# Tax update

June 2019

**In this month's update we report on (1) HMRC's guidance in relation to off-payroll working in the public sector and the intermediaries legislation (so-called IR35); (2) the extension of late payment and repayment interest to penalties levied under the DOTAS, promoters, and enablers of tax avoidance, regimes; and (3) HMRC's guidance on the economic interest requirement for shareholders who wish to claim entrepreneurs' relief. We also comment on three recent cases relating to (1) insurance premiums and earnings from employment; (2) an invalid discovery assessment due to 'staleness'; and (3) carelessness on the part of the taxpayer.**

## News items

### HMRC guidance in relation to off-payroll working in the public sector

On 16 April 2019, HMRC published updated guidance outlining changes to the way the intermediaries legislation (so-called IR35) is applied to off-payroll working in the public sector to clarify how the accounts of intermediary personal service companies should be prepared. more›

### Late payment and repayment interest extended to penalties levied under various anti-avoidance regimes

On 9 May 2019, the Treasury made two orders applying the provisions of sections 101 and 102, Finance Act 2009, on late payment and repayment interest, to penalties levied under various anti-avoidance regimes. more›

### HMRC guidance on new shareholding conditions in relation to entrepreneurs' relief

On 21 May 2019, HMRC published updated paragraphs CG64050 and CG64051 of its Capital Gains Manual, which provide guidance on the economic interest requirement, introduced by Finance Act 2019, for a shareholder who wishes to claim entrepreneurs' relief on a disposal of shares in a personal company on or after 29 October 2018. more›

## Case reports

### *Macleod* – insurance premiums paid were not earnings from taxpayer's employment

In *Macleod and Mitchell Contractors Limited and William Mitchell v HMRC*, the Upper Tribunal (UT) has held that insurance premiums paid by a company on policies taken out in the sole director's name were not earnings from his employment. more›

### Any comments or queries

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### About this update

Our 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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## *Hargreaves* – discovery assessment invalid due to "staleness"

In *Hargreaves v HMRC*, the FTT has found that HMRC's discovery of an underpayment of tax had become "stale" and accordingly the subsequent assessment issued under section 29, Taxes Management Act 1970, was invalid. All statutory references below are to this Act, unless stated otherwise. more>

## *Atherton* – discovery assessment not stale and taxpayer was careless

In *Richard Atherton v HMRC*, the UT has held that a discovery had not become stale by the time an assessment was issued under section 20, Taxes Management Act 1970 and that the taxpayer had been careless in making an inadequate "white space" disclosure in his self-assessment return. more>

Back to contents>

# News items

## HMRC guidance in relation to off-payroll working in the public sector

On 16 April 2019, HMRC published updated guidance outlining changes to the way the intermediaries legislation (so-called IR35) is applied to off-payroll working in the public sector to clarify how the accounts of intermediary personal service companies should be prepared.

A copy of the guidance can be viewed here.

Back to contents>

## Late payment and repayment interest extended to penalties levied under various anti-avoidance regimes

On 9 May 2019, the Treasury made two orders applying the provisions of sections 101 and 102, Finance Act 2009, on late payment and repayment interest, to penalties levied under various anti-avoidance regimes.

**The Finance Act 2009, Sections 101 and 102 (Disclosure of Tax Avoidance Schemes: Penalties) (Appointed Day and Consequential Provisions) Order 2019 (SI 2019/918)**
Appoints 1 June 2019, as the day on which the interest regime comes into force for amounts payable to, or payable by, HMRC, in relation to penalties in connection with the disclosure of tax avoidance schemes (DOTAS) regime, and the national insurance contributions disclosure regime.

**The Finance Act 2009, Sections 101 and 102 (Avoidance: Penalties) (Appointed Day) Order 2019 (SI 2019/921)**
Appoints 1 June 2019, as the day on which the interest regime comes into force in relation to penalties in connection with the VAT and indirect taxes disclosure regime, the promoters of tax avoidance regime, and the enablers of defeated avoidance schemes regime.

For DOTAS penalties, these provisions will replace the interest regime in section 103A, Taxes Management Act 1970.

A copy of the orders can be viewed here and here.

Back to contents>

## HMRC guidance on new shareholding conditions in relation to entrepreneurs' relief

On 21 May 2019, HMRC published updated paragraphs CG64050 and CG64051 of its Capital Gains Manual, which provide guidance on the economic interest requirement, introduced by Finance Act 2019, for a shareholder who wishes to claim entrepreneurs' relief on a disposal of shares in a personal company on or after 29 October 2018. Section 39 of and Schedule 16, Finance Act 2019, amended section 169S(3) to impose the following two additional conditions, at least one of which must be satisfied:

**Condition 1**
The shareholding would entitle the individual to at least 5% of the profits available for distribution and at least 5% of the profits available on a winding up.

**Condition 2**
The individual would be entitled to at least 5% of the proceeds of a disposal of the whole of the ordinary share capital of the company.

The second condition was introduced to assist shareholders in companies with complex share capital structures but is subject to anti-avoidance provisions.

HMRC's guidance and examples in paragraph CG64051 clarify how, and at what date, the valuation of the company and the individual's entitlement to notional proceeds are determined. For the purposes of condition 1, the entitlement to profits and assets is calculated largely in accordance with Chapter 6, Part 5, Corporation Tax Act 2010. For condition 2, the company is valued at the date on which the individual's actual disposal occurs, but without a discount for a minority holding, and the amount apportioned to the individual is then used to measure whether the criteria have been met throughout the relevant period.

A copy of the updated paragraphs can be viewed here and here.

Back to contents>

# Case reports

## *Macleod* – insurance premiums paid not earnings from taxpayer's employment

In *Macleod and Mitchell Contractors Limited and William Mitchell v HMRC*[1], the Upper Tribunal (UT) has held that insurance premiums paid by a company on policies taken out in the sole director's name were not earnings from his employment.

### Background

Mr Mitchell was the sole director and shareholder of Macleod and Mitchell Contractors Ltd (MMCL). Several insurance policies were taken out and the premiums paid by MMCL.

In each case, Mr Mitchell was the insured but MMCL and Mr Mitchell had understood that the policyholder in each case was MMCL. In 2013, it was discovered that the policies ought to have been in the name of, or for the benefit of, MMCL.

Following this discovery, Mr Mitchell assigned the policies to MMCL in 2014. None of the policies had paid out benefits prior to the assignment.

HMRC assessed Mr Mitchell to income tax and national insurance contributions in respect of the premiums paid by MMCL up to the date of the assignment. MMCL was assessed to pay primary and secondary class 1 national insurance contributions in respect of the payments.

The assessments were appealed to the First-tier Tribunal (FTT).

### FTT decision

The appeals were dismissed.

The FTT held that the premium payments were subject to income tax and national insurance contributions as they constituted earnings from Mr Mitchell's employment.

In the view of the FTT, the tax treatment must follow the transactions that actually took place, regardless of the parties' intentions. It rejected the proposition that the policies were held on constructive trust for MMCL. The payments of the premiums had relieved Mr Mitchell of pecuniary liabilities to the insurance company and therefore the payments were earnings from his employment (section 62, Income Tax (Earnings and Pensions) Act 2003).

Mr Mitchell and MMCL appealed to the UT.

### UT decision

The appeals were allowed.

The central issue for the UT to determine was whether the premium payments conferred a profit or benefit on Mr Mitchell and whether such a benefit derived from Mr Mitchell's employment.

In the view of the UT, the premium payments made were not earnings from Mr Mitchell's office or employment. The payments were not intended to be a reward, return or remuneration for his services. They were intended to provide the benefit of insurance cover to MMCL and that is why the premiums were paid. The UT said at [22]:

1. [2019] UKUT 0046 (TCC).

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"In our opinion the premium payments here were very clearly not earnings from Mr Mitchell's office or employment. On the contrary, echoing the language of Lord Diplock [in *Tyrer v Smart* [1979] STC 34], they "were bestowed upon him for some other reason". They were not intended to be a reward, return or remuneration for his services. They were intended to benefit MMCL, not him. They were made on the erroneous understanding that MMCL was the policyholder and that it would be the beneficiary of any policy proceeds."

The UT stated that Mr Mitchell owed a fiduciary duty to MMCL as a director not to make a personal profit and to avoid any possible conflict between his interests and those of the company. Mr Mitchell did not enjoy any personal benefit from being the policy holder and had an obligation to assign the policies on demand, which he did once the error was discovered.

MMCL had no right to recover the premiums from Mr Mitchell as he was only the policyholder due to MMCL's mistake and the premiums could only be recovered if MMCL accepted that Mr Mitchell was the rightful owner of the policies, which it did not. As such, MMCL was not relieving Mr Mitchell of any pecuniary liability and payment of the premiums was not a reward, return or remuneration for his services. The same analysis applied to national insurance contributions under section 3, Social Security Contributions and Benefits Act 1992.

**Comment**

The FTT erred in law by failing to focus correctly on the critical question of whether there was any benefit to Mr Mitchell from the payment of the premiums and, if so, whether this arose "from" his employment.

The FTT also treated the company's intention when granting a benefit to an employee as irrelevant, when in fact the purpose of an employer in granting a benefit to an employee is a crucial factor when determining whether the benefit is to be regarded as a reward, or return, for the employee's services.

A copy of the decision can be viewed here.

Back to contents›

## *Hargreaves* – discovery assessment invalid due to "staleness"

This report is based on an article first published in Tax Journal on 24 April. A copy of that article can be viewed here.

In *Hargreaves v HMRC*[2], the FTT has found that HMRC's discovery of an underpayment of tax had become "stale" and accordingly the subsequent assessment issued under section 29, Taxes Management Act 1970, was invalid. All statutory references below are to this Act, unless stated otherwise.

**Background**

Once HMRC has discovered a loss of tax to the Crown it must act within a reasonable amount of time if it wishes to issue an assessment under section 29.

2. [2019] UKFTT 0244 (TC).

In *Hargreaves*, the taxpayer filed his tax returns on the basis that he had ceased to be UK tax resident on 11 March 2000, two months before disposing of shares worth £231m. On 16 January 2004, following a newspaper article published in March 2003 (which alleged that the taxpayer spent three days each week in the UK), HMRC opened an enquiry into his 2001/02 return. HMRC was out of time to open an enquiry into the return for the prior year in which the share disposal occurred, and on 9 January 2007 issued a discovery assessment, pursuant to section 29, for £84m in respect of the gain on the share disposal. The taxpayer appealed the assessment on the basis that it had become stale.

**FTT decision**

The appeal was allowed.

The FTT rejected HMRC's argument that it only made its discovery of the taxpayer's continuing UK tax residence in January 2006, following receipt of a report from the taxpayer's advisers addressing issues raised by HMRC. This was because the officer's evidence was that he had not changed his initial view of November 2004 on the taxpayer's residence status, notwithstanding the information subsequently received. The delay in question ie between March 2003 and January 2006, was considered by the FTT to be sufficient to render the discovery stale and the assessment was therefore invalid.

**Comment**

HMRC has relied on its discovery assessment powers a great deal in recent years and has stretched the concept of "discovery" to an ever expanding variety of circumstances. Clearly concerned by recent cases, such as *Beagles v HMRC*[3], in which it has been held that HMRC's discovery was stale and the potential check on its powers, HMRC has been resolute that the concept of "staleness" cannot be discerned from legislation or case law and does not exist.

The Court of Appeal is due to hear the appeal in *Beagles* later this year. If the Court of Appeal rejects HMRC's position and confirms that discovery assessments can be invalid due to staleness, it is to be hoped that it will provide guidance on when and how a "discovery" is likely to become stale as the time periods considered by the tax tribunals to date have varied considerably.

A copy of the decision can be viewed here.

Back to contents>

## *Atherton* – discovery assessment not stale and taxpayer was careless

In *Richard Atherton v HMRC*[4] the UT has held that a discovery had not become stale by the time an assessment was issued under section 20, Taxes Management Act 1970, and that the taxpayer had been careless in making an inadequate "white space" disclosure in his self-assessment return.

**Background**

Mr Atherton (the taxpayer) was a partner in a hedge fund. He engaged a firm of accountants, Fitzgerald and Law (F&L), to complete his tax returns. In 2008, F&L introduced the taxpayer to NT Advisers (NTA), who provided tax avoidance arrangements.

NTA recommended to the taxpayer a tax avoidance arrangement known as "Romangate", as a way to shelter his 2007/08 partnership income by creating an employment loss.

3. [2018] UKUT 380 (TCC).
4. [2019] UKUT 0041 (TCC).

The taxpayer implemented Romangate in 2009. Following advice from F&L, he claimed the Romangate loss in his 2007/08 tax return, reducing the tax he would otherwise have to pay from £2m to nil. The taxpayer used box 3 on the additional information pages of his tax return to make a standalone claim for loss relief and box 20 on the partnership pages to try to "force" the year 2 loss into the computation of year 1 liability.

Later in 2009, HMRC opened an enquiry into the loss relief claim under Schedule 1A, TMA . In December 2013, NTA wrote to HMRC and accepted that due to retrospective legislative changes, Romangate  was ineffective.

Following the Supreme Court's decision in *Cotter v HMRC*[5], HMRC concluded that its enquiry into the taxpayer's loss relief claim was invalid but was of the view that it had made a discovery, for the purposes of section 29, Taxes Management Act 1970, on realising that the Supreme Court's confirmation in *Cotter* that a claim could be "forced" into a tax return for an earlier tax year meant that HMRC should have treated the taxpayer as having made a claim in his return (rather than a standalone claim) and therefore the assessment had become insufficient. HMRC therefore issued an assessment in 2014, under section 29, Taxes Management Act 1970.

The taxpayer appealed the assessment.

**FTT decision**

The appeal was dismissed.

The two issues before the FTT were (1) whether there had been a valid discovery by HMRC and if there had been, was the discovery stale; and (2) whether the insufficiency in the taxpayer's 2007/08 return was brought about by his carelessness.

*1. The discovery issue*

The effect of the Supreme Court's decision in *Cotter* was that HMRC had been wrong to open the 2009 enquiry on the basis that the loss relief claim was a standalone claim. HMRC should have opened the 2009 enquiry under section 9A, Taxes Management Act 1970, as the claim was made 'in' the taxpayer's return and was not a standalone claim. The discovery issue turned on whether HMRC's realisation of the effect of *Cotter*, which was released when HMRC was out of time to open an enquiry under section 9A, was a discovery for the purposes of section 29.

The FTT concluded that HMRC had made a valid discovery in 2014, when it realised the effect of the Supreme Court's decision in *Cotter* and this discovery was not stale.

*2. The carelessness issue*

The FTT also concluded that the taxpayer was careless in making an inadequate white space disclosure. He was careless to use box 20 on the partnership pages of the return to try and "force" the year 2 loss into the computation for the year 1 liability, without providing any further explanation.

The taxpayer appealed.

5. [2013] UKSC 69.

**UT decision**

The appeal was dismissed.

In reaching its decision, the UT considered the same two substantial issues as the FTT.

*1. The discovery issue*

When HMRC opened its enquiry in 2009, it made a discovery of insufficiency of tax, for the purposes of section 29. The UT agreed with the FTT that HMRC made a new discovery in 2014, when it had appreciated the effect of the Supreme Court's decision in *Cotter*. In the view of the UT, the 2009 discovery was too long prior to 2014, as the concept of staleness meant that a valid discovery assessment had to be issued by HMRC without undue delay following the making of the discovery. However, although both discoveries related to the Romangate loss, they were separate discoveries as there was nothing to prevent HMRC from making successive different discoveries in relation to the same tax liability. Accordingly, the discovery assessment was valid.

*2. The carelessness issue*

The UT also agreed with the FTT that the taxpayer had been careless in making an inadequate white space disclosure. However, in relation to causation, it considered the FTT had failed to ask the right question. Section 118(5), Taxes Management Act 1970, to which the FTT had not referred, provides that a situation is brought about carelessly if a person fails to take reasonable care to avoid brining it about. The insufficiency of tax in the taxpayer's return was caused by "forcing" the loss into the return but this could have been avoided by the taxpayer making a standalone claim. The taxpayer was therefore careless.

**Comment**

The UT's conclusion that HMRC had made a discovery, for the purposes of section 29, on realising the effect of the Supreme Court's decision in *Cotter*, is not surprising as the courts have confirmed that for a discovery to be made all that is required is a new conclusion, there does not need to be any new facts and it is sufficient for HMRC to simply change its mind (*Cenlon Finance Co Ltd v Ellwood*[6] and *HMRC v Charlton Corfield & Corfield*[7]). Given that the discovery assessment was issued shortly after HMRC's realisation of the effect of the Supreme Court's decision in *Cotter*, it was not stale.

With regard to the issue of carelessness, although the UT concluded that the taxpayer had been careless in "forcing" his claim into his return, it did not consider that "forcing" a claim into a return would be careless in all circumstances, for example, where a taxpayer acted reasonably in taking advice from a professional adviser he would not be careless.

A copy of the decision can be viewed here.

**Back to contents>**

6. [1962] AC 782.
7. [2012] UKUT 770 (TCC).

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