



## **Budget Update**

**Presented by**

**Tim Good**

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**1. Business and corporation tax**


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**Corporation tax rates**

- 1.1.** To support small companies during the recovery, 2009 Pre-Budget Report announced a further one year deferral in the planned increase in the small companies' rate of corporation tax. The rate will remain at 21% in 2010-11, after which it will increase to 22%.
- 1.2.** Legislation will be introduced in Finance Bill 2010 to set the main rate of corporation tax at 28% on and after 1.4.11.
- 1.3.** The main rate of corporation tax for companies' ring fence profits will remain at 30% on and after 1.4.11.
- 1.4.** Profits limits have not been amended. They remain:

<i>£ per year</i>	<i>2010-11</i>	<i>2009-10</i>
Small companies' rate: 21%	£0 - £300,000	£0 - £300,000
Marginal relief	£300,001 - £1,500,000	£300,001 - £1,500,000
Main rate: 28%	£1,500,001 or more	£1,500,001 or more

**Associated companies: proposals**

- 1.5.** A joint HMT/HMRC consultation document was published in October 2009 with a proposal for reforming the associated company rules as they apply to the small companies' rate of corporation tax. Following from FA 2008 changes affecting partners' holdings, the Government have continued discussions with representative bodies and tax advisers; these have identified that the main priority for further reform are the rules governing control of a company through the attribution to them of rights held by one or more of their associates. The proposal is that the attribution would only be made in cases where entities had been 'fragmented' as part of 'relevant tax planning arrangements'.
- 1.6.** These changes will be adopted from April 2011 by means of legislation in FB 2011; no further changes to the associated company rules are anticipated.
- 1.7.** The proposed new test would not amend the status of companies within the same group or under the control of the same person or persons: these would still be automatically associated. It would only amend the circumstances in which rights held by linked persons are attributed between them to establish control. The test follows the approach taken by both the FA 2008 amendments and ESC C9 in seeking to ensure rights held

are only attributed between linked persons where links between the companies are sufficient to consider them interdependent and thus fragments of a wider whole.

**1.8.** The guidance notes, published in draft with the proposal document, suggest that, whilst the rights of a person and his nominees will always be taken into account, the rights of others will only be relevant in limited circumstances, ie those of relevant tax planning arrangements. It suggests that there are three categories of links to consider: financial links, economic links and organisational links.

**1.9.** Signs of **financial** interdependence include:

- financial support given by one company, or its owner(s) to another company/companies. The company would not be viable without support from the other(s). The support may be directly to the company concerned or indirect in, for instance, the form of guarantees or cross-guarantees; and
- a common financial interest in the affairs of a business shared by the separate companies.

**1.10.** Where more than one business activity is operated from the same or adjoining premises, and the existence of one guarantees or underpins the viability of the other, the companies should be considered to be associated.

**1.11.** Where there are direct and **economic** links between companies, it may be appropriate to treat them as associated. Indicators include:

- separate companies seeking to realise the same economic objective;
- the activities of one company benefiting the other company/companies; and
- separate companies supplying the same circle of customers.

**1.12.** Where there are direct and immediate **organisational** links between separate companies, such that they could not reasonably be run by a third party at arm's length from the other(s), they may be parts of a single enterprise. Inspectors are instructed to look for:

- common management;
- common employees;
- common premises; and

- common equipment.

1.13. In determining 'control' for the purposes of s13(4) TA 1988, the attribution of rights held by associates is not intended to apply where there is an 'accident of circumstance' but rather on whether there has been in a real sense a 'fragmentation' of business activities. Each case will depend on its specific circumstances but there is no fragmentation of control in situations where:

- separate companies are controlled by associated persons but have no financial, organisational or economic links; and
- the associated persons have not, and never have had, involvement in the affairs of the companies controlled by the other associated persons.

#### **Comment**

1.14. Iain Robertson suggests that, while HMRC await responses to their proposals, taxpayers with associated companies might review matters to see if they stand to win.

1.15. For instance, a husband and wife have separate businesses with profits expected of £250,000 each in the year to 31.3.10 and a cash surplus in each of £100,000 or more. A £100,000 bonus paid by the year end could lead to a double benefit:

- tax relief at 28% rather than 21%;
- income tax at a top rate of 40% rather than 50%.

1.16. Other companies which are likely to benefit from the rule changes should review the extent to which profit recognition can be legitimately deferred until the new rules come in. Were they to do so, or in certain cases adapt business practice to improve the position, the question could arise whether such tactics may themselves represent arrangements securing a tax advantage, creating issues within the new s13(4)(A) to (C) and so prevent the hoped-for benefits.

*(HM Treasury press release 29.10.09; Iain Robertson writing in Taxation 25.11.09)*

#### **Capital distributions**

1.17. Before 2005, it was possible to interpret the law as saying that all UK distributions were income in nature unless a specific rule said otherwise—for example, distributions in a winding up. In 2005, in clarifying the law, amendments in a Tax Law Rewrite Act made that view impossible to sustain. Despite this, prevailing practice remained unaltered and UK distributions have generally been regarded until recently as income in nature and potentially exempt from corporation tax.

1.18. In the absence of a rule treating distributions as income, companies in receipt of capital distributions may now face an unexpected tax charge. In some cases, it has become clear that commercial transactions have been put on hold until the tax consequences become clear, with a corresponding effect on the normal business of those companies.

1.19. In order to resolve the issue, the Government will introduce legislation in the Finance Bill with a view to restoring previous expectations about the way that distributions are taxed. The changes will apply retrospectively where appropriate and will be subject to an opt-out to ensure that UK retrospective application of the new legislation does not increase tax liabilities.

#### **Annual investment allowance**

1.20. Legislation will be introduced in Finance Bill 2010 to double the maximum amount of the annual investment allowance (AIA) from the current limit of £50,000 to a new limit of £100,000.

1.21. The AIA is currently available to:

- any individual carrying on a qualifying activity (this includes trades, professions, vocations, ordinary property businesses and individuals having an employment or office);
- any partnership consisting only of individuals; and
- any company (subject to the rules relating to groups of companies and companies related for the purposes of this relief).

1.22. The increase will have effect for expenditure incurred on or after 1.4.10, for businesses within the charge to corporation tax, and on or after 6.4.10, for businesses within the charge to income tax. Where a business has a chargeable period that spans the operative date of the increase, the maximum allowance for that business's transitional chargeable period is the sum of:

- the AIA entitlement, based on the previous £50,000 annual cap for the portion of a year falling before the relevant operative date; and
- the AIA entitlement, based on the new £100,000 cap for the portion of a year falling on or after the relevant operative date.

#### **Example**

1.23. A company with a 2010 calendar year chargeable period would calculate its maximum AIA entitlement based on:

(a) the proportion of a year from 1.1.10 to 31.3.10, that is,  $3/12 \times £50,000 = £12,500$ ;  
and

(b) the proportion of a year from 1.4.10 to 31.12.10, that is  $9/12 \times £100,000 = £75,000$ .

**1.24.** The company's maximum AIA for this transitional chargeable period would therefore be the total of (a) + (b) =  $£12,500 + £75,000 = £87,500$ .

**1.25.** Furthermore, in the part of the chargeable period falling before 1.4.10, only a maximum of £50,000 of the company's expenditure would be covered, whereas for the chargeable period as a whole, up to £87,500 of its expenditure would be covered (whether the whole had been incurred on or after 1.4.10, or part - up to a maximum of £50,000 - had been incurred before that date).

#### ***New anti-avoidance rule***

**1.26.** Anti-avoidance legislation will also be introduced to disallow property loss relief against general income (in terms of Chapter 4 of Part 4 of the Income Tax Act 2007) to the extent that the loss is attributable to the AIA. This restriction will apply to losses arising as a result of relevant tax avoidance arrangements entered into on or after 24.3.10 and, where this legislation applies, the loss will be treated as attributable to the AIA before anything else, including any other capital allowance. In this context, 'relevant tax avoidance arrangements' means arrangements where the main purpose or one of the main purposes is the obtaining of a reduction in tax liability by means of property loss relief against general income, and ones to which the person claiming the relief is a party.

#### ***Comment***

**1.27.** This provision appears to be aimed at those who have been taking advantage of the reliefs available for furnished holiday letting activities. The Chancellor announced at Budget 2009 that this regime would terminate on 5.4.10 and transitional rules were published, together with draft legislation, on 9.12.09. AIA has been available on qualifying capital expenditure incurred on an FHL activity. But if expenditure in the 'dying days' of the regime triggers the above rule, whilst the AIA would be available to offset income in 2009-10, any excess loss would not be available for carry-forward.

#### **Enhanced capital allowances**

**1.28.** The Energy Saving and Water Efficient (environmentally beneficial) Enhanced Capital Allowance (ECA) schemes allow businesses investing in designated technologies that reduce energy consumption, save water or improve water quality to write off 100% of the cost against the taxable profits of the period during which the investment was made.

1.29. With effect on and after a date to be appointed by Treasury Order to be made prior to the summer 2010 Parliamentary recess, the energy efficient scheme List will be revised to include two new sub-technologies:

- permanent magnet synchronous motors and
- biomass fired warm air heaters.

1.30. One existing technology (Compact heat exchangers) and one sub-technology (Liquid pressure amplification) will be removed. The criteria for taps and showers in the Water Efficient scheme will be tightened. Minor housekeeping changes will also be made to the existing criteria of both schemes.

1.31. The lists are available on the internet at [www.eca.gov.uk](http://www.eca.gov.uk).

**Capital allowances: zero-emission vehicles**

1.32. Expenditure incurred on a new (and not second hand) zero-emission goods vehicle will qualify for a new 100% FYA if:

- the vehicle cannot under any circumstances produce CO<sub>2</sub> emissions when driven;
- it is of a design primarily suited to the conveyance of goods or burden; and
- the expenditure is incurred on or after 1.4.10 (corporation tax) or 6.4.10 (income tax) and within five years after those dates.

1.33. In order to comply with State aid rules, a number of additional conditions will also apply to the new FYA. In particular, the FYA will not be available to a business:

- in difficulty or subject to an outstanding recovery order following a EC decision declaring an aid illegal;
- engaged in the fisheries and aquaculture sectors; or
- managing waste for other undertakings.

1.34. To comply with State aid intensity rules, there will also be a cap that limits the amount of expenditure that will qualify for the new FYA to €85 million per undertaking over the five year life of the measure.

**Release of loans to participators in close companies**

- 1.35.** Legislation will be introduced in FB 2010 to deny a corporation tax deduction for the amount of the release or write-off of a loan or advance of money by a close company made to a relevant person who is a participator in that company or an associate of such a participator.
- 1.36.** When a close company makes a loan or advances money to a relevant person who is a participator in the company or an associate of a participator, s455 CTA 2007 imposes a charge equivalent to corporation tax on that company.
- 1.37.** The income tax treatment on the person to whom the released or written off loan was made is at chapter 6 of part 4 ITTOIA 2005. Broadly, that person is treated as if they had received a distribution. This treatment is unaffected by this measure.
- 1.38.** This measure prohibits any deduction being brought into account for loan relationship purposes for the release or write off of such a loan (in whole or in part) on or after 24.3.10.

**Furnished holiday lettings: transition**

- 1.39.** The pre-Budget report confirmed the abolition of all tax benefits applying to furnished holiday lettings (FHL). A number of tax benefits will be withdrawn from April 2010; two technical documents set out the effect of the changes in some detail, including the draft legislation.
- 1.40.** The technical note which provides guidance on the change summarises the changes and their impact in the following areas.
- 1.41.** An unused FHL loss, arising from the commercial letting of furnished holiday accommodation in 2009-10 or previous tax years will be treated for income tax purposes as a loss made in a property business in the tax year 2009-10. It can be deducted from the profits of that property business in 2010-11 and subsequent tax years. Losses arising from commercial FHL in 2009-10 or future tax years will be treated as a property business loss.
- 1.42.** Capital allowances are not available in respect of plant and machinery in a dwelling house which is let. The classification of FHL activities as normal lettings will therefore mean that capital allowances cannot be claimed in respect of expenditure incurred on or after 6.4.10. However, the guidance document states that capital allowances will be available on the remaining expenditure in the pool for businesses which have commenced prior to the date of change.

- 1.43. FHL operations are excluded from claiming the 10% wear and tear allowance, but will be permitted to claim in future. The document clearly states that this will be in addition to any residual capital allowances available under the transitional rules described above.
- 1.44. The landlords' energy saving allowance of £1,500 per property in respect of certain energy saving expenditure (such as insulation) will now be available on FHL properties.
- 1.45. CGT rollover relief will no longer be available on the reinvested gains arising on FHL assets disposed of after 5.4.10, unless the disposer carries on a separate trade in which case the rollover will be restricted to recognise the non-trade use of the asset between 6.4.10 and the date of disposal. Generally speaking, gains rolled into FHL assets are not affected, but of course these gains cannot be further rolled over on subsequent disposal. Where a gain has been held over into an FHL depreciating asset, it will crystallise in the normal way.
- 1.46. There will be no CGT holdover relief for FHL assets gifted after the date of change, but assets which have been obtained subject to a holdover election will not be affected. Any latent gain will be taxed on eventual disposal as normal.
- 1.47. The guidance document also includes HMRC's view on whether an FHL business might 'convert' to a trading business by the provision of additional services. It is HMRC's view that the provision of additional services would amount to a separate trade and that any charges for the use of the property should be separated from other charges, such as the provision of cleaning and fresh laundry or the provision of meals, to form property income on the one hand and a small trading activity on the other. Charging separately would be an indication of a separate trade.

**Comment**

- 1.48. As far as planning for entrepreneurs' relief (ER) is concerned, it was originally suspected that owners would have to sell by 5.4.10 to secure ER, but the deemed cessation rule permits the subsequent sale of the assets within a three year period after the change which will qualify for ER under the 'cessation of business' rules. This will apply to both individual property owners and partnerships, and seems to apply irrespective of whether the FHL activity continues for a while after April 2010, as the cessation is 'deemed' by the change in the rules. This means that owners do not have to decide now what to do as they effectively have a further three years to decide whether to sell up or not. However, possible changes in the rate of CGT and any effect that might have on ER should be added as a caveat.

*(HMRC guidance notes 9.12.09; Comment by Rebecca Benneyworth, AccountingWeb 14.12.09)*

**OTHER DEVELOPMENTS****Tax Health Plan disclosure opportunity**

- 1.49. Medical professionals are being encouraged under a new Tax Health Plan to tell HMRC if they have understated their income.
- 1.50. Those who contact HMRC by 31.3.10 to make a voluntary disclosure will be able to put their tax affairs in order simply and on the best available terms. After that date, using information they hold about how much is paid to them, HMRC will carry out targeted investigations aimed at medical professionals who have not come forward. Substantial penalties or even criminal prosecution could follow for those who have undeclared tax liabilities.
- 1.51. The Health Plan is the first initiative in a new HMRC campaign focused on professionals. It is designed to make it 'easy for taxpayers to put their tax affairs right and keep them that way'.
- 1.52. The Health Plan will operate in two stages:
- from 11.1.10 to 31.3.10, medical professionals can register their intention to make a voluntary disclosure with HMRC; and
  - by 30 June, those who have registered must have made their disclosure as well as arrangements to pay all tax interest and penalties due.
- 1.53. If HMRC receive a full and accurate disclosure of any income on which tax hasn't been paid, along with payment, by 30.6.10, those who qualify can expect a reduced penalty of 10%.
- (HMRC press release 10.1.10)*

**Tax warning for fish and chip shops**

- 1.54. Local chippies are being advised to keep their tax affairs in order as HMRC's penalties for chip shop owners continue.
- 1.55. Initially the main focus is likely to be on gross profit percentage, particularly if it is considered to be lower than expected. HMRC are able to compare the gross profit percentage declared by each business within a specific geographical area from the information submitted on self assessment returns. This search can be fine-tuned to identify fish and chip shops in a specific town, county or region, for example, who are declaring the lowest or a lower gross profit percentage than other comparable businesses within the locality.

- 1.56. It is understood that there will be no restrictions on penalties for non-compliance when it comes to fish and chip shops, unlike the 10% fixed penalty offered to medical professionals.
- 1.57. Ultimately in any review carried out by HMRC the key focus will be on the quality of the records maintained by the owner of the business. It is therefore vital that shop owners maintain detailed records of business results. Abbey Tax Protection suggests the following steps to keeping healthy records:
- take a till Z reading at the end of each day and retain it, together with the till rolls to support the declared record of sales in your cash book;
  - keep a clear record of the business cash flow together with purchase invoices, any other expense receipts and a detailed record of drawings to support what cash has been taken for private purposes as well as any capital introduced to the business;
  - keep a detailed record of any wastage that occurs in the shop on potatoes, fish and other products as this will have a bearing on the results achieved. If the inspector is able to demonstrate any weaknesses in the records then the next step will be to gather information to enable a Business Economics Exercise to be carried out. This may then produce an expected sales figure which is much higher than that declared and difficult to contest fully;
  - if you do not pay for any food, drinks and other sales items taken from the shop personally, you should keep a record of this own consumption;
  - keep a record of any special offers and discounts given;
  - keep detailed records (names, addresses and payments made) of any members of staff, even on a part-time basis such as school children, as HMRC will check that all payments made to staff are genuine. Obtain form P45 or a signed P46 where appropriate to show that you are their main employer. If you do not obtain either of these forms, you should deduct basic rate tax from any payments made; and
  - keep a record of the stock-take carried out at the end of your accounting period, even though this may be minimal.

*(AccountingWeb 25.1.10)*

**Profit made by director*****The issue***

- 1.58. Whether the transfer of a property by a company to its shareholder and director was employment income under s62 ITEPA 2003.

***The facts***

- 1.59. T was a builder, and since 1997 had traded solely through a company of which he was the sole director and shareholder.
- 1.60. He entered into an agreement with B to construct three cottages in the garden of a house belonging to B. The proposal was that B would provide the land, the company would build the three cottages at its own cost and, on completion, retain two of them, while the title of one cottage would be transferred by the company to B. By the time of completion, the contract wording actually showed that B would retain one cottage and transfer the other two. Since company did not have the title during the building, it was not possible for the company to borrow the costs of building; T contributed half the cost himself, some £105,000.
- 1.61. The company agreed to sell one property to T for half of the development costs and this then happened with adjustments made to the director's loan account. Subsequently T sold the cottage to the company for £190,000.
- 1.62. T contended that, by making contributions to the building costs, he had acquired an equitable interest in the land. He also submitted that the contractual negotiations which took place created a tripartite agreement between B, the company and him.
- 1.63. Thus any profit to him in the transfer to him of the cottage was not properly taxable as earnings from his office or employment under the company, either because he was already entitled to the profit by virtue of his accrued beneficial interest in the cottage or because it was a reward for his having taken the risk involved in financing one half of the development costs of the project (all three cottages).
- 1.64. HMRC submitted that the benefit was received by reason of T's employment because he had acted in the development entirely in his capacity of sole director of the company and not as an individual.
- 1.65. They also submitted that T was attempting to put into effect a tax and NIC avoidance scheme. He would move into the cottage and later sell it to the company. The capital gain attributable to his period of ownership/residence would be exempt from capital gains tax and the company would take the cottage at a base cost which was higher than it would have been without the intervening period of ownership by T.

- 1.66. They accepted that the payments totalling £105,000 were made by T to the company, but noted that they were made via his director's loan account and submitted that they should be regarded as injections of funds into the company to be used by the company for its purposes, rather than as contributions towards the building costs made by T on his own account.

***The decision (FTT)***

- 1.67. The tribunal felt that the cottage had been transferred to T by B by direction of the company. They did not accept that there was a tripartite agreement between B, the company and T. They also rejected the submission that T had a beneficial interest before the cottage was transferred to him.
- 1.68. The transfer of the cottage to T was caused entirely by the arrangement which he had made with the company. It did not concern B at all. T dealt with B at all times *qua* director of the company and not on his own behalf as an individual.
- 1.69. However, the transfer to T of the cottage, assuming it was a profit to him or 'money's worth', was not received by him by reason of his office or employment under the company, but, instead, by reason of his arrangement with the company (entered into in his individual capacity and not as a director) that he would provide financial assistance to the company to enable it to carry out the development in return for the transfer to him of the cottage on completion.
- 1.70. Having found in principle for T, the tribunal left the parties to agree on the disposal of the appeal.

*(Desmond John Thresh v HMRC TC00343 13.1.10)*

**Capital allowances: alterations to buildings**

***The issue***

- 1.71. Whether costs incurred in the conversion, fitting out and refurbishment of public houses qualified for capital allowances under s24 CAA 1990 or s66 CAA 1990 (or both).

***The facts***

- 1.72. JDW Plc had incurred expenditure in the year ended 31.7.99 in respect of building costs of £34m which were amended by HMRC to £17.5m. The company appealed and a detailed review of expenditure followed. Two properties were chosen as representative of the projects undertaken in the year.
- 1.73. JDW and HMRC were unable to agree the application of that decision of the Special Commissioners to every part of the expenditure in contention. Further argument was therefore heard, whilst recognising that other issues could still be at stake in relation to

the other 286 properties affected. Lists were prepared of 'clear items', where the parties sought a formal decision on the qualification of the items for allowances, and 'unclear items', where they remained in disagreement over the application of the earlier decision.

- 1.74. Much of the debate concerned s66 CAA 1990 which treated expenditure on 'alterations to an existing building incidental to the *installation of machinery or plant for the purposes of the trade*' as if it were expenditure on the provision of that plant and machinery. *IRC v Barclay, Curle & Co. Ltd (1969)* 45 TC 221 clarified the words in italics as meaning 'installation so that the machinery or plant can function properly by reference to the purpose for which it was installed'.

***The decision (FTT)***

- 1.75. Tiling: wipe-clean tiling was excluded, apart from splash-backs to sinks and the immediate surrounds of lavatory basins. Where a larger area of tiling included a splash-back area, the qualification under s66 was restricted to 'tiling sufficient specifically to deal with splashing which may be expected to be caused by the usual functioning of any qualifying items of machinery or plant'. To include wipe-clean floors as the cost of an alteration to the building was 'unrealistic'. As a consequence, the tribunal rejected an apportionment of the cost of fully-tiled walls and rejected also the notion that plastering to accept tiling was part of the alteration of the building.
- 1.76. Floors: non-slip and wipe-clean floors were needed for the operation of equipment in a pub, but this did not mean that expenditure on preparing the floors was part of the installation cost of the equipment: it did not have sufficient nexus with the installation.
- 1.77. The floor of the cold store needed to slope in order that drainage equipment could deal with spillages and their removal. A proportion of the expenditure on the floor was recognised by HMRC as allowable since it related to the functioning of the drainage equipment. The cost of breaking out the existing slab in the floor had been excluded by HMRC. The tribunal considered that the whole of this preparation expenditure was eligible, since it was always intended that the floor should be inclined.
- 1.78. Lighting: the eligibility of expenditure on fitting lights and adapting ceilings depended on whether the lighting fittings themselves qualified as plant or machinery. It was suggested that some created an attractive ambience, but this was not enough to suggest that the fittings had a function in the trade. Some kitchen lighting was accepted as 'trade-specific' on the slight evidence that was available.
- 1.79. Miscellaneous works: specific consideration was given to food hoists, toilet cubicle dividers, floor reinforcement, partition strengthening and waterproofing.

- 1.80. Preliminaries: should trade-specific overheads be apportioned to items of main contract expenditure to which they related or pro-rated over all classes of work? Those attributable to particular items of measured work were not really preliminaries and should be treated as part of the cost of the items concerned. Project overheads (not trade-specific overheads or preliminaries) fall to be apportioned globally. Items such as propping and photos of drainage work related to more limited and specific categories of work; here the extent of attribution or apportionment required depended on reasonableness and proportionality, on the application of common sense. An overall global apportionment of preliminaries which do not relate to individual items was held to be a legitimate approach to such items.

**Comment**

- 1.81. Deloitte, who acted as instructing accountants on behalf of JDW, comment that many technical areas under appeal in this case are pertinent to the majority of taxpayers incurring capital expenditure on property, so this case has wide-ranging ramifications.  
(*J D Wetherspoon PLC v HMRC TC00312 18.12.09*)

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## 2. Employment tax and national insurance contributions

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### Bank payroll tax

- 2.1. As announced at PBR, legislation in Finance Bill 2010 will introduce a new bank payroll tax. This will be set at 50%. It will be payable by a bank, on the amount of a bonus to which a banking employee is entitled, to the extent that the bonus exceeds £25,000. A bank will also be liable to the bank payroll tax where the bonus entitlement arises in respect of services performed for the bank regardless of who awards the bonus.
- 2.2. The bank payroll tax will have effect from 9.12.09 until 5.4.10 for all discretionary and contractual bonus awards. There is an exception for contractual bonus entitlements where the payer has no discretion as to the amount of the bonus because of a contractual obligation existing at the time of the Chancellor's announcement. Bank payroll tax is payable on 31.8.10.
- 2.3. The detailed provisions for the assessment and the collection of bank payroll tax were published in December, including provisions for penalties and interest.
- 2.4. A number of changes have been made to the draft clauses. The main changes are:
- clarification of the scope of the legislation in connection with when relevant remuneration is taken to be 'awarded' during the chargeable period;
  - clarification of the scope of the legislation in connection with the definition of 'taxable company';
  - introduction of a 60 day rule for relevant banking employees; and
  - inclusion of detailed machinery provisions for the assessment and the collection of BPT. These include provisions for penalties and interest.
- 2.5. A Technical Note, including draft legislation and explanatory notes, can be found on the HMRC website.

### Enterprise management incentives

- 2.6. Paras 13 to 15 sch 5 ITEPA 2003 require that, in the case of a single company granting EMI options to its employees, that company must carry on a trade 'wholly or mainly' in the UK or, in the case of a parent company, at least one company in the group must be carrying on a 'qualifying trade' (within the meaning of the legislation) 'wholly or mainly' in the UK.

- 2.7. To ensure EMI complies with EU State aid guidelines, the present rule will be amended. In future, a single company wishing to grant EMI options must have a 'permanent establishment' in the UK. Alternatively in the case of a parent company, at least one company in the group that is carrying on a 'qualifying trade' within the meaning of the legislation must have a 'permanent establishment' in the UK.
- 2.8. 'Permanent establishment' has the same meaning as in s148 FA 2003. The change will have effect in respect of EMI options granted on or after the date that the legislation receives Royal Assent.

#### **Employer-supported childcare**

- 2.9. Condition C in s270A ITEPA 2003 sets out the conditions for employees to participate in childcare voucher schemes which qualify for the tax exemption on the chargeable benefit up to the value of £55 per week. Where such arrangements are made without being available generally to employees, the exemption from the chargeable benefit should not apply. In practice, some employers have been excluding employees at or near the national minimum wage (NMW) from schemes provided through salary sacrifice arrangements.
- 2.10. Employees at or near the NMW cannot normally take advantage of salary sacrifice arrangements if the result would be to depress the level of their income below NMW rates. The measure introduces an exception to Condition C in the case of relevant low-paid employees where the childcare voucher scheme is provided through a salary sacrifice arrangement.
- 2.11. S318A ITEPA sets an equivalent condition in respect of directly-contracted childcare. Again, the measure introduces an exception to Condition C in the case of relevant low-paid employees where the directly-contracted childcare is provided through a salary sacrifice arrangement.
- 2.12. All these amendments will have retrospective effect for the tax year 2005-06 and subsequent tax years.

#### ***Non-Budget announcement***

- 2.13. On 3.12.09, the Government announced changes to the tax and NIC exemptions for employer-supported childcare. HMRC have now issued technical guidance on this area.
- 2.14. From 6.4.11, the limit on the amount of exempt income associated with childcare vouchers and directly contracted childcare for employees joining an employer's scheme will be restricted in cases where an employee's earnings and taxable benefits are liable to tax at the higher or additional rate. This is to ensure that the income tax saving for

higher paid employees is limited to that available for employees whose earnings and taxable benefits are liable to income tax at the basic rate.

- 2.15. Anyone already in a scheme by 5.4.11 will not be affected by these changes as long as they remain within the scheme.
- 2.16. From 6.4.11, employers will be required at the beginning of the relevant tax year to estimate the level of basic employment earnings that their employee is likely to receive during that year, ignoring potential bonus and overtime payments, but including other known taxable benefits.
- 2.17. An employee joining the scheme after 5.4.11 who has estimated earnings and taxable benefits equal to or below the equivalent of the sum of personal allowances and the basic rate limit for the year will be entitled to relief on £55 exempt income for each qualifying week.
- 2.18. If the level of estimated earnings and taxable benefits exceeds the equivalent of the sum of personal allowances and the basic rate limit for the year, but falls below the limit at which tax becomes payable at the additional (50%) rate limit for the year, the employee will be entitled to relief on £28 exempt income for each qualifying week.
- 2.19. If the level of estimated earnings and taxable benefits exceeds the equivalent of the additional (50%) rate limit for the year, the employee will be entitled to relief on £22 exempt income for each qualifying week.
- 2.20. The figures of £28 for higher rate taxpayers and £22 for additional rate taxpayers have been set to ensure that they receive approximately the same level of income tax relief as basic rate taxpayers, ie £11 per week.
- 2.21. 'Basic employment earnings' does not include bonuses or overtime and there is no equivalent NIC change.

**Benefit in kind: zero-emission vehicles and low-emission cars**

- 2.22. Individuals who, by reason of their employment, are provided with a company car or van which is made available for private use are subject to a taxable charge on the benefit.
- 2.23. Legislation in FB 2010 will introduce a relief from the chargeable benefit where the car or van concerned cannot produce CO<sub>2</sub> engine emissions under any circumstances when driven.
- 2.24. FB 2010 will also introduce a reduction to the chargeable benefit where a car has an approved CO<sub>2</sub> engine emission figure of 75g per kilometre or less.

- 2.25. The measure will have effect on and after 6.4.10 until 5.4.15.

#### **National insurance contributions rates and thresholds**

- 2.26. The Budget confirmed the national insurance contributions (NIC) rates and thresholds that will apply for 2010-11. The lower earnings limit (LEL) which is linked to the basic State Pension will increase by £2 to £97 per week and the special Class 2 rate for volunteer development workers will increase by 10p to £4.85 per week as this is linked to the LEL.
- 2.27. All other NIC rates and thresholds are unchanged for 2010-11.
- 2.28. From 2011-12, the 2009 PBR proposed to increase the main rate of Class 1 and 4 NIC by 1% to 12% and 9% respectively (not the 0.5% originally proposed in the 2008 PBR).
- 2.29. The Class 1 employer rate will also be increased by 1% to 13.8% from 2011-12. The increased rate will also apply to Class 1A and 1B contributions.
- 2.30. The additional rate of Class 1 and 4 NIC will be increased by 1% to 2% from 2011-12.
- 2.31. The primary threshold and lower profits limit will be increased by £570 for 2011-12 above plans announced in the 2008 PBR to compensate the lowest earners for the increase in the Class 1 and 4 rates.
- 2.32. The change to the rates of Class 1 and 4 NIC in 2011-12 will require a National Insurance Contributions Bill.

#### **OTHER DEVELOPMENTS**

##### **Incorrect tax codes**

- 2.33. Taxpayers and agents are reporting large numbers of incorrect tax codes sent by HMRC for 2010-11. HMRC responded that they had no evidence of a widespread problem but advised taxpayers to check their codes carefully as it is not clear how many incorrect tax codes have been sent out or may be distributed in the coming weeks.
- 2.34. The CIOT said the scale of the problem might be indicated by the fact that this year about 25 million coding notices are being distributed, which is about twice last year's number. The new PAYE computer system launched in July (NPS) is in play for the first time for the code run. The big difference is that the master file system is organised by employee name rather than by employer, allowing HMRC to marry up records of people who have more than one job/pension etc. Ultimately this will be much more efficient as it will allow accurate issue of tax allowances where someone has several part time jobs and wants part of their allowances transferred to a second job. However, this is the first

year and the system has collated data from P35s, some of which are suspect. So HMRC are already warning that this year there will be extra code notices and there may be some bugs that are coming through due to duplicate records.

(AccountingWeb 27.1.10)

### **Tax deductible clothing**

#### ***The issue***

- 2.35. Whether a TV presenter could claim tax relief for the cost of clothing she wore only whilst on TV.

#### ***The facts***

- 2.36. The appellant, W, is employed by the BBC as a television newsreader. In her 2004-05 tax return, she claimed certain deductions from her earnings, including:

Professional hairdo and colouring	£975
Professional clothing for studio	£3,231
Laundry of professional clothes	£325

- 2.37. W argued that these were allowable expenses under s336 ITEPA 2003 because there was no duality of purpose - she didn't wear any of the clothes when not appearing on TV - and that the only legislative difference between her claims and successful claims made by her self-employed colleagues was the difference between 'wholly and exclusively' and 'wholly, exclusively and necessarily'.
- 2.38. She argued that the clothing costs were necessarily incurred because, while she was prepared to present without clothing, her employers would not accept this and her contract implied that she should not be seen wearing the same clothes more than two or three times a month.

#### ***The decision (FTT)***

- 2.39. The evidence did not suggest that W had her hair done and coloured immediately before performing her duties as newsreader and then changed it back again immediately afterwards. Therefore the costs could not relate wholly, exclusively and necessarily to the employment.
- 2.40. No express term in W's contract insisted she change her clothing as often as she said it implied but, even if it had, the requirement of a varied wardrobe would be an aspect of the requirement that clothing be of a standard required for the occupation.
- 2.41. W's lack of need of clothes for warmth (as it is warm inside the studios) and her readiness to read the news without clothes were not accepted as realistic by the tribunal,

which rejected the argument that she only wears the clothes because her employer requires it. The tribunal therefore rejected W's appeal.

(*S Williams v HMRC TC00397 8.2.10*)

### **Training costs: off-the-job**

#### ***The issue***

- 2.42. Whether the cost of training courses attended by an employee was an amount expended wholly, exclusively and necessarily in the performance of her duties.

#### ***The facts***

- 2.43. B was employed as a specialist registrar by two NHS trusts. Throughout her period of employment, the terms and conditions of her employment included a training clause which required her to continue to hold a national training number and to attend meetings, courses and conferences 'in carrying out the duties of her employment' as prescribed by her managers. The courses and training that B attended were compulsory and a prerequisite of her maintaining her post and employment. B claimed deductions under s198 TA 1988 [s336 ITEPA 2003] for the costs of her courses.
- 2.44. The amounts were disallowed by HMRC who argued that, to fall within s198, the expense had to be related to an objective necessity imposed by the duties of the employment itself, irrespective of what the employer might prescribe. Further, the expenditure had to have been incurred in the actual performance of the duties of the employment as opposed to courses outside the time B was working. The General Commissioners said that the training had been sufficiently related to the employment to be deductible. HMRC appealed.

#### ***The decision (ChD)***

- 2.45. Early precedents featured taxpayers who were preparing, by attending training courses, to undertake professional examinations. This was not the case with B, whose employment constituted part of her five year training programme. The post was, in the words of one witness, 'essentially a training post'. The more recent case of *Decadt* was very similar to the present case, possibly identical. The High Court in that case upheld the decision of the General Commissioners, who had nonetheless been wrong in law to ask only whether the training condition was a term of the contract. In *Fitzpatrick v IRC* [1994] 66 TC 407, the House of Lords had denied journalists relief for expenditure on newspapers and periodicals on the basis that the expenditure had not been incurred in performing the duties of the employments concerned; the principles of law had not been in doubt, but the question was whether the commissioners had erred in law in finding as they did.

**2.46.** The High Court (Mr Justice Henderson) ruled in the present case that the General Commissioners had been fully entitled to take the view that attendance at the courses was an objectively necessary requirement of B's employment. It had not merely been a contractual obligation undertaken by her at her employer's request, nor had it been an extra-curricular obligation that she had chosen to undertake in order to qualify herself to do her job or improve her prospects of promotion. There was no basis for saying that the commissioners had erred in law in taking the view that they had. To assert the contrary would amount to saying that it was impossible for the test in s198 to be satisfied in any case where the taxpayer was paid to undergo training. Stringent though the section undoubtedly was, there was no reason why it should be construed in such an extreme way.

*(HMRC v Banerjee ChD 19.6.09)*

#### **Private cars with business use**

**2.47.** It is well known that where an employee uses a personally owned car for a business journey, a payment of up to 40p per mile can be made tax and NIC-free for the first 10,000 business miles per year. Where more than 10,000 business miles are undertaken in a tax year the tax-free amount is limited to 25p per mile.

**2.48.** What is commonly overlooked is that for NIC purposes the 40p rate applies to ALL miles (whether amongst the first 10,000 or not).

**2.49.** Since any excess is taxable, but goes on the P11D rather than being caught by PAYE, there is no requirement to payroll payments up to and including 40p per mile just to catch the NIC liability since there is none.

**2.50.** Amounts paid above 40p per mile attract Class 1 on the excess over that figure (which will therefore need to be payrolled) and the excess (over 40p/25p as applicable) goes on the P11D to be taxed separately.

*(Peter Arrowsmith writing on TaxationWeb 17.1.10)*

### 3. Personal income tax

#### Income tax allowances

3.1. The pre-Budget report of 9.12.09 announced a freezing of the values of all personal allowances for 2010-11 at their 2009-10 levels. The allowances for those two tax years will thus be as follows.

£ per year (unless stated)	2009-10	Change	2010-11
Personal allowance (age under 65)	£6,475	£0	£6,475
Personal allowance (age 65-74)	£9,490	£0	£9,490
Personal allowance (age 75 and over)	£9,640	£0	£9,640
Married couple's allowance* (age 75 and over)	£6,965	£0	£6,965
Married couple's allowance* - minimum amount	£2,670	£0	£2,670
Income limit for age-related allowances	£22,900	£0	£22,900
Blind person's allowance	£1,890	£0	£1,890

\*Married couple's allowance is given at the rate of 10%.

#### Income tax: taxable bands

3.2. There is to be no increase in the bands of taxable income for 2010-11, except that the new 50% additional rate band will apply for the first time.

2009-10	£ per year	2010-11	£ per year
Starting savings rate 10%	£0-£2,440	Starting savings rate 10%	£0-£2,440
Basic rate: 20%	£0-£37,400	Basic rate: 20%	£0-£37,400
Higher rate: 40%	Over £37,400	Higher rate: 40%	Over £37,400
Additional rate	N/A	Additional rate: 50%	Over £150,000
Basic rate on dividends (effective rate with tax credit)	10% (0%)		10% (0%)
Higher rate on dividends (ditto)	32.5% (25%)		32.5% (25%)
Additional rate on dividends (ditto)	N/A		42.5% (36.1%)

**Tax credits**

- 3.3. Budget 2010 announced further support for low-income families including:
- supporting families with young children, from April 2012, the Government will introduce additional support in the child element of the Child Tax Credit for each child aged 1 and 2 by £4 per week;
  - supporting parents with childcare by simplifying and improving the responsiveness of the childcare element of the Working Tax Credit. This will allow parents with short-term childcare needs to receive payments when they incur them, such as in the school holidays, rather than receiving a smaller, average payment over the course of the year as is currently the case.

**Individual savings accounts**

- 3.4. As announced at Budget 2009, from 6.4.10 the ISA annual subscription limits are being increased for all savers, to £10,200, of which £5,100 can be saved in cash.
- 3.5. From 6.4.11 and over the course of the next Parliament, the annual ISA limits will increase annually in line with RPI. The new annual limits will be rounded to the nearest multiple of £120 so that individuals who save monthly will be able to calculate their monthly savings more easily.
- 3.6. The new limits will be calculated by reference to the RPI for the September before the start of the tax year. HMRC will announce the new limits as soon as possible after the RPI figure is published, and at least four months in advance of the start of the new tax year in which they will apply. In the event that RPI is negative, the ISA limits would be unchanged.
- 3.7. As is the case now, following indexation, the cash ISA limit will be half the value of the stocks and shares ISA limit.

**Venture capital schemes**

- 3.8. Four changes are required of the UK as a condition of the approval of the Enterprise Investment Scheme (EIS) and Venture Capital Trust (VCT) as approved State aids. The changes generally will have effect on and after the date that the legislation receives Royal Assent, with the exception of the definition of eligible shares for VCTs, which will not affect monies raised by the VCT before that date.

**VCTs only**

- 3.9. The current legislation at s274 ITA 2007 requires the shares making up a VCT's ordinary share capital to be included in the official UK list throughout the relevant accounting

period. This will be replaced with a requirement that the shares instead be admitted for trading on any EU regulated market. The effect is that VCTs will be able to be listed on markets throughout the EU/European Economic Area (EEA). The European Commission publishes a list of all regulated markets in the Official Journal of the European Union at least annually, and the list of regulated markets is also available on its website.

- 3.10. The current legislation at s274 ITA 2007 requires that at least 30% of the VCT's qualifying holdings is represented throughout the relevant accounting period by holdings of eligible shares. S285(3) ITA 2007 defines 'eligible shares' for this purpose. The new legislation will increase the eligible shares holdings requirement to 70%, but will also change the definition to allow VCTs to include shares which may carry certain preferential rights to dividends.

#### ***EIS and VCTs***

- 3.11. The new legislation will exclude shares in a company from qualifying for the purposes of the EIS or VCT legislation if it is reasonable to assume that the company would be treated as an 'enterprise in difficulty' for the purposes of the European Commission's Rescue and Restructuring Guidelines, published in the Official Journal at OJ C 2004/244/02, at section 2.1.
- 3.12. The current legislation, in ss179 and 291 ITA requires that there is a qualifying trade carried on wholly or mainly in the UK. For shares issued on or after the commencement date of the legislation, the requirement will be that the company issuing the shares must simply have a permanent establishment in the UK.
- 3.13. 'Permanent establishment' will be defined based on art 5 of the OECD Model Tax Convention on Income and Capital. It is intended that the definition will be published in full in secondary legislation to be made after the date that the primary legislation receives Royal Assent.
- 3.14. Regulations will also be made at this time to update Statutory Instrument 2004/2199 to reflect the new conditions concerning eligible shares.

#### **Pensions: anti-forestalling for high-income individuals**

- 3.15. The Government announced at Budget 2009 its intention to restrict tax relief on pensions savings with effect from 6.4.11 for people with incomes of £150,000 or over. At the same time legislation was introduced to prevent those likely to be affected from seeking to forestall this change.

- 3.16.** The special annual allowance and tax charge apply only to high-income individuals. Under the FA 2009 measures, these are individuals with income of £150,000 or over for the tax year or for either of the preceding two tax years.
- 3.17.** From 9.12.09, the special annual allowance and tax charge will also apply to those with income of £130,000 or over, for the tax year or for either of the two preceding tax years.
- 3.18.** For these individuals, the special annual allowance and tax charge will apply in the same way as for those with incomes of £150,000 or over. However, in these cases the special annual allowance tax charge will apply only to additional pension savings over and above the individual's normal regular pension saving made on or after 9.12.09.
- 3.19.** Those individuals who do increase their pension savings on or after 9.12.09 over and above their normal pattern of regular pension savings may be affected if their total pension savings in that year are over £20,000. In certain circumstances where contributions have been made less frequently than quarterly this limit may be increased up to £30,000.
- 3.20.** The tax charge will not apply to any normal, regular ongoing pension savings arrangements that were in place before 9.12.09, whatever their value. It applies only to additional savings over and above those made on or after 9.12.09.
- 3.21.** Where regular pension savings exceed the special annual allowance, the special annual allowance charge will apply to any additional pension savings made on or after 9.12.09 in excess of regular savings. Where regular pension savings are below the special annual allowance, the tax charge applies to any excess over the special annual allowance. The charge has the effect of restricting tax relief on the additional pension savings to basic rate.
- 3.22.** The special annual allowance and associated tax charge apply to total contributions, regardless of whether these are made by the individual, their employer or by a third party and to any benefits accruing in a defined benefits scheme. The tax charge will be collected through the self assessment tax return.

***Effect of the additional (50%) rate of income tax***

- 3.23.** The rate of the special annual allowance charge for the purposes of the anti-forestalling rules is currently 20%. From 6.4.10 the special annual allowance charge will be set at the 'appropriate rate'. The 'appropriate rate' is determined by the rate of tax relief given on the amount of their pension savings which exceeds their special annual allowance and will restrict tax relief on that excess to the basic rate of income tax.

**Pensions relief restriction: 2011 onwards**

- 3.24.** The proposals for restriction of tax relief for pension contributions with effect from April 2011 were laid out in a consultation document, '*Implementing the restriction of pensions tax relief*', published on 9.12.09.
- 3.25.** A 'high income excess relief charge' will be imposed to restrict the amount of higher-rate tax relief when relevant income exceeds £130,000. The restriction will apply in relation to personal or employee pension contributions, as well as on those made by employers or third parties for the individual's benefit. It will apply to contributions otherwise gaining relief at 40% as well as to those in the 50% range.
- 3.26.** The restriction will only apply to those whose 'relevant income' exceeds £130,000. Relevant income is that on which the individual is charged to income tax (including employment income less allowable expenses, trading income and other taxable income) less available losses and other reliefs, but with no deduction for personal or employer pension contributions or charitable donations.
- 3.27.** Where relevant income does exceed £130,000 for 2011-12 or a later tax year, the special annual allowance charge applies if 'gross income' exceeds £150,000. Gross income takes relevant income and adds any employer pension contributions made on the individual's behalf.

**Example**

Employment income	£120,000
Employer contributions into pension	£20,000
Rental and savings income	£15,000
Personal pension contributions (gross amount)	£10,000
Hence	
Relevant income	£135,000
Gross income	£155,000

- 3.28.** The relief for pension contributions will be restricted to 20% for those with gross income above £180,000. Where gross income exceeds £150,000 but not £180,000, the rate of relief will be reduced by 1% for every £1,000 of income in that range. This reduction will apply to the rate of relief otherwise attaching to the pension contributions in question. A 20% reduction will take 50% relief down to 30% or 40% relief down to 20%. A reduction of 10% or less, however, will only be applied to 50% relief contributions.

**Example**

- 3.29. In the above case, total pension contributions are £30,000, otherwise attracting relief at 50% on £5,000 and 40% on £25,000. Since £5,000 falls into the range £150,000 to £180,000, the reduction in rate will be  $5 \times 1\% = 5\%$ . As this result is less than 10%, the restriction will apply only to the relief that would otherwise be given at 50%. There will be a special annual allowance charge of  $5\% \times £5,000 = £250$ .

**Example**

- 3.30. Consider another taxpayer whose relevant income is £170,000 in 2011-12 and who makes personal pension contributions of £30,000 (gross amount). Relief would normally be given on £20,000 at 50% and £10,000 at 40%, a total of £14,000 of relief.
- 3.31. Since £20,000 of income falls into the range £150,000 to £180,000, the reduction that applies is  $20 \times 1\% = 20\%$ . This applies to all contributions, since the reduction rate exceeds 10%. Hence relief will be given for the whole of the £30,000 at 30% only, ie £9,000. A special annual allowance charge of £5,000 ( $£14,000 - £9,000$ ) will be made.

**Pensions: the lifetime allowance and annual allowance**

- 3.32. As announced in the 2008 pre-Budget report, the 2010-11 lifetime allowance of £1.8 million and the annual allowance of £255,000 will continue to apply, with their rates held constant, for a further five tax years, ie up to and including the tax year 2015-16.

**Pensions: enabling legislation**

- 3.33. Measures are being put in place which will affect employers, their employees (referred to as 'jobholders' in the Pensions Act 2008), the National Employment Savings Trust (NEST) and its members, other qualifying pension schemes when automatic enrolment of jobholders is introduced from 2012 and scheme administrators of all registered pension schemes.
- 3.34. The measures will:
- allow NEST to register with HMRC for tax purposes, and to be subject to the same tax rules as other tax-registered pension schemes;
  - remove the tax liability on any interest charges on late pension contributions made by an employer to qualifying pension schemes;
  - provide a regulation-making power to deal with any unintended tax consequences that may emerge as a result of the implementation of NEST and the employer duties and compliance as set out in the Pensions Act 2008; and

- remove the tax charge on borrowing linked to the cost of establishing and operating a registered pension scheme, subject to conditions.
- 3.35.** The Pensions Act 2008 places a duty on employers to ensure that their jobholders are active members of a pension scheme. The introduction of this 'automatic enrolment' duty is planned for 2012.
- 3.36.** The Pensions Act 2008 also obliges the employer of a jobholder to make pension contributions to qualifying pension schemes. When the contributions are paid late the employer may, at the Pensions Regulator's discretion, be asked to pay interest to their jobholder's pension account.
- 3.37.** Under s369 ITTOIA 2005, the jobholder would be taxed on any interest paid by employers to a jobholder's pension account. This tax charge on the jobholder will be removed.

#### **Extending UK charity reliefs**

- 3.38.** FB 2010 will extend UK charitable tax reliefs to certain organisations equivalent to UK charities and Community Amateur Sports Clubs (CASCs) in the EU and in the European Economic Area (EEA) countries of Norway and Iceland, following a judgement in the case of *Persche v Finanzamt Ludenscheid* (Case C-318/07 27.1.09) in the European Court of Justice.
- 3.39.** A number of definitions of a 'charity', 'charitable company' and a 'charitable trust' can be found throughout the legislation on tax reliefs and exemptions for charities. The definition of a 'charity' relies in most cases upon case law and the measure explicitly incorporates the case law definition of a charity under the law of England and Wales into the new definition of an organisation eligible for UK charity tax reliefs.
- 3.40.** A new definition of an organisation eligible for charity tax reliefs and exemptions will be introduced, applicable to all UK charitable tax reliefs and exemptions administered by HMRC. An eligible organisation must be:
- set up for charitable purposes only, within the meaning of the Charities Acts 2003 and 2006;
  - located in a member state of the EU or other territory specified in regulations by HMRC (Iceland and Norway will be specified as soon as possible after FB 2010 receives Royal Assent);

- regulated by any body in their home country with an equivalent function to the Charity Commission or any similar regulator, as required by the law of the home country; and
  - supervised by 'managers' (trustees, directors and other persons with a management function) who are 'fit and proper' persons.
- 3.41.** CASCs, and their non-UK equivalents, will also be required to meet the location condition above and their 'managers' must also meet the 'fit and proper' persons test.
- 3.42.** Additional changes to the regime for charitable tax reliefs and exemptions will be introduced to ensure existing provisions work for both UK and non-UK organisations, namely:
- organisations will be required to apply donations received under Payroll Giving for charitable purposes, if the donations are to remain tax-exempt; and
  - the rules requiring UK charities that make payments to bodies outside the UK to take reasonable steps to ensure the monies are used for genuine charitable purposes will be strengthened.
- 3.43.** A number of other changes to legislation will also be introduced to ensure they work effectively within the new regime, namely:
- the rules on recovering tax overpaid to charities under Gift Aid where an individual has not paid enough tax to cover the donation will be amended to apply the same treatment to UK resident and non-UK resident donors; and
  - the practice of HMRC making repayments of tax under Gift Aid to charitable companies before the end of the tax year on a concessionary basis will be put on a statutory basis.
- 3.44.** In order to maintain current service levels to UK charities whilst dealing with additional demand from organisations outside the UK, HMRC will introduce new procedures for making repayments of tax to charities under Gift Aid. The new procedures will include:
- restrictions on the number of in-year repayments that may be claimed, and the amount of each claim (currently a charity may make an unlimited number of claims); and
  - new forms for making a claim.

3.45. HMRC will be consulting informally with charities on the detail of these proposals over the next few months. In the meantime, detailed questions and answers were published on 24.3.10 on the HMRC website.

3.46. One of the questions asks: Will eligibility to UK charitable tax reliefs be available retrospectively to non-UK charities? HMRC's reply: Claims to charitable tax reliefs in respect of organisations equivalent to UK charities in the EU, Norway or Iceland on or after the date of the ECJ judgment on 27.1.09 will be considered on a case by case basis.

#### **The remittance basis: relevant person**

3.47. The remittance basis is an optional basis of taxation available to individuals who are resident but either not domiciled or not ordinarily resident in the UK. Individuals who choose to use the remittance basis will be subject to UK tax on their foreign income and gains only when they are remitted to the UK, rather than on their total worldwide income and gains.

3.48. Finance Act (FA) 2008 introduced significant changes to the remittance basis which became effective from 6.4.08. Minor amendments to these rules were made in FA 2009 which were designed to make the rules clearer and simpler to operate in practice. Finance Bill 2010 introduces a further minor amendment to the remittance basis.

3.49. The concept of relevant person was introduced in FA 2008 to ensure that any foreign income or gains of an individual which are remitted to the UK by way of any relevant person, or for the benefit or enjoyment of any relevant person, are taxed on the individual. A relevant person is widely defined and includes the individual, their spouse, civil partner, children and grandchildren under the age of 18. It also covers close companies and their subsidiaries in which such persons are participators.

3.50. However, it is not explicit that references to a close company are intended to include subsidiaries of non-resident companies which would be close companies if they were resident in the UK. To remove any uncertainty, and to remove the potential for abuse, the legislation will be amended to make clear that a relevant person includes such companies.

3.51. This change will have effect on and after 6.4.10.

#### **Care providers to children**

3.52. Income from providing care is normally taxed under the trading income rules, or the rules for miscellaneous income. However, there are special income tax rules for foster carers,

those who have adopted a child, and shared lives carers. A new income tax relief for the latter was announced in the 2009 pre-Budget report.

**3.53.** Following informal consultation about the latter, it has been decided that carers who take on legal parental responsibility for a child should be taxed in a similar way to those who have adopted a child. Therefore a new income tax exemption for special guardians and certain kinship carers will be introduced.

**3.54.** Qualifying payments are payments:

- by the child's parents or payments by, or on behalf of, the local authority;
- to a qualifying carer; and
- which are made in relation to a special guardianship order or a residence order.

**3.55.** Qualifying carers are individuals who care for one or more children placed with them under:

- a special guardianship order; or
- a residence order, where the individual is not the child's parent or step-parent.

**3.56.** Kinship carers who are providing care to a child who has not been placed with them under a residence order will not be a qualifying carer for the purposes of this income tax exemption. However, they will be entitled to claim the new income tax relief for shared lives carers.

**3.57.** Qualifying carers will not be able to claim the new income tax relief for shared lives carers, as they will be exempt from income tax on their caring income instead.

#### **Income tax adjustments between settlors and trustees**

**3.58.** Settlors (people who set up a trust) may receive repayments of tax on trust income if they are liable to income tax at a lower rate than the trustees. This measure will require settlors to pay any such repayments of tax they receive to the trustees. The result of this will be that these payments to trustees will be disregarded for inheritance tax purposes.

**3.59.** The Government intends to legislate this measure in a Finance Bill to be introduced as soon as possible in the next Parliament. The measure will have effect for repayments relating to income tax chargeable on or after 6.4.10.

<b>Comment</b>
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This measure is almost certainly aimed at situations where a discretionary trust will be paying the trust rate of 50% with effect from 6.4.10, whereas a settlor may be a marginal 40% taxpayer thus obviously otherwise in line for a repayment of tax suffered by the trustees.

## OTHER DEVELOPMENTS

### Residence: temporary purposes

#### *The issue*

- 3.60. Whether the appellant was resident in the UK for the tax years 1997-98 to 2002-03.

#### *The facts*

- 3.61. G was an airline pilot, flying long-haul flights for BA out of Gatwick or Heathrow. He had to be in England for some days before any outward flight and, in practice, sometimes between inward and outward flights. From 1986 to 1997 he had been resident in the UK, latterly owning and living in a house in Horley. In August 1997, he took a rented apartment in Cape Town, and later bought a house there. He contended that, since then, he had not been resident in the UK, spending as much time in Cape Town as possible, consistent with performing his duties, and intending to spend his retirement there in due course. HMRC argued that his continued presence in the UK, as the base from which he did his work, showed that he was still resident here, just as he had been before 1997.
- 3.62. The Special Commissioner had decided that s336 TA 1988 ('temporary residents in the UK') applied to the case. On HMRC's appeal, Lewison J held in the High Court that 'the recurrent nature of his regular presence in the UK [led] inevitably to the conclusion that his purpose for being here [was] neither casual nor transitory'. It could not be described as a temporary purpose; hence s336 did not apply. He went on to conclude that the commissioner had misdirected herself in law and that there was only one possible answer on the primary facts found, namely that G was resident.
- 3.63. G appealed, contending that the Special Commissioner had been right, or alternatively that if there was any error of law in her ruling, the question should be remitted for a fresh decision.

#### *The decision (CA)*

- 3.64. The court drew attention to the fact that, even if G did not satisfy s336, it did not follow that he was resident for tax purposes. It concluded that s336 was not, in fact, relevant: G's presence in the UK before every outward long-haul flight and between flights on some occasions, the UK being the base from which he operated as a pilot, did not fit the statutory words 'who is in the United Kingdom for some temporary purpose only'. The

court accepted that G was not in the UK 'with the intention of establishing his residence' here; he had previously established his residence in the UK and the question was whether he had retained it or not. However that question was not to be decided on the basis of temporary purposes.

- 3.65.** Lewison J had concluded that there was only one answer possible on the facts, namely that G was resident, but the Court of Appeal disagreed, even if a resident conclusion was likely. It would be wrong to treat G's presence for the purposes of his employment as a factor which necessarily showed residence; it was necessary to take into account, weigh up and balance all relevant factors, those connecting him with the UK on the one hand, and his connections with South Africa on the other hand, in terms of satisfying the non-statutory tests for residence and ordinary residence.
- 3.66.** The decision was that the commissioner had misdirected herself in law and hence the High Court had been right to allow HMRC's appeal. However it should then have remitted the case for re-hearing; the Court of Appeal now ordered this to be done (by the First Tier Tribunal).
- (Grace v HMRC ChD 28.10.09)*

### **Residence: breaking family ties**

#### ***The issue***

- 3.67.** Whether HMRC could add or needed to add wording into IR20 retrospectively, relating to the need to cut ties to the UK to become non-resident.

#### ***The facts***

- 3.68.** In November 2006, HMRC determined that the taxpayers in the first appeal were ordinary residents in the UK. The taxpayers sought judicial review of that decision which, following appeal was granted.
- 3.69.** In the second appeal, HMRC rejected the taxpayer's contention that he had not been resident or ordinarily resident in the UK from 1993 to 2004. The taxpayer sought judicial review of that decision and again, after appeal, that was granted.
- 3.70.** The taxpayers contended that it was not necessary to demonstrate that they had severed ties to the extent that previous social and family ties in the UK were no longer retained. They maintained that it was not until 2004-05 that HMRC had sought to require taxpayers to demonstrate that they had made a distinct break from ties in the UK in order to establish that they had left permanently or indefinitely. They submitted that such a change in approach first applied to them after they had left and breached their legitimate expectation that the authorities would continue, as a matter of practice, to apply IR20 in

the manner in which it had been applied consistently in the past, until it publicly announced that it proposed to change its practice for the future. Full facts of the Gaines-Cooper argument are included in our analysis of the Special Commissioners' case.

***The decision (CA)***

- 3.71.** The adverbs 'permanently or indefinitely' made, as a matter of construction, all the difference to an individual's departure from the UK. The extent to which a taxpayer retained social and family ties within the UK had to have a significant and often dispositive impact on the question whether a taxpayer had left permanently or indefinitely (for at least three years). It made no sense to construe 'leave' when qualified by the adverbs permanently or indefinitely as referring to the process of going abroad. The description, in IR20, of the evidence required to establish permanent or indefinite absence demonstrated the need to cut existing ties with the UK.
- 3.72.** It would be absurd if a taxpayer could acquire non-resident status on the basis of his claim that he had left permanently or indefinitely, without establishing that he had severed social and family ties in the UK, merely because he could not provide the evidence he had done so.
- 3.73.** There was no public law obligation of fairness which prevented HMRC from increasing, without warning, the intensity of inquiry or scrutiny of claims to be non-resident. That they might, in the past, have adopted an attitude of laissez-faire was not and ought not to be a guarantee that they would continue to do so, even without any prior warning of a change in attitude. Indeed, the absence of warning might be a powerful tool to deploy to ensure that taxpayers provided frank disclosure.
- 3.74.** HMRC had not altered their interpretation and application of IR20 to the taxpayers' cases.

***Comment***

- 3.75.** It has been widely reported that Mr Gaines-Cooper will appeal to the Supreme Court to try to avoid a tax bill estimated to be in the region of £30m. Many commentators have suggested that a statutory residence test may follow this case.

*(R (on the application of Davies and anor) v HMRC; R (on the application of Gaines-Cooper) v HMRC CA 17.2.10)*

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## 4. Capital taxation

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### Capital gains tax: rates and annual exemption

- 4.1. The Chancellor confirmed that he would not make any increase in the rate of capital gains tax, which therefore remains at 18%.
- 4.2. The annual exemption for individuals is to be frozen at its value in 2009-10, ie £10,100. Trustees' gains usually benefit from an annual exempt amount of one-half of this, ie £5,050.

### Capital gains tax: entrepreneurs' relief

- 4.3. The amount of an individual's gains that can qualify for entrepreneurs' relief is subject to a lifetime limit of £1 million. For trustees, the £1 million limit is that of the beneficiary of the settlement who meets the conditions for the trustees to claim the relief.
- 4.4. FB 2010 will include provision to increase that limit to £2 million from 6.4.10.
- 4.5. Where individuals or trustees make qualifying gains above the previous £1 million limit before 6.4.10, no additional relief will be allowed for the excess above the old limit. But if they make further qualifying gains after 5.4.10, they will be able to claim relief on up to a further £1 million of those additional gains, giving relief on accumulated qualifying gains up to the new limit of £2 million.
- 4.6. The other rules for entrepreneurs' relief are unchanged. Gains qualifying for the relief will continue to be reduced by the fraction 4/9, leaving the effective rate of capital gains tax on these gains at 10%.

### Inheritance tax: nil rate band

- 4.7. IHT is payable on the value transferred by a chargeable transfer above the nil rate band. The nil rate band is increased automatically each year in line with inflation unless an alternative nil rate band is provided for. Finance Act 2007 currently provides that it will rise to £350,000 for transfers made (or deemed to be made) on or after 6.4.10.
- 4.8. The 2009 PBR measure proposed to override this planned increase and instead retain the threshold at £325,000. This will now be extended to cover the tax years 2011-12 to 2014-15 as well.

### Comment

- 4.9. But there was no announcement of an increase in the rates of inheritance tax as some were predicting. It remains at 40% on the excess of value transferred over the nil rate

band. For lifetime transfers to individuals, potential exemption is confirmed if the donor survives the gift by seven years.

#### Stamp duty land tax: thresholds and rates

- 4.10.** Legislation in FB 2010 will introduce a higher stamp duty land tax (SDLT) rate of 5% for purchases of residential property where the consideration exceeds £1 million.
- 4.11.** The new higher rate will apply to residential purchases where the effective date (normally the date of completion) is on or after 6.4.11.
- 4.12.** With more immediate effect, there will be relief from SDLT for purchases of residential property at up to £250,000 where the purchaser or all the purchasers are first-time buyers and intend to occupy the property as their only or main home.
- 4.13.** This relief is time-limited to two years. It will be available for residential purchases where the effective date (normally the date of completion) is on or after 25.3.10 and before 25.3.12.

Stamp duty land tax (based on total value of consideration)				
Rate	Residential		Non-residential	
	2009-10	2010-11	2009-10	2010-11
0%	£0 - £125,000*	£0 - £125,000*	£0 - £150,000	£0 - £150,000
1%	Over £125,000 - £250,000**	Over £125,000 - £250,000†	Over £150,000 - £250,000	Over £150,000 - £250,000
3%	Over £250,000 - £500,000	Over £250,000 - £500,000	Over £250,000 - £500,000	Over £250,000 - £500,000
4%	Over £500,000	Over £500,000	Over £500,000	Over £500,000
*Starting residential threshold in 2,000 disadvantaged areas is £150,000 **SDLT holiday for residential transactions up to £175,000 applied until 31.12.09 †First time buyers can claim relief from SDLT on residential transactions up to £250,000 between 25.3.10 and 25.3.12				

#### Stamp duty land tax: partnerships

- 4.14.** The SDLT partnerships rules apply, broadly, to transactions between a partnership and one of the partners. The rules calculate the chargeable consideration of a land transaction according to the degree of connection, by way of the partnership, between the vendor and purchaser. These rules are being exploited for some land transactions by contriving a partnership relationship between the vendor and the purchaser such that the chargeable consideration, and thus the SDLT due, is greatly reduced.
- 4.15.** There are existing SDLT anti-avoidance rules which, where they apply, impose a charge on a 'notional land transaction'. The SDLT partnerships rules currently apply to a 'notional land transaction'.

- 4.16. The legislation in FB 2010 will disapply the partnerships rules from a 'notional land transaction'. Transactions which fall within the anti-avoidance rules will not benefit from the special partnerships rules for calculating chargeable consideration.
- 4.17. The effective date of a notional land transaction is, broadly, the date that the last scheme transaction occurs; 'scheme transactions' being the transactions that effectively make up the notional land transaction. The transitional rules provide that a notional land transaction where any of the scheme transactions is entered into before 24.3.10 will usually come under the old rules.

## OTHER DEVELOPMENTS

### Taper relief: non-business apportionment

#### *The issue*

- 4.18. The apportionment for the purposes of taper relief of a gain arising on the disposal of an asset used both for business and non-business purposes.

#### *The facts*

- 4.19. Mr and Mrs J owned a hotel building which, it was agreed between the parties, was used as to 35% for the hotel business and as to 65% for their own residential purposes. 65% of the gain was thus exempted by s222 TCGA 1992 (PPRR), leaving a balance of £201,931. The parties agreed that PPRR should be applied before the application of any other CGT reliefs and in particular before the application of taper relief.
- 4.20. In applying the taper relief rules of s2A and sch A1 TCGA, HMRC argued that the gain arose on the disposal of an asset which had been used only partially for business purposes and therefore had to be further apportioned:

	Business (35%) £	Non- business (65%) £
Gain	70,676	131,255
Relief (75%/15%)	<u>53,007</u>	<u>19,688</u>
Chargeable	<u>£17,669</u>	<u>£111,567</u>
Total (pre-AE)		<u>£129,236</u>

- 4.21. The taxpayers, in contrast, argued that no apportionment need be made for taper relief purposes since such an apportionment has been made for PPRR purposes; the whole gain would qualify for the business asset rate of taper relief (BATR), 75%, leaving £50,483 chargeable. HMRC acknowledged that any other conclusion would not appear intuitive; however:

- the hotel was acquired and disposed of as a single asset;
- the chargeable gains arising were the gains accruing on the sale of the hotel minus PPRR;
- the chargeable gains arose from the disposal of the whole asset and not just the part used for the taxpayers' business; and
- these chargeable gains were subject to taper relief and had to be apportioned into a business and a non-business gain in order to calculate taper relief.

### ***The decision (FTT)***

- 4.22.** The Tribunal Judge observed that s222 operates by removing the gain, or a part of the gain, from charge, not by removing the asset, or any part of the asset from charge. Mr and Mrs J argued that the reference to 'parts' of the asset used exclusively for business purposes in s224 meant that s222 operates by removing that part of the asset from charge. The tribunal did not agree: the section is concerned with apportioning and relieving the gain arising from the asset, not in apportioning the asset itself.
- 4.23.** The definition of 'business asset' for taper relief and 'business gain' for PPRR purposes are not exactly the same. It would be possible in theory to have a non-PPRR gain for the purposes of s224 which did not qualify for BATR and vice-versa. Here, it had been agreed between the parties that the business/non-business apportionments should be the same for both purposes.
- 4.24.** The essence of the issue was that the taper relief legislation at s2A(3) asks not whether the gain for which relief is sought is a gain arising from an asset (or part of an asset) which was used exclusively for business purposes, but whether it is the gain on the disposal of a business asset. Since PPRR had not removed the asset from charge, the taper relief rules had to operate on the whole asset. The legislation did not provide room to argue that only a proportionate part of the asset needed to be considered for taper relief purposes. However, the specific requirement of para 21 sch A1 was that any apportionments should be done on a just and reasonable basis: the apportionment which should be made was to apportion the chargeable gains on the basis that there is no proportion of the use of the asset which is a non-qualifying use.
- 4.25.** The taxpayers' appeal was thus allowed.

### ***Comment***

- 4.26.** The problems associated with disposing of flats above shops was considered at length by Mike Truman in *Taxation* magazine on 14.7.05 and 8.9.05. He concluded that an

adviser may have been better off trying to persuade HMRC that Statement of Practice D1 applied on a non-statutory basis instead. This statement allows the owner of an estate to sell off individual parts of the estate, such as fields, as if they are separate assets rather than treating them as part-disposals of the main asset.

- 4.27. The result of this case will interest anyone who used part of their residence for business purposes (eg hoteliers, guest-house owners, publicans, home-workers) and anyone who disposed of a property prior to 2008 or is still arguing about the computations with HMRC. Many taxpayers will have used HMRC's method of calculation, many will have not.

*(Jefferies v HMRC TC00235 29.10.09; comment by Nichola Ross Martin in Taxation 10.12.09)*

### **Let property taper relief**

#### ***The issue***

- 4.28. Whether a let property qualified for business asset taper relief.

#### ***The facts***

- 4.29. In 1984, a brother and sister were given a property which they then held as joint tenants. They divided the house into fully-furnished bedsits, which they let to tenants. In 2005, they sold the house and treated the gain in their tax returns as qualifying for business asset taper relief. HMRC issued amendments to their self assessments on the basis that the house was not a business asset: the income received from the property was letting income and not trading income; accordingly business asset taper relief was not applicable
- 4.30. The vendors appealed, contending that an inspector of taxes had previously agreed that their income from letting the bedsits qualified as earned income. Two accountants who had acted for them gave evidence that inspectors had accepted this categorisation, although neither had retained correspondence to this effect.
- 4.31. HMRC's view was that no evidence had been provided to suggest that services had been rendered beyond those which a landlord would normally be expected to undertake in normal course of conducting a rental business. A letting activity would only constitute a trade where the owner remained in occupation of the property and provided services over and above those usually provided by a landlord.

#### ***The decision (FTT)***

- 4.32. The tribunal dismissed the appeals, holding that the income which the vendors had received from letting the bedsits was not trading income and the house did not qualify as

a business asset. The relevant legislation and case law - ie *Salisbury House Estate Ltd v Fry* and *Griffiths v Jackson* – clearly show that annual profits from property have always been assessed under the rules applicable to Schedule A income and not under Schedule D as a trade.

- 4.33. Furthermore, there had to be a clear and unambiguous representation by HMRC upon which the appellant has relied before it could be held that it was unfair for HMRC to undertake their tax collection obligations under legislation.

*(MG Jones v HMRC (and related appeal) TC00256 8.12.09)*

### **Non-compulsory repurchase of land**

#### ***The issue***

- 4.34. Whether a plot of land had been subject to a compulsory repurchase order and accordingly whether the taxpayer could claim rollover relief.

#### ***The facts***

- 4.35. A acquired the right to build a restaurant on land by a grant from the Milton Keynes Development Corporation (MKDC), with the plans for the construction of the restaurant approved by the Commission for the New Towns (CNT) which had succeeded to some of the functions of MKDC.
- 4.36. A 125-year lease of the land was granted for a purchase price of £160,000, payable by instalments, and CNT agreed to transfer the freehold of the land for a consideration of £1, once the development of the restaurant was complete. The terms of the lease included a restrictive covenant, the effect of which was that A was prevented from assigning, under-letting or transferring the lease.
- 4.37. The plans to build the restaurant were abandoned after local residents became aware of the proposed development and objected to it. As a result of the objections the CNT approached A with a view to him ceasing or abandoning the development.
- 4.38. A accepted the CNT's proposal that he give up his interest in the land on the basis that he would be granted an alternative site in Milton Keynes. He agreed to sell his interest in the land to Abbeygate, whose purpose was to build a supermarket. He paid £50,000 to the CNT to remove the restrictive covenant from the lease and sold his resultant interest in the land to Abbeygate for £360,000.
- 4.39. A originally claimed rollover relief on the disposal of the land under s152 TCGA 1992 but this claim was withdrawn when he recognised that the land had not been used for the purposes of his trade. He then made a claim for rollover relief under s247 TCGA 1992 which states that relief is available for land disposed of by any person to an authority

exercising or having compulsory powers. A argued that the relief was available where a compulsory purchase could be authorised and, as he had only sold following CNT's approach, he was entitled to claim.

- 4.40. HMRC submitted that the CNT did not have powers to purchase land compulsorily and that, even if it did, the land was not disposed of by A to 'an authority exercising or having compulsory powers' to acquire it for the purposes for which it was acquired.

***The decision (FTT)***

- 4.41. The rollover relief provided for by s247 TCGA 1992 applies only in a case where land is disposed of to an authority exercising or having compulsory powers. In this case A disposed of the land to Abbeygate. The relief can therefore only apply to the disposal if Abbeygate is an authority exercising or having compulsory powers. It is not and it could not be said that CNT were acquiring the land on Abbeygate's behalf.
- 4.42. The appeal was dismissed and the assessment to capital gains tax determined.  
(*Abdul Ahad v HMRC TC00291 13.1.10*)

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**5. Administration and miscellaneous**

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**Disclosure of tax avoidance schemes**

- 5.1.** Legislation will be introduced in FB 2010 revising the Disclosure of Tax Avoidance Scheme (DOTAS) and providing for increased penalties for failure to comply with the rules.
- 5.2.** Regulations, not dependent upon the Bill, will be laid revising and extending the DOTAS 'hallmarks' (descriptions of schemes required to be disclosed).
- 5.3.** NIC regulations will mirror the tax changes in primary and secondary legislation, to the extent that they concern income tax.
- 5.4.** Part 7 FA 2004 and regulations (the disclosure regulations) require certain persons (normally the promoter but in some cases the user) of tax schemes falling within certain descriptions to provide information to HMRC about the scheme within certain time limits.
- 5.5.** HMRC may allocate a scheme reference number (SRN) to a disclosed scheme. Promoters must pass the SRN to their clients who have entered into the scheme. Clients who are intermediaries must pass on a SRN to persons it knows to be end users of the scheme. Scheme users are required to report the use of the scheme back to HMRC.
- 5.6.** FB 2010 amends part 7 FA 2004 and s98C TMA 1970 to strengthen and improve the DOTAS regime. The new and amended provisions:
- introduce a new 'trigger point' for the disclosure of actively marketed schemes – the point at which a promoter first communicates a fully designed scheme to a third party for the purpose of obtaining clients of that scheme;
  - include a new requirement for a person who introduces a client to a notifiable scheme to provide HMRC with the name and address of the promoter who provided them with details of that scheme;
  - increase the penalties for failure to comply with a disclosure obligation, subject to determination by the Tribunal; and
  - introduce a new requirement for promoters to provide HMRC with periodic information about clients who implement a notifiable scheme for SRNs issued on or after the date the regulations come into force.
- 5.7.** FB 2010 will contain substantive provisions and powers to make regulations. The substantive powers will come into effect on separate days to be appointed by Order. It is

expected that the substantive provisions and the regulations (including both the Descriptions Regulations and the NIC regulations) will come into effect on a common date in autumn 2010.

#### **Relief for overpayments of stamp duty land tax**

- 5.8.** This measure will amend the SDLT (and PRT) error or mistake relief rules. This follows similar changes to the income tax, capital gains tax and corporation tax rules in the FA 2009. The changes will provide a means of reclaiming overpayments where there is no other statutory route. They will ensure there is a comprehensive statutory scheme of remedies in such cases.
- 5.9.** Para 34 sch 10 FA 2003 provides relief in cases where a person has overpaid tax under an assessment to SDLT that is excessive due to a mistake in a land transaction return.
- 5.10.** The time limit for claiming repayments is currently six years. From 1.4.11 they must be claimed within four years.
- 5.11.** No repayment is given where the return followed the general practice at the time it was made, or where the mistake is governed by another statutory claim.
- 5.12.** The measure will remove the requirement that the overpayment must be the result of a mistake in a return and that it must be made under an assessment.
- 5.13.** The measure will also provide that HMRC are not liable to repay an amount except as provided by the measure or by another provision of the Taxes Acts.
- 5.14.** The current restrictions on the right of appeal will be removed, allowing an appeal to the courts on the same grounds as appeals against other matters.
- 5.15.** The Government intend to legislate this measure in a Finance Bill to be introduced as soon as possible in the next Parliament. To allow a transitional period in which claims can be made under the old rules, the measure will have effect on and after 1.4.11.

#### **Interest harmonisation for corporation tax**

- 5.16.** This measure will bring CT (and PRT) within the harmonised interest regime introduced in the FA 2009. The harmonised interest regime will apply to all late payments and repayments of taxes and duties administered by HMRC.
- 5.17.** The new harmonised interest provisions replace the current range of differing regimes with a single legislative framework for interest chargeable on late payments and payable on repayments which will apply to all taxes and duties administered by HMRC. Interest

will be charged from the date the tax or duty was due to be paid to HMRC until the date it is paid.

- 5.18.** HMRC will pay interest on repayments from the date the tax or duty was due to be paid or, if later, the date the payment was actually received, to the date the repayment is made.
- 5.19.** The Government intend to legislate this measure in a Finance Bill to be introduced as soon as possible in the next Parliament. Implementation of interest harmonisation requires changes to a number of HMRC computer and operational systems and is to be phased in over a number of years. The new provisions will be brought into effect by Treasury Orders which will specify the dates from which they have effect.

#### **Penalties for late filing of returns and payment of tax**

- 5.20.** This measure will complete the reform of the penalty regimes for late filing of tax returns and late payment of tax.
- 5.21.** It will affect taxpayers who do not file their tax returns on time or pay their tax liabilities in full and on time for:
- VAT and insurance premium tax;
  - aggregates levy, climate change levy and landfill tax;
  - air passenger duty, alcoholic liquor duties, tobacco products duty,
  - hydrocarbon oil duties, general betting duty, pool betting duty, bingo
  - duty, lottery duty, gaming duty and remote gaming duty; and
  - other excise duties.
- 5.22.** This measure will not have effect for tax credits.
- 5.23.** The late filing and late payment penalty models are broadly similar. These are designed to encourage filing and payment by the correct dates by introducing an escalating series of penalties depending upon the number of failures within a set penalty period. Further penalties will arise if there is a prolonged delay in filing returns or paying the tax due.
- 5.24.** The new penalties will include a right of appeal against penalty decisions if the taxpayer has a reasonable excuse for the lateness. Late payment penalties may also be avoided where taxpayers have agreed a time to pay arrangement with HMRC.

5.25. The key elements of the new penalty models are as follows:

***Penalties for late filing returns (quarterly)***

- £100 penalty immediately after the due date for filing (whether or not the tax has been paid);
- the failure also starts a penalty period, which is set for a year;
- if there are further failures within the penalty period, then the fixed penalty escalates by £100 for each of those subsequent failures, up to a maximum of £400 per failure. The penalty period is also extended to the first anniversary of the latest failure;
- if any of the failures are prolonged, then additional penalties of 5% of the tax on the relevant return are charged at six and 12 months from the date of the failure; and
- if, by failing to make the return, the taxpayer is deliberately withholding information to prevent HMRC from correctly assessing the liability to tax, then penalties of up to 100% of the tax on the return may be chargeable.

***Penalties for late filing returns (monthly)***

- This is a very similar structure to the quarterly model above, except that the fixed penalties are £100 for the first three failures in any penalty period, £200 for the second three failures, etc. up to a maximum of £400 per failure.

***Penalties for late payments (quarterly)***

- Where a taxpayer first pays late, although there is no penalty, it does start a penalty period, which is set for a period of a year;
- any further failures within that period will attract a penalty of 2% of the unpaid tax, as well as extending the penalty period to the first anniversary of the latest failure;
- a third failure within the period will attract a penalty of 3%, with further failures attracting a maximum of 4%; and
- if any of the failures are prolonged, then additional penalties of 5% of the unpaid tax are charged at six and twelve months from the date of the failure.

**Penalties for late payment (monthly)**

- This is a very similar structure to the quarterly model above, except that, after the first failure, the tax-geared penalties are 1% for the next three failures in any penalty period, 2% of the next three failures, etc, up to a maximum of 4% per failure.
- 5.26. There are special provisions to deal with circumstances where taxpayers may change from a monthly to a quarterly return, or where exceptional payment obligations may arise.
- 5.27. The Government intends to legislate this measure in a Finance Bill to be introduced as soon as possible in the next Parliament. Implementation of new penalties for late filing and late payment requires changes to HMRC computer systems and internal processes and is to be staged over a number of years. The new provisions will be brought into effect by Treasury Orders which will specify the dates from which they have effect.

**Offshore tax evasion**

- 5.28. Legislation will be introduced in FB 2010 to provide for larger penalties for taxpayers who fail to provide a full account of their income tax or capital gains tax liabilities, where the failure is linked to an offshore matter.
- 5.29. Penalties for under-declaration of tax are determined by sch 24 FA 2007 (penalties for inaccuracies in returns), sch 41 FA 2008 (penalties for failure to notify) and sch 55 FA 2009 (penalties for failure to make a return).
- 5.30. Each of these schedules provides for tax-geared penalties. The level of the penalty is determined by the behaviour of the taxpayer and the quality of disclosure.
- 5.31. The mechanics of the penalty frameworks will remain the same, but the absolute level of the percentage used to determine the tax-geared penalty will be determined by the jurisdiction in which the non-compliance arises.
- 5.32. Where the non-compliance occurs in a jurisdiction which has provision to exchange information on savings income automatically with the UK, the penalty percentages will be the same as those in the current schedules (i.e. the same as for non-compliance arising in the UK).
- 5.33. Where the non-compliance arises in a jurisdiction which has agreed to exchange information with the UK, but does not automatically share that information, the penalty percentages will be 1.5 times those set out in the existing Schedules.

- 5.34.** Where the non-compliance arises in a jurisdiction which has not agreed to exchange information with the UK, the penalty percentages will be double those set out in the existing Schedules.
- 5.35.** The safeguards built into the existing penalties legislation will apply equally in the case of offshore non-compliance.
- 5.36.** The new penalty frameworks for offshore non-compliance will apply to income tax and capital gains tax. It is expected that the new penalty framework will apply to tax periods commencing on or after 1.4.11.

#### **Excise modernisation and compliance checks**

- 5.37.** This measure will update the compliance checking framework for excise duties, including:
- modernising information and inspection powers; and
  - aligning the record-keeping rules and the time limits for assessments and claims with changes made to other taxes and duties.

#### ***Record-keeping***

- 5.38.** The current legislation in the Customs and Excise Management Act 1979 (CEMA) on excise record-keeping is now slightly out of step with the other taxes. This will be changed so that the high-level rules for record-keeping are aligned across all taxes and duties. It will not change the detailed rules on what information needs to be kept.
- 5.39.** The existing information and inspection powers in CEMA will be updated, as in the table below:

<b>Existing Power</b>	<b>Elements of proposal that are new, aligned or unchanged</b>
To enter premises of revenue traders	A new element that would permit inspection of documents.
To enter premises of those thought to be acting as revenue traders	A new power to inspect documents is included.
To enter premises used by a revenue trader	Clarification that the existing powers include the power to enter premises used by a revenue trader, even if those premises are owned by another.

Existing Power	Elements of proposal that are new, aligned or unchanged
To make unannounced visits	No change.
Prohibition of inspection of wholly private premises	This is current practice but is now made explicit.
Application for a warrant to search (section 161A)	The power exists but would be extended to search for documents required to accompany the goods.
Information from those who may hold relevant information	This is new and would allow HM Revenue & Customs (HMRC) to seek information from other parties such as banks. Safeguards would be a formal notice requirement, pre-authorised by a tribunal.

### ***Time limits***

- 5.40.** As time limits across other taxes and duties have been aligned in recent years, excise is now out of step. The standard time limit for making claims and assessments will be increased from three to four years. The extended twenty-year time limit for deliberate underpayment of excise duty will be retained but the terminology used to describe the behaviours subject to it will be aligned with recent penalties legislation.
- 5.41.** Time limits for making assessments and claims need a transitional period and are not expected to become fully operative before 1.4.12.
- 5.42.** Treasury orders will bring the changes into effect and specify the operative date. The record-keeping changes and amendments to information and inspection powers are expected to have effect from 1.4.11.

### **Security for payment of PAYE**

- 5.43.** Legislation will be introduced in FB 2010 to allow HMRC to require a financial security from employers where amounts due under PAYE or NIC obligations are seriously at risk. The amount of security will be set by HMRC in the light of the potential tax liability.
- 5.44.** The detailed arrangements for this security will be set out in regulations. These will provide that HMRC will require a security by notice and set out the right of appeal against the imposition of the security and the amount.
- 5.45.** There will be a full twelve week consultation on the regulations.

- 5.46.** The measure introduces a new criminal offence where a person required to give a security fails to do so. If the person is found guilty of the offence they may be fined (up to level 5 of the standard criminal scale (£5,000)).
- 5.47.** There are similar provisions requiring businesses to provide financial security where HMRC believes that VAT revenue is at risk because those running the business do not intend to meet their obligations. There is currently no similar power for HMRC to require a security within PAYE or NIC legislation.
- 5.48.** S684 ITEPA 2003 will be amended to include provisions allowing HMRC to require security in the matters that can be covered in PAYE regulations. It will also set out the new offence of failing to provide security. Similar provisions will be made for NIC through regulations using existing powers.
- 5.49.** The measure will not have effect until regulations are made and the intention is that the operative date will be 6.4.11.

#### **Landline duty**

- 5.50.** Legislation will be introduced in FB 2010 to establish a new duty on landlines in the UK. Accompanying secondary legislation will be laid after FB 2010 has received Royal Assent.
- 5.51.** The duty will be set at 50 pence per line per month. The duty will apply when a local loop is made available for use and will be payable by the owner of the loop. It is expected that the owners will recoup the duty from the end user, wholesaler or retailer.
- 5.52.** The duty has effect on and after 1.10.10.

#### **Small business rate relief**

- 5.53.** The Budget announces that the Government will fund a temporary increase in the level of small business rate relief in England, so that eligible small businesses occupying properties with rateable values up to £6,000 will pay no business rates for one year from October 2010. Small businesses that benefit from the rate relief taper (rateable values up to £12,000) will receive significant reductions.

#### **HMRC online and other support for businesses**

- 5.54.** HMRC will build on the success of Time to Pay in engaging with businesses early and offering a single point of contact by enhancing the online support it provides to SMEs by the end of 2011. This will include personalising businesslink.gov.uk for start-ups and making it easier for businesses to register for multiple taxes online with a single interactive form.

**OTHER DEVELOPMENTS****Working with agents**

- 5.55.** Proposals have been made which would allow HMRC to report members of professional bodies to their body. There was broad agreement in the first consultation that HMRC should use this power more effectively, so the principle seems to have been accepted.
- 5.56.** The tax authority already has a statutory authority lawfully to disclose information to a body regulating a profession, in relation to misconduct on the part of a member which relates to an HMRC function. The current consultation seeks to establish a method of reporting to be used by the tax authority which falls within these statutory powers.
- 5.57.** 'Misconduct' is not defined and discussions with the main professional bodies in the past has indicated that there is broad consensus about what it means: conduct likely to bring discredit on the member, the member's professional body or the profession as a whole. The policy intention was that the term should mean 'frequent error or unethical behaviour'. HMRC's current view is that the term can be interpreted to include persistent errors, failure to take reasonable care or negligence.
- 5.58.** Where a tax agent is a member of a professional body which acts as a regulatory body, the route is open for HMRC to make a formal report to that body. However, the tax authority views this as the last resort, and will therefore contact the agent directly where it believes that grounds exist for a report to be made to a professional body. This approach would identify whether there was indeed a problem, alert the agent to HMRC's concerns and attempt to agree a mechanism which would enable the agent to address the problems. Members may at this point seek support from their professional body, but if a solution can be found no report would be made.
- 5.59.** Only where a member did not wish to engage with HMRC, or a problem persisted despite efforts to resolve it, would HMRC seek to take formal steps to disclose details to the professional body.
- 5.60.** Those who are members of bodies which do not perform any regulatory function would be treated in the same way as those tax agents who are not affiliated to a body. Work will continue to establish appropriate civil sanctions to deal with poor work by such agents, but the initial approach to the agent regarding concerns identified by HMRC would be the same as for those who are members of a professional regulatory body.

**5.61.** The consultation states that in every case, HMRC would ensure that the misconduct was serious enough to warrant disclosure. This would require authorisation at a senior level independent of the officer who has investigated the behaviour.

*(Rebecca Benneyworth writing on AccountingWeb 15.2.10)*

#### **Agent penalties**

**5.62.** HMRC have also published draft legislation that would introduce new penalties for agents. The draft legislation was published on 8.2.10 and HMRC are seeking comments on it by 28.4.10 (extended from the original date of 3.3.10).

**5.63.** The new draft legislation covers two of the proposals set out in the consultation document:

- to allow HMRC to access the working papers of tax agents who engage in deliberate wrongdoing which leads or is intended to lead to a loss of tax; and
- to impose penalties on a tax agent who has been involved in deliberate wrongdoing.

**5.64.** The draft rules do not include anything in relation to the proposed 'naming and shaming' of agents involved in deliberate wrongdoing, nor do they include any provisions in respect of 'high volume agents'.

**5.65.** The ICAEW is very concerned about the draft legislation, in particular because the definitions of 'tax agent' and 'deliberate wrongdoing' are far too wide. So much so that ordinary tax planning appears to be included in the definition of deliberate wrongdoing and advice from a friend could constitute advice from a tax agent.

**5.66.** Chris Try, senior partner of Try Lunn and Co, a firm in Hull, said that the document 'constitutes a Pearl Harbour moment for all tax agents in the UK'. He went on to say that the draft legislation represents 'a declaration of unrestricted, total warfare against all of those who make the UK tax system work'.

**5.67.** Clause 3 of the draft legislation begins: 'A tax agent engages in deliberate wrongdoing if, with respect to the tax affairs of one or more clients:

'(a) the tax agent does an act that is capable (directly or indirectly) of bringing about a loss of tax; and

'(b) the act is done deliberately, with the intention of bringing about such a loss.

'(2) It does not matter whether a loss is actually brought about.

'(3) Nor does it matter whether the tax agent does the act alone or on the instruction of the client.

'(4) 'Loss of tax' means loss of revenue from tax, and includes a loss involving a relief, deduction, repayment or credit of any kind.'

**5.68.** This would bring capital allowance advice or advice relating to the timing of pension contributions in to the realms of 'deliberate wrongdoing'.

**5.69.** It appears that HMRC have listened to the barrage of criticism and have confirmed that following the extended consultation, legislation will not appear in this year's (first) Finance Bill.

*(ICAEW Tax Faculty website 16.2.10 and Taxation magazine 12.2.10)*

#### **Informal enquiry**

**5.70.** Practitioners familiar with the tax issues surrounding big companies and HMRC's review of links with large business will have come across the term 'collaborative engagement'. HMRC intend to 'engage with and respond to our customer population' and they make it clear that 'collaborative engagements' are not part of 'an intervention regime'. They recognise that 'this is a programme outside the statutory framework' and that there may be circumstances where 'a more formal intervention may be necessary'. But would HMRC ever think of extending a form of 'collaborative engagement' to smaller cases within local compliance?

**5.71.** Most tax agents are familiar with the terms 'tax investigation', 'tax enquiry' and 'compliance check'. But 'informal enquiry', what is that? HMRC have potentially always been able to ask taxpayers for information without opening a formal enquiry. However, apart from the poorly received pilot on interventions, the department has chosen not to do so.

**5.72.** Under the new sch 36 FA 2008 regime, HMRC have a broad range of formal powers to request information from the taxpayer and from third parties to check the taxpayer's 'tax position'. However, sch 36 para 21 provides that where a return (other than VAT or PAYE) has been submitted to HMRC, unless there is a suspicion of any loss of tax, a request for information can only be made if a formal enquiry is opened.

**5.73.** Informal enquiries have some possible advantages to the taxpayer. These include:

- resolution may well be quicker and HMRC may be more inclined to focus on a single, real, issue rather than asking a number of broad questions;

- costs of compliance may be lower because informal requests for information can be discussed enabling peripheral information to be set aside;
- there could be added flexibility in closing a case down: if HMRC officers can avoid the statutory enquiry opening and closing formalities, they might be more amenable in borderline cases to accepting a swift resolution; and
- by responding to an informal request, a tax agent should enjoy a better relationship with HMRC and any goodwill so gained might well assist when dealing with other clients.

**5.74.** Informal enquiries typically might involve queries raised in a letter, or possibly an HMRC officer will telephone either the accountant or, if unrepresented, the taxpayer, and ask for information to help them to consider a self assessment tax return. The caller will have a list of questions and where the officer is not satisfied with the initial response he will go on to request answers and documents in writing.

**5.75.** There is no reason why the receipt of a formal opening notice should prevent the adviser from working quickly and constructively with HMRC to obtain the advantages of the informal enquiry.

**5.76.** If the client decides that he wants the protection of a formal enquiry, the practitioner will need to notify HMRC accordingly and explain that, while the client wishes to move forward in a spirit of cooperation, before any information is supplied, the issue of a formal notice is required.

*(Mike Down and Gary Cryer writing in Taxation 19.11.09)*

#### **Enquiry window is now irrelevant**

**5.77.** HMRC now have a statutory power to undertake fishing expeditions into any person's tax affairs. They can use a compliance check to ask questions about a person's past, present or future liabilities to pay tax, make tax claims, or pay tax penalties. HMRC may also visit business premises with only seven days' notice (not seven working days) and may make unannounced visits. Advisers must use the privacy provisions of the Human Rights Act 1998 if requests to produce records become excessive.

*(Andrew Gotch speaking at TaxAid conference 30.10.09 reported in Taxation 23.11.09)*

#### **Taxman's powers of entry**

**5.78.** Reports tell of a street in the North East of England where several businesses received a surprise visit from someone claiming to be an HMRC officer, in the same afternoon. This is very strange, as HMRC have stated that its officers will only make unannounced visits to businesses where they suspect serious non-compliance. This is not likely to be the case for every business on one street.

- 5.79.** Where a visit has not been arranged in advance with the business owner, the HMRC officer must bring a notice stating that the visit has been authorised by either the First-Tier Tax Tribunal or by an authorised officer within HMRC. The officer should also present the business owner with compliance factsheet CC/FS4. Clients should be warned to be cautious of anyone claiming to be an HMRC officer, who turns up without an appointment. HMRC officers always carry identification documents and should be happy for the business owner to check their ID by a phone-call to their base office. The HMRC officer has no power to force entry to the premises, and the owner can ask the officers to wait outside until you arrive to support your client through the visit.

*(Mark Lee's Tax Advice Network practical tax newsletter, quoted in TAXline December 2009)*