views set out in their note. I think this is going to run and run.

In addition to the details of HMRC's latest stance on goodwill and trade related properties, they have also published a Guidance Note on the valuation of assets generally – pretty much all the things which are valued by SAV including land and property, goodwill, quoted and unquoted shares, chattels, livestock, works of art and some other items. It is only 12 pages long and therefore does not contain a full exposition of their views but it is very helpful nevertheless, even though there are (naturally) a number of points which might not have universal support.

Void and Voidable Transactions

In the August Tax Bulletin I mentioned the case of *Russell Baker* which involved transactions undertaken by the taxpayer which were found to be void. As a result, everything had to be unravelled, and despite valiant efforts by HMRC to salvage their position on the grounds of "economic reality", the tax consequences fell away too.

My attention has been drawn to the case of *AC v DC and Others [2012] EWHC 2032 (Fam)* which deals far more comprehensively with void and voidable transactions (including transactions set aside under such provisions as Section 37 Matrimonial Causes Act 1973), and the implications for tax purposes. In this case the court set aside various transactions by the husband which had been intended to defeat his wife's claims in the divorce. The question was whether the order of the court that the transactions were void ab initio applied equally for tax purposes.

The court said that tax law is not an island. The right for HMRC to charge tax on a particular transaction depends on the effect of that transaction under the general law – unless of course there is a taxing statute to the contrary. (There often is – but that does not detract from the general principle.)

There is long standing authority in the shape of *IRC v Spence (1941) 24 TC 312* which says that the tax effects of a transaction are annulled retrospectively if a voidable transaction is declared void – and all the necessary payments and repayments (including tax) must follow this treatment.

For inheritance purposes, Section 150 IHTA 1984 provides that where a chargeable transfer is set aside as being voidable, the same IHT consequences follow as if the transaction had been void ab initio – with a corresponding effect on any subsequent chargeable transfer. That is clear enough but there is no similar provision for income tax or capital gains tax and it was suggested that these consequences should therefore not follow for other taxes. For numerous and interesting (at least to me) reasons the court decided that the same principle also applied for other taxes.

This does not seem particularly earth shattering – it is probably what everybody expected the rules to be. It is perhaps only the development of arguments by HMRC on the basis of “economic reality” which has caused the subject to be revisited.

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