Tax update

July 2018

In this month's update we report on new EU transparency rules for tax intermediaries; HMRC's revised Disguised Remuneration Settlement Terms; and the Law Society's Response to HMRC's consultation on Tax Avoidance involving profit fragmentation. We also comment on three recent decisions relating to discovery assessments; pensions; and capital allowance claims.

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EU transparency rules adopted for tax intermediaries

On 25 May 2018, the Economic and Financial Affairs Council formally adopted a Council Directive aimed at boosting transparency rules for tax planning intermediaries. more›

HMRC extends the deadline for taxpayers who participated in disguised remuneration arrangements to register an interest in settling their tax affairs

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Bayonet Ventures: Loan by pension scheme was not an unauthorised payment

In Bayonet Ventures LLP & Anor v HMRC [2018] UKFTT 262 (TC), the FTT, has held that a loan made to a limited liability partnership (LLP) by a pension scheme in which one of the partners of the LLP was a member, was not an unauthorised payment (section 164, Finance Act 2004) and should not be treated as a loan to the partner (section 863, Income Tax (Trading and Other Income) Act 2005 (ITTOIA)) as section 863 only applies if the LLP is carrying on a 'trade, profession or business with a view to profit', which it was not. **more›**

Dundas: out of time capital allowance claims become valid due to HMRC opening enquiries

In *Dundas Heritable Ltd v HMRC* [2018] UKFTT 0244 (TC), the FTT has held that a taxpayer was entitled to make, what would otherwise have been out of time capital allowance claims, as a result of HMRC opening enquiries. **more›**

About this update

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

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

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News items

EU transparency rules adopted for tax intermediaries

On 25 May 2018, the Economic and Financial Affairs Council formally adopted a Council Directive aimed at boosting transparency rules for tax planning intermediaries.

The Directive targets intermediaries such as tax advisors, accountants and lawyers, who design and promote tax planning schemes. It will require such intermediaries to report aggressive schemes.

Member states have until 31 December 2019 to transpose the provisions of the Directive into national laws and regulations. The new reporting requirements will apply from 1 July 2020. The information reported will be automatically exchanged through a centralised database and penalties will be imposed on intermediaries who do not comply with their reporting obligations.

A copy of the European Commission press release can be viewed here.

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HMRC extends the deadline for taxpayers who participated in disguised remuneration arrangements to register an interest in settling their tax affairs

On 1 June 2018, HMRC announced that it will continue to allow taxpayers who took part in disguised remuneration arrangements to register an interest in settling their tax affairs. The settlement opportunity was announced on 7 November 2017 and HMRC had set an original deadline of 31 May 2018 for taxpayers to register.

HMRC has now advised that the deadline is not absolute and that those wishing to register with HMRC should do so as soon as possible. HMRC has said that if the required information is provided after 30 September 2018, it may not be possible to reach a settlement before the loan charge arises on 5 April 2019.

A copy of the Guidance can be viewed here.

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Law Society publishes its response to HMRC's consultation on tax avoidance involving profit fragmentation

On 15 June 2018, the Law Society published its response to HMRC's consultation on tax avoidance involving profit fragmentation, which HMRC published on 10 April 2018.

HMRC's consultation proposes that additional anti-avoidance legislation be introduced in the 2018/19 Finance Bill to ensure that UK businesses cannot avoid UK tax by using arrangements that direct profits to a low or nil tax territory in circumstances where such profits arise out of a single activity.

In summary, the Law Society urges the government not to add to the already lengthy and complex tax legislation unless a clear need to do so has been established. In the view of the Law Society, the additional proposed anti-avoidance legislation is not needed.

A copy of the Law Society's response can be viewed here.

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Case reports

Anderson: Upper Tribunal considers knowledge test for the purpose of discovery assessments

In *Jerome Anderson v HMRC* [2018] UKUT 159 (TC), the Upper Tribunal (UT) has dismissed a football agent's appeal upholding the First-tier Tribunal's (FTT) decision to disallow relief for losses incurred in relation to a football academy run by the agent. The UT also agreed with the FTT that HMRC had issued a valid discovery assessment.

Background

Mr Jerome Anderson (the taxpayer), is a well-known football agent. In January 2009, he paid £2,943,000 to Bafana Soccer Developments Limited (Bafana), a soccer academy based in South Africa. Bafana had been set up to train and nurture young footballers and to promote their prospects in the lucrative European footballing leagues. In return for the finance he had provided, the taxpayer was able to choose three players from the academy, securing an interest for himself in any future transfer fees made by Bafana in relation to those players. Bafana went into Administration in 2011 and the taxpayer did not make any significant profits from Bafana.

The taxpayer's tax return for the 2008/09 tax year was filed with HMRC on 28 January 2010 and included a claim for £3,002,772 of losses in relation to Bafana. On 2 May 2012, HMRC issued a "discovery" assessment under section 29, Taxes Management Act 1970 (the discovery assessment), which disallowed all of the losses claimed. The taxpayer appealed to the FTT.

The appeal was unsuccessful. The FTT decided, first, that the discovery assessment had been validly made, and secondly that the taxpayer had not been entitled to the losses he had claimed, either under section 64, Income Tax Act 2007 (ITA) or section 72, ITA, as he was not carrying on a trade with a view to a profit.

The taxpayer appealed the FTT's decision to the UT.

UT decision

The appeal was dismissed.

In relation to the validity of the discovery assessment, the UT considered the test to be applied for the purposes of discovery. It was not in dispute between the parties that the concept of a "discovery" by an officer involves the application of both a subjective test, as to the officer's state of mind, and an objective test, as to whether that belief was reasonable.

The UT considered the test described by Patten LJ in *Sanderson v HMRC* [2016] EWCA Civ 19, and confirmed that the subjective test requires an officer to have more than a mere suspicion of insufficiency of tax, but he or she need not conclude that an insufficiency is more probable than not. The officer must believe that the information available "points in the direction" of there being an insufficiency. With regard to the objective test, the UT agreed with the UT in *HMRC v Charlton* [2012] UKUT 770 (TCC), and confirmed that the objective test requires the officer's belief to be reasonable, that is, a belief that a reasonable officer could form.

The FTT had considered whether the officer's belief was reasonable but had applied too strict an interpretation of the objective test. However, applying the UT's test to the facts of the present case, both the subjective and objective tests for a valid discovery were satisfied.

In relation to the second issue, the UT agreed with the FTT that the extent of the taxpayer's activities with Bafana did not constitute a trade. In the view of the UT, the taxpayer's activities were more akin to an investor, and, even if there was a trade, he had not been carrying on the trade on a commercial basis with a view to a profit.

Comment

The UT's formulation of the knowledge test for discovery assessments is helpful and provides useful clarification in this important area of the law.

The FTT asked itself whether the officer's belief that there had been an insufficiency of tax was a reasonable belief. It appears that the FTT applied a wholly objective test as to whether the officer's belief was reasonable. The UT considered that the correct test was whether the officer's belief was one "which a reasonable person could form on the information available to her".

The UT did not consider that the taxpayer provided sufficient evidence to demonstrate a commercial trade. As the burden is on the taxpayer, under section 74, ITA, to establish that the trade was carried on with a view to a profit, it is important that taxpayers provide sufficient evidence if they are to discharge this burden.

A copy of the decision can be viewed here.

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Bayonet Ventures: Loan by pension scheme was not an unauthorised payment

In Bayonet Ventures LLP & Anor v HMRC [2018] UKFTT 262 (TC), the FTT, has held that a loan made to a limited liability partnership (LLP) by a pension scheme in which one of the partners of the LLP was a member, was not an unauthorised payment (section 164, Finance Act 2004) and should not be treated as a loan to the partner (section 863, Income Tax (Trading and Other Income) Act 2005 (ITTOIA)) as section 863 only applies if the LLP is carrying on a 'trade, profession or business with a view to profit', which it was not.

Background

Up until 2012, Ronald Keith Howard (the second appellant) had operated as a sole trader. He set up Bayonet Ventures LLP (the first appellant) in around 2009 but did not transition his business into it immediately, and it was not until 2012 that the first appellant began to trade. In November 2009, the second appellant established the Bayonet Ventures Pension Scheme (BVPS). The first appellant was the principal employer and administrator, and the second appellant was a trustee and scheme member. In the same month, the scheme entered into a loan agreement with the first appellant, agreeing to lend it £66,000. The money was paid into the second appellant's bank account and the loan was not recorded in the first appellant's accounts for the relevant period.

BVPS filed its pension scheme tax return for the tax year ended 2009/10. HMRC opened an enquiry into the return and on 13 June 2013 wrote to the scheme administrator, the first appellant, claiming that BVPS had "made an unauthorised member payment of £66,000". The letter went on to assert that by reason of section 863, ITTOIA "the loan to the LLP is treated as a loan to the partners of the LLP. One of the partners of the LLP is also a member of the pension scheme". The letter went on to explain that HMRC considered the loan to be an "unauthorised member payment", within the meaning of section 164, Finance Act 2004.

The letter confirmed that HMRC had made an assessment in respect of a Scheme Sanction Charge at 40% of £66,000, being £26,400 and HMRC sent a Notice of Assessment to the second appellant.

On 17 June 2013, HMRC wrote to the second appellant asserting that BVPS had made a loan of £66,000 to the first appellant on 27 November 2009. It asserted that that loan must be treated as made to the individual members of the LLP and said that it was of the view that the loan was an "unauthorised member payment" because it fell outside of section 164, Finance Act 2004. Accordingly, the second appellant had to pay an unauthorised payment charge under section 208, Finance Act 2004, in the sum of £26,400 and an unauthorised payment surcharge under section 209, Finance Act 2004, at the rate of 15%, being £9,900. The letter enclosed an assessment dated, 17 June 2013, against the second appellant, in the total sum of £36,300 (5%).

The first appellant and second appellant appealed the assessments.

The appeals involved:

- an appeal by the second appellant against the assessment of £26,400 made against him on the basis that HMRC had deemed him to be the scheme administrator when, as a matter of fact, he was not
- an appeal by the first appellant against the scheme sanction charge, which was levied on the basis that there had been an unauthorised member payment, and
- an appeal by the first appellant against the surcharge on the allegedly unauthorised member payment.

FTT decision
The appeals were allowed.

With regard to the unauthorised payment charge in the sum of £26,400, the FTT concluded that the assessment had to be discharged. HMRC had no statutory power to appoint the second appellant as, or deem him to be, a scheme administrator and it could not point to any lawful basis on which it was entitled to do so.

In relation to the unauthorised member payment charge and surcharge, the FTT determined that pursuant to the loan agreement, the £66,000 had been loaned by the scheme to the first appellant. The first appellant was free to use the money as it pleased, and it was free to pay it to the second appellant, provided that such payment did not breach the terms of the loan agreement. Thus, the mere fact that the money passed from the scheme to the second appellant did not mean that the loan had been made to the second appellant.

The FTT said that the identity of the parties to a loan is a matter of law, albeit informed by the factual matrix. The issue was whether section 863(1), ITTOIA required HMRC to treat the loan as having been made to the second appellant. Under section 863(1), if an LLP carries on a trade, profession or business with a view to profit, its activities are to be treated for income tax purposes as being carried on "in partnership by its members", and not by the LLP as such.

In the instant case, the question was whether section 863(1) applied even though the first appellant had not begun trading until after the loan had been made. HMRC argued that it did, on the basis that an LLP was to be treated as carrying on a business with a view to profit from the moment it comes into existence, regardless of when it actually begins trading. The FTT rejected that argument. In doing so, the FTT commented that there was no basis for departing from the literal rule of statutory construction. In particular, there was "nothing whatsoever surprising in Parliament applying certain statutory rules, for income tax purposes, only if a limited liability partnership is in fact carrying on a trade". If that gave rise to some perceived gap in the legislation, it was to be filled by Parliament and not by the inventiveness of judges.

The first appellant had not been carrying on a trade, profession or business with a view to profit when the loan was made, and the mere fact of its having entered into a loan agreement and received a loan did not mean that it had. Furthermore, section 863(1) did not say that all the activities of an LLP were to be treated as being carried on by its members. It simply assimilated the position of partners in an LLP with that of partners in a non-LLP. In conclusion, there had been no unauthorised member payment. The assessments in respect of the unauthorised member payment and the surcharge therefore had to be discharged.

Comment

Although this case relates to a payment by a pension scheme, it could have wider ramifications in that it clarifies the meaning of the deeming provisions relating to LLPs and their members, in particular, the notion that the activities of an LLP are the activities of its members.

This decision is yet another example of HMRC unsuccessfully inviting the FTT to depart from a literal interpretation of the statutory provisions under consideration (see our recent blog on *Patel & Anor v HMRC* [2018] UKFTT 0185 (TC), which can be viewed here). When a literal interpretation is unhelpful and does not suit HMRC, it tends to argue for a purposive interpretation. This decision demonstrates that the FTT and courts will not always be amenable to such an approach.

A copy of the decision can be viewed here.

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Dundas: out of time capital allowance claims become valid due to HMRC opening enquiries

In *Dundas Heritable Ltd v HMRC* [2018] UKFTT 0244 (TC), the FTT has held that a taxpayer was entitled to make, what would otherwise have been out of time capital allowance claims, as a result of HMRC opening enquiries.

Background

Dundas Heritable Ltd (the taxpayer) operates various pubs and bars. It submitted its corporation tax returns for the periods ending 31 March 2012 (the 2012 return) and 31 March 2013 (the 2013 return). The 2012 return was received by HMRC in February 2015 and included a claim for capital allowances which should have been lodged by 31 March 2014. The 2013 return was received by HMRC in November 2015 and included a claim for capital allowances which should have been lodged by 31 March 2015. Both returns were submitted late (paragraph 82(1)(a), Schedule 18, Finance Act 1998).

HMRC opened enquiries into both returns, within the statutory time limits. HMRC accepted that the capital allowance claims, had they been lodged in time, would have been accepted, however, since the claims had been made out of time, HMRC disallowed them and issued closure notices. The taxpayer appealed.

FTT decision
The appeal was allowed.

In determining the appeal, the FTT was required to interpret paragraph 82, Schedule 18, Finance Act 1998, which provides:

"82.—

(1) A claim for capital allowances may be made, amended or withdrawn at any time up to whichever is the last of the following dates—

(a) the first anniversary of the filing date for the company tax return of the claimant company for the accounting period for which the claim is made;

(b) if notice of enquiry is given into that return, 30 days after the enquiry is completed;

(c) if after such an enquiry the Inland Revenue amend the return under paragraph 34(2), 30 days after notice of the amendment is issued;

(d) if an appeal is brought against such an amendment, 30 days after the date on which the appeal is finally determined.

(2) A claim for capital allowances may be made, amended or withdrawn at a later time if the Inland Revenue allow it.

(3) The time limits otherwise applicable to amendment of a company tax return do not apply to an amendment to the extent that it makes, amends or withdraws a claim for capital allowances within the time allowed by or under this paragraph.

(4) The references in sub-paragraph (1) to an enquiry into a company tax return do not include an enquiry restricted to a previous amendment making, amending or withdrawing a claim for capital allowances.

An enquiry is so restricted if—

(a) the scope of the enquiry is limited as mentioned in paragraph 25(2), and

(b) the amendment giving rise to the enquiry consisted of the making, amending or withdrawing of a claim for capital allowances."

The critical sub-paragraphs were 82(1)(a) and (b). It was accepted by the taxpayer that it had failed to make a claim in accordance with paragraph 82(1)(a), due to the late filing of its claims. However, the taxpayer argued that paragraph 82(1)(b) operated separately such that the opening of the enquiry by HMRC afforded the taxpayer an opportunity to make its claim timeously, under paragraph 82(1)(b).

HMRC argued that at the time the claim was made, some 10 months after the deadline provided for under paragraph 82(1)(a) had expired, there was no valid claim and the opening of an enquiry could not validate a claim which was invalid at the time it was made.

The taxpayer argued that the scope of paragraph 82(1) was permissive rather than restrictive. The use of the words “may” and “at any time” in the opening sentence indicated that a claim could be made before the last of the dates referred to in the paragraph.

The FTT observed that the purpose of HMRC opening an enquiry is so that it can fulfil its duty to collect the correct amount of tax. In such circumstances, a taxpayer is entitled to make any relevant claims that may then have been available to it. In the view of the FTT, this is a sensible approach as it ensures that a taxpayer is not ‘cornered’ by an assessment by being time barred from utilising a relief it may have otherwise used had it known of the assessed tax.

The FTT applied this approach in interpreting paragraph 82(1). With regard to paragraph 82(1)(b), the FTT considered that Parliament was attempting to ensure that a taxpayer had a similar opportunity to seek relief when it became subject to an enquiry. In the view of the FTT, nothing in the wording of paragraph 82(1) appeared to limit its scope only to claims which had been made in accordance with paragraph 82(1)(a). On the contrary, the paragraph clearly refers to four distinct situations in which a taxpayer may submit a claim for capital allowances.

The FTT considered that the claims would also be valid under subparagraphs (c), after the notice of amendment was issued and (d), following the release of the FTT’s decision.

Comment

Some commentators have remarked that this decision has produced an unexpected result, however, the wording of paragraph 82(1) is clear and the FTT’s reasoning is persuasive.

Interestingly, several of the reasons given in the original HMRC decision letter were abandoned by HMRC during the course of the hearing. In particular, there had been reference to the absence of a “reasonable excuse” on the part of the taxpayer for the late submission of the claims. HMRC accepted that the notion of an excuse was irrelevant for the purpose of construing the statutory provisions under consideration and acknowledged that some of the drafting in its letters had been “unfortunate”.

HMRC tends to adopt a restrictive approach when construing statutory provisions in circumstances where to do so will deprive the taxpayer of the benefit of the provisions under consideration. If in doubt, taxpayers and their advisers should return to the legislation itself and consider the words actually used by Parliament.

A copy of the decision can be viewed here.

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