Tax update

March 2017

In this month's update we report on HMRC's Spotlight 36 which has been issued in respect of planning designed to circumvent the loan taxation rules in Part 7A ITEPA; new draft legislation in relation to the taxation of non-domiciled individuals and a recent report by the Public Accounts Committee on the taxation of high net worth individuals. We also comment on three recent cases concerning misfeasance in public office; the transfer of a pension fund to a personal pension plan and motor racing sponsorship payments made to a family member.

News items

HMRC issues new Spotlight on planning intended to avoid new rules on disguised remuneration loan charges

HMRC has published a new Spotlight to deal with new, or proposed tax products, which are intended to circumvent the new rules on the taxation of loans under the disguised remuneration rules in Part 7A of the Income Tax (Earnings and Pensions) Act 2003. more›

Draft legislation on the taxation of non-domiciled individuals

The Government has published further draft legislation on proposed reforms to the taxation of non-domiciled individuals. The draft legislation (which includes explanatory notes) is expected to be included in the Finance Bill 2017. more›

Report of the Public Accounts Committee on taxing high net worth individuals

The Public Accounts Committee has released a Report urging the Government to be tougher and clearer in its approach to taxing the wealthy including, in particular, those who participate in tax avoidance or tax evasion. more›

Case reports

Sandhu – Timing and detail critical in misfeasance claims against HMRC

In *Monmohan Sandhu v HMRC* [2017] EWHC 60 (QB), the claimant, who had been wrongly convicted of cheating the public revenue, had his claim of misfeasance in public office against HMRC struck out by the High Court because it was brought too late and he had failed adequately to plead his case. more›

Any comments or queries

Adam Craggs
Partner
+44 20 3060 6421
adam.craggs@rpc.co.uk

Robert Waterson
Senior Associate
+44 20 3060 6245
robert.waterson@rpc.co.uk

Michelle Sloane
Senior Associate
+44 20 3060 6255
michelle.sloane@rpc.co.uk

About this update

The Tax update is published on the first Thursday of every month, and is written by members of RPC's Tax Dispute team.

We also publish a VAT update on the final Thursday of every month, and a weekly blog, RPC Tax Take.

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Parry & Others – Upper Tribunal confirms that the transfer of a pension fund to a personal pension plan is not a transfer of value for IHT purposes

In *HMRC v Parry & Others* [2017] UKUT 4 (TCC), the Upper Tribunal (UT) held that a transfer of funds from a registered pension scheme to a personal pension plan made by the deceased shortly before her death was not a "transfer of value" for the purposes of section 3, Inheritance Tax Act 1984 (IHTA). Similarly, the deceased's omission to exercise her right to take lifetime benefits from the personal pension plan was not a transfer of value. more>

Crown and Cushion Hotel – Tribunal allows tax deduction for motor racing sponsorship payments made to a family member

In *The Crown and Cushion Hotel (Chipping Norton) Ltd v HMRC* [2016] UKFTT 765 (TC), the First-tier Tribunal (FTT) allowed the appeal of the appellant company against HMRC's disallowance of expenditure it had incurred in sponsoring a racing driver who was the daughter of its sole director. The FTT concluded that the payments were made "wholly and exclusively" for the purposes of the company's trade as required by section 54, Corporation Tax Act 2009 (CTA). more>

News items

HMRC issues new Spotlight on planning intended to avoid new rules on disguised remuneration loan charges

HMRC has published a new Spotlight to deal with new, or proposed tax products, which are intended to circumvent the new rules on the taxation of loans under the disguised remuneration rules in Part 7A of the Income Tax (Earnings and Pensions) Act 2003. The new rules will apply in respect of certain loans which are outstanding on 6 April 2019.

The Spotlight sets out HMRC's view that such structures do not work and that the new rules will catch any such arrangements. HMRC also states that it will consider utilising the GAAR in such circumstances.

A copy of Spotlight 36 can be found here.

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The Government has published further draft legislation on proposed reforms to the taxation of non-domiciled individuals. The draft legislation (which includes explanatory notes) is expected to be included in the Finance Bill 2017.

A copy of the draft legislation can be found here.

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Report of the Public Accounts Committee on taxing high net worth individuals

The Public Accounts Committee has released a Report urging the Government to be tougher and clearer in its approach to taxing the wealthy including, in particular, those who participate in tax avoidance or tax evasion.

The Report provides details of various measures intended to assist HMRC in the collection of tax.

A copy of the Report can be found here.

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Case reports

Sandhu – Timing and detail critical in misfeasance claims against HMRC

In *Monmohan Sandhu v HMRC* [2017] EWHC 60 (QB), the claimant, who had been wrongly convicted of cheating the public revenue, had his claim of misfeasance in public office against HMRC struck out by the High Court because it was brought too late and he had failed adequately to plead his case.

Background

In 2003, Mr Sandhu (the claimant) was convicted of the offence of cheating the public revenue and sentenced to seven years imprisonment. HMRC had argued that his company had been a knowing participant in a "carousel fraud" involving the purchase of mobile phones in another member state of the EU. HMRC alleged that false invoices had been used in order to off-set fictional input tax which had never been due or payable.

The claimant appealed his conviction to the Court of Appeal in March 2006 on the basis that documents, which ought to have been disclosed by HMRC prior to the trial, had been improperly withheld. The Court of Appeal quashed the claimant's conviction and ordered a re trial.

The re-trial was to commence on 8 May 2007, however, before it took place, further undisclosed material came to light which ought to have been disclosed to the claimant before his trial. In the end, HMRC offered no evidence against the claimant and he was acquitted.

Some six years later, on 25 April 2013, the claimant issued proceedings alleging that unnamed HMRC officers had in the course of their employment maliciously abused their power in failing to disclose evidence during his criminal trial. The claimant alleged that the documents had been deliberately concealed in order to strengthen the case against him.

HMRC applied to the High Court to strike out the claim on the basis that it was out of time and inadequately pleaded.

The judgment

The claim was struck out.

In a claim for misfeasance in public office, it is necessary to identify the individual, or individuals, who it is alleged committed the relevant acts. This is necessary because, further to the case of *Three Rivers* [2003] 2 AC 1, a claimant has to establish that he has been the subject of "targeted malice" which must necessarily involve a subjective valuation of a particular officer/officers' conduct.

The Court was influenced by the fact that the claimant was unable to identify the officer against whom his allegations were made. A general complaint about poor treatment is insufficient.

The Court also found that the claimant's claim had been brought out of time. The actions which could be said to have given rise to the claim took place at, or before, the time of the criminal trial in 2003. The standard limitation period to commence proceedings is six years, although, in certain circumstances, the date from which this period is considered to run can be extended.

The claimant relied on section 32 Limitation Act 1980, which affords an extended limitation period:

"(1) … , where in the case of any action for which a period of limitation is prescribed by this Act, either –

…

(b) any fact relevant to the plaintiff's right of action has been deliberately concealed from him by the defendant; …

the period of limitation shall not begin to run until the plaintiff has discovered the fraud, concealment or mistake (as the case may be) or could with reasonable diligence have discovered it.

…"

HMRC accepted that the circumstances of the case were such that section 32(1)(b) applied, and that the date from which the limitation period commenced would be later than 2003. It also accepted that the concealment of undisclosed material must have meant that the claimant could not be said to have discovered the concealment until later than 2003, however, it disputed that the date would be as late as a date after April 2007 (it six years prior to the date of issue).

The claimant argued that it was not reasonable to expect him to commence his action until the outcome of the re-trial was known and it was from that date that the six year limitation period should run.

The Court rejected this argument. All of the material which demonstrated that documentation had been withheld by HMRC had been provided to the claimant before April 2007. The fact that HMRC entered no evidence during the re-trial was not a "fact relevant to the plaintiff's right of action"[1]. The relevant facts concerned the existence of the material itself and this was in the knowledge of the claimant well before April 2007. Accordingly, the Court concluded that the claim had been issued more than six years after that date of knowledge, for the purposes of section 32(1)(b) and was accordingly out of time.

Comment
Claims for misfeasance in public office necessarily involve establishing bad faith or dishonesty. The courts have been at pains to draw a clear line between acts which amount merely to negligence, which is insufficient to establish a claim for misfeasance, and those involving dishonest conduct on the part of a public official.

Where HMRC officers have deliberately and wrongfully withheld information which ought to have been disclosed during the course of a prosecution, the individuals concerned will understandably feel aggrieved. That sense of grievance will be all the more acute where the consequences lead, as they did in this case, to incarceration.

1. *AIC Limited v ITS Testing Services (UK) Limited (The Kriti Palm)* [2006] EWCA Civ 1601.

Although the law does provide redress to individuals in such circumstances, the claimant's claim failed because his pleadings were not sufficiently detailed or specific and the claim was commenced outside the relevant limitation period.

Anyone who believes they have been treated poorly by a state authority, to a degree which involves malice or dishonest conduct, should seek expert legal advice promptly from lawyers familiar with claims of this nature. Where the behaviour of a state authority is so bad that it amounts to malfeasance, claims must be carefully prepared and issued timeously.

A copy of the judgment can be found [here].

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Parry & Others – Upper Tribunal confirms that the transfer of a pension fund to a personal pension plan is not a transfer of value for IHT purposes

In *HMRC v Parry & Others* [2017] UKUT 4 (TCC), the Upper Tribunal (UT) held that a transfer of funds from a registered pension scheme to a personal pension plan made by the deceased shortly before her death was not a "transfer of value" for the purposes of section 3, Inheritance Tax Act 1984 (IHTA). Similarly, the deceased's omission to exercise her right to take lifetime benefits from the personal pension plan was not a transfer of value.

Background

As part of her divorce settlement, Mrs Staveley (the deceased) gave up her job in her former husband's company and received her share of the company pension fund. She was advised by an actuarial company that, in light of the law at the time, her best option was to transfer her fund into a buyout policy under section 32, Finance Act 1981 (the s.32 buyout policy). Although this would provide her with independence on a choice of investments, any surplus on the fund would be returned to the company on her death. Her pension fund was over-funded in respect of her level of salary and she was advised that she would have to wait 10 years before she could transfer the fund to a personal pension plan, the terms of which would enable the entire value of the fund to be paid to her estate or beneficiaries.

The deceased did not want her former husband to benefit from her pension fund upon her death and in July 2000, shortly after the conclusion of her divorce, she transferred her fund from the company occupational pension scheme into the s.32 buyout policy.

In 2004, she was advised that in light of legislative changes that were expected to come into effect in April 2006, she would be able to transfer her fund to a personal pension plan after six years, rather than 10 years. In 2005, she made a will which provided that her estate was to be divided equally between her two sons. In November 2006, she applied for her fund to be transferred to a personal pension plan. As part of that application she completed an expression of wishes by requesting that her death benefits be paid equally to her two sons.

The personal pension plan began on 9 November 2006. Whilst the policy allowed the deceased to have access to lifetime benefits, she died on 18 December 2006 without accessing any of the fund. Under the policy, the scheme administrator had discretion to pay death benefits to all or any of: (i) the persons nominated by the deceased (ie her two sons); (ii) her grandchildren; or, (iii) her personal representatives. In 2007, the scheme administrator exercised its discretion and paid the lump sum death benefit to the two sons in equal shares.

HMRC issued notices of determination to inheritance tax (IHT) to the deceased's personal representatives and her two sons (who were the beneficiaries of the death benefit paid out of the personal pension plan after her death), in respect of two alleged lifetime transfers of value by the deceased. The alleged transfers of value arose from the transfer by the deceased of funds from one registered pension scheme to another and from her omission to take any lifetime benefits from her personal pension plan.

The personal representatives and sons appealed the notices of determination.

The First-tier Tribunal (FTT) accepted that the transfer of the fund from the s.32 buyout policy to the personal pension plan was not a transfer of value and allowed the appeal on that issue but concluded that the deceased's decision not to take her pension benefits had preserved the value of her estate for her sons and found in favour of HMRC on that issue.

HMRC appealed in respect of the first issue and the personal representatives and the deceased's sons cross-appealed on the second issue.

The issues before the UT were whether (1) the transfer from the s.32 buyout policy to the personal pension plan was a "transfer of value" which attracted IHT; and (2) whether the deceased's omission to exercise the right to take lifetime benefits from her personal pension plan was a "transfer of value" which attracted IHT.

UT's decision
HMRC's appeal on the first issue was dismissed and the taxpayers' appeal on the second issue was allowed.

It was common ground that the transfer to the personal pension plan had reduced the value of the deceased's estate. This would constitute a transfer of value, subject to section 10, IHTA (dispositions not intended to confer gratuitous benefit). In order to rely upon section 10 a number of conditions have to be satisfied.

First, the taxpayer has to show that the disposition was not intended to confer a gratuitous benefit on any person.

Second, it has to be shown that the disposition was not made in a transaction (including a series of transactions or any associated operations) intended to confer such a benefit.

Third, it has to be shown either that the disposition was itself made in an arm's length transaction between unconnected persons or, if not, that it might be expected to be made in a transaction at arm's length between persons not connected with each other.

The UT concluded that all of these conditions were satisfied and that the FTT had been entitled to find that the disposition by the transfer of funds from the s.32 buyout policy to the personal pension plan was not intended to confer a gratuitous benefit on any person. The UT was also of the view that the deceased's sole motive had been to prevent any further pension funds from benefitting her former husband.

HMRC had argued that the transfer and the deceased's omission to take lifetime benefits from her pension as "associated operations". The UT rejected that submission and concluded that the transfer and the omission were unconnected and were not part of any scheme to confer a benefit on the deceased's sons. The transfer was an arm's length transaction between unconnected parties. In the view of the UT, the surrender and transfer themselves and the personal pension plan, were unexceptional, and the expression of wishes in the personal pension plan was a feature of an arm's length transfer into a pension of that nature. In the circumstances, the transfer was not a "transfer of value" for the purposes of section 3, IHTA.

The UT was of the view that the FTT had erred on the issue of causation. Section 3(3) provides that where the value of one person's estate is diminished and another's value increased due to the first party's omission to exercise a right (here, the deceased's omission to enjoy the lifetime benefits from her personal pension plan), that party will be considered to have made the disposition at the time when they could have exercised their right. The direct cause in the increase in the values of the two son's estates was due to the exercise of the discretion of the scheme administrator, rather than the deceased's omission to exercise her right to lifetime benefits. The UT therefore concluded that the conditions in section 3(3) were not satisfied and the omission could not be treated as a disposition or as a transfer of value.

Comment

This case illustrates the importance of thorough preparation when bringing an appeal before the FTT. The FTT found that the transfer by the deceased from the s.32 buyout policy to the personal pension plan was not intended "to confer a gratuitous benefit on anyone person", within the meaning of section 10, IHTA, and was not a transfer of value for the purposes of section 3, IHTA. Given such a finding, it was always going to be difficult for HMRC to persuade the UT to reach a contrary conclusion.

A copy of the decision can be found here.

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Crown and Cushion Hotel – Tribunal allows tax deduction for motor racing sponsorship payments made to a family member

In *The Crown and Cushion Hotel (Chipping Norton) Ltd v HMRC* [2016] UKFTT 765 (TC), the First-tier Tribunal (FTT) allowed the appeal of the appellant company against HMRC's disallowance of expenditure it had incurred in sponsoring a racing driver who was the daughter of its sole director. The FTT concluded that the payments were made "wholly and exclusively" for the purposes of the company's trade as required by section 54, Corporation Tax Act 2009 (CTA).

Background

The Crown and Cushion Hotel (Chipping Norton) Limited (the appellant) operates a family owned hotel business comprising of six hotels. Mr Fraser established the business in the 1980s and is the company secretary. Throughout the relevant period, Mr Fraser was the driving force behind the business and ran the business on a day-to-day basis, notwithstanding that the appellant is owned by his two daughters, one of whom, Mrs Powell, is also the sole director of the appellant.

In 2008, Mr Fraser put an agreement in place between the appellant and Miss Alice Powell, his granddaughter and the daughter of Mrs Powell, under which the appellant would sponsor Miss Powell, who was a young aspirational racing driver who had begun to attract substantial media attention, in return for Miss Powell undertaking various promotional and advertising activities in relation to the appellant's business.

HMRC conducted enquiries into the appellant's corporation tax returns for the accounting periods ended 31 March 2011 and 31 March 2012. In June 2014, HMRC issued closure notices in respect of its enquiries and amended the returns. HMRC claimed additional corporation tax for the above periods in the sum of £155,355.17, on the basis that the appellant was not entitled to a corporation tax deduction in computing the profits of its trade in relation to the motor racing sponsorship payments made to Miss Powell, as such expenditure had not been incurred "wholly and exclusively" for the purposes of its trade, as required by section 54, CTA. HMRC was of the view that the expenditure had a dual purpose of both advertising the hotel business and advancing Miss Powell's racing driving career.

The appellant appealed against the amendments.

FTT's decision

In allowing the appellant's appeal, the FTT confirmed that in deciding whether expenditure is incurred "wholly and exclusively" for the purposes of the taxpayer's trade it is necessary to ascertain the object of the taxpayer in incurring the expenditure, which is a question of fact. In making that factual assessment, the FTT has to observe a number of principles established by relevant case law and summarised by Millet LJ in *Vodafone Cellular v Shaw* [1997] STC 734 (at page 742) as follows:

- the words "for the purposes of the trade" mean "to serve the purposes of the trade". They do not mean "for the benefit of the taxpayer"
- to ascertain whether the payment was made for the purposes of the taxpayer's trade it was necessary for the FTT to discover the taxpayer's object in making the payment. Save in obvious cases, this involves an inquiry into the taxpayer's subjective intentions at the time of the payment
- the object of the taxpayer in making the payment must be distinguished from the effect of the payment. A payment may be made exclusively for the purposes of the trade even though it also secures a private benefit. This will be the case if the securing of the private benefit was not the object of the payment but merely a consequential and incidental effect of the payment
- although the taxpayer's subjective intentions are determinative, these are not limited to the conscious motives which were in his mind at the time of the payment. Some consequences are so inevitably and inextricably involved in the payment that unless merely incidental they must be taken to be a purpose for which the payment was made
- the question does not involve an inquiry of the taxpayer whether he consciously intended to obtain a trade or personal advantage by the payment. The primary inquiry is to ascertain what was the particular object of the taxpayer in making the payment in issue. Once that has been ascertained, its characterisation as a trade or private purpose is a matter for the FTT to determine.

HMRC argued that the payments made by the appellant to Miss Powell were not "wholly and exclusively" for the purposes of its trade. They were of a personal nature, arising out of natural love and affection for a close family member.

The FTT disagreed with HMRC and found in favour of the appellant. The FTT commented that Mr Fraser's sole object in the appellant making the payments to Miss Powell was to benefit the appellant by attracting customers to the hotels, which were situated near Silverstone race track. He was not motivated by a desire to further Miss Powell's racing career and any benefit to Miss Powell was merely an incidental effect of the sponsorship payments.

Comment

Whether an expense has been incurred "wholly and exclusively" for the purposes of the taxpayer's trade will of course depend on the individual facts of the case under consideration, but this decision demonstrates that it is possible for businesses to make sponsorship payments to family members and for such payments to be tax deductible provided that any benefit to the family member was an "incidental effect" of the sponsorship payment.

A copy of the decision can be found here.

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16982

Tower Bridge House
St Katharine's Way
London E1W 1AA
T +44 20 3060 6000

Temple Circus
Temple Way
Bristol BS1 6LW
T +44 20 3060 6000

11/F Three Exchange Square
8 Connaught Place
Central Hong Kong
T +852 2216 7000

12 Marina Boulevard
#38-04 Marina Bay Financial Centre Tower 3
Singapore 018982
T +65 6422 3000