UHY Hacker Young
Chartered Accountants

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Tax Update

Our summary of the latest tax issues

Unwary trustees may be caught out by tax changes in the Finance Act 2014

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The problem with most legislation is that the devil is in the detail. This was certainly the case with the Finance Act 2014 which brought about a number of changes that will affect Inheritance Tax (IHT). If you are a trustee you need to be especially careful to ensure that you do not increase your tax liabilities unnecessarily – particularly as it is possible to do so as a result of cautious treatment of trust income.

Income in a trust fund can be either distributed to the beneficiaries or added to trust capital. However, if nothing is done, by default it is retained as trust income. It is this income that may be caught by the changes.

To explain further, those trusts (except certain exempted trusts) containing 'relevant property' pay IHT on transfers out of the trust and on the trust's ten year anniversaries. 'Relevant property' includes assets such as property, land, shares and money. Following the changes, any retained income that has been held in the trust for more than five years is now also treated as relevant property.

The question is how the five year rule applies. In the first instance, if a specific part of income has been distributed this is clearly removed from the calculation. In all other cases HMRC assume that income is distributed on a 'first in, first out' basis. Therefore, when a ten year anniversary arises, trustees need to deduct income that has arisen in the past five years. Any remaining balance is included as relevant property.

The changes take effect on ten year anniversary charges arising on or after 6 April 2014. This means that as a trustee you should be taking action now to calculate how much retained income sits in the trust and consider your options if this now falls within the scope of these changes.

If you are a trustee of a trust subject to ten year anniversary IHT charges, you should speak to your usual UHY adviser well in advance of the anniversary date.

Andrew Hulse, partner, Sheffield

Can HMRC discover you?

Recently, a case was heard to determine whether the taxpayer could successfully challenge the validity of discovery assessments raised by HMRC relating to benefit in kind (BIK). If HMRC finds out that your tax return is wrong, they can make an assessment to collect the extra corporation tax your company should have paid. This is known as a discovery assessment.

Via his company, the taxpayer in question ran and lived above a restaurant business. The company also entered into consecutive leases for motor cars which the owner used over several years. The cars were not shown in the company balance sheet and the cost of the leases was charged to his current account on a monthly basis. Neither the cars nor the accommodation had been reported as BIK when HMRC conducted a compliance visit.

Some might think that, as the taxpayer was paying for the leases, there was no resulting BIK, however, the problem arose due to the informal nature of the arrangements. Had the reason for the company entering into the leases been properly documented no benefit need have arisen but, in its absence, the Tribunal held that the company made the cars available to him. Others might then think that the taxpayer had paid for the cars and, therefore, the measure of the benefit should be reduced accordingly. Again, strict rules apply and unless the payment is specifically made for the private use of the vehicle no deduction can be made. However, he was fortunate in that the Tribunal accepted his fuel arrangements, otherwise a further significant benefit could have arisen.

He was also fortunate in relation to his personal accommodation above the business, where it was held that no benefit arose as the accommodation was provided for the better performance of his duties.

Overall, the Tribunal found that the taxpayer had taken a legitimate position on professional advice when he completed his returns and so had not been careless. Accordingly, the time limit for making discovery assessments where there is no careless behaviour is four years. Nevertheless, even though he had ended up paying for the cars he remained taxable for their provision for the 'in-time' years. As is often the case, taking shortcuts cost him dearly, even though most of the assessments were cancelled for being out of time.

If you are concerned about your own assessments, or would like to know more about BIK, please contact your usual UHY adviser.

Roy Maugham, partner, London

Car dealer closed down

A recent tax case held that, despite having set up another car dealership, the owner was entitled to entrepreneurs' relief thereby enjoying a 10% rate for Capital Gains Tax (CGT) on the disposal of his old premises.

Previously, the dealer had run a 'performance car' sole trader business from a site strategically placed on a main road with appropriate signage and a forecourt to attract passing customers. Following repeated problems with vandalism he decided to close the site down and sold the remaining stock through auctions and newspaper adverts. He subsequently sold the premises and claimed entrepreneurs' relief against the gain. In the meantime, he had started to sell four wheel drive and other family cars via the internet, whilst storing the vehicles on land adjacent to his home.

HMRC argued that, as a sole trader, he had continued to deal in motor cars and accordingly there had been no cessation and hence no disposal of the relevant business to enable entrepreneurs' relief to apply.

Whilst many would form the same view, fortunately for him the Tribunal recognised the distinctions between the two operations as described above and awarded him the relief. Just like the proverbial second hand car, all is not necessarily what it seems to be at first sight.

Nevertheless, as well as the CGT implications, there were no doubt consequential income tax consequences for the individual concerned. His old business profits would have been revised from the continuation basis to those earned up to the date of cessation and taking into account overlap relief, whilst his new business will have started under the commencement rules. Depending upon his choice of accounting dates for each business both circumstances may have afforded further tax savings.

If you are in a similar situation to the above case study, or indeed have any questions about your position, please contact your usual UHY adviser.

Roy Maugham, partner, London

Decisions, decisions…

HMRC have been keeping busy over the summer; they have enjoyed some 'successes' in the tax courts, Accelerated Payment Notices (APNs) have been introduced, and changes have been made to existing settlement opportunities, which seem to suggest that HMRC are keen for taxpayers to disclose and regularise their historic tax issues sooner rather than later.

Accelerated Payment Notices

The Finance Act 2014 introduced legislation which affects taxpayers who have used certain arrangements that have been disclosed under the Disclosure of Tax Avoidance Scheme (DOTAS) rules or which fall under the General Anti-Abuse Rule (GAAR). This legislation requires taxpayers using avoidance schemes to pay the disputed tax upfront through the use of APNs where there is an open enquiry or appeal.

The disputed tax relates to the 'tax advantage' that the use of the tax avoidance scheme tried to achieve.

The first APNs have now been issued with more to follow. If you receive an APN, payment of this disputed tax will be due within 90 days and penalties will be applied to late payment.

It may be possible to dispute an APN but such challenges will require professional advice.

Further, if funds to pay the disputed tax upfront are limited, time-to-pay arrangements with HMRC could be negotiated to avoid incurring any potential late payment penalties or even bankruptcy.

If you believe you are in this position please contact your usual UHY adviser or a member of our tax investigations team.

Opportunities for early settlement

HMRC have begun to distribute letters encouraging taxpayers involved in non-DOTAS registered tax avoidance schemes to contact them for discussions regarding the resolution of the outstanding issues, rather than continue with litigation. These letters indicate that there is a limited window of opportunity to register an interest in exploring settlement with HMRC. Such an approach may also be followed swiftly by an APN, to further encourage discussion.

It may, therefore, be advisable to consider whether an early settlement is beneficial for you, however, it is important to have a clear understanding of your position given the complexity of the tax and legal issues involved in such schemes before entering into discussions with HMRC. Settlement does, however, mean that if the planning is eventually found to be legally sound you will have lost the benefit of such an outcome.

There is also a risk that, despite reaching a settlement which addresses the historic tax position, there may be future tax exposures which remain unaddressed due to appeals not yet heard in the courts.

Employee Benefit Trust settlement opportunity to close

The Employee Benefit Trust (EBT) settlement opportunity, which began in April 2011, is due to close in March 2015. Taxpayers wishing to settle will need to notify HMRC of their intention by 31 March 2015 and have paid all amounts due by 31 July 2015. HMRC have indicated that they are directing resource into litigating those who do not settle under this opportunity.

Taxpayer wins Rangers case

Despite what has been said above, the Upper Tribunal (HMRC v Murray Group, FTC/15/2013) confirmed the First-tier Tribunal's finding and found in favour of the taxpayer that the payments made to staff (mainly footballers) were genuine loans.

To summarise the case, MGM (a company of the Murray Group) had set up an employee remuneration trust, which had in turn set up sub-trusts for employees. The sub-trusts were financed by loans of the company to the head trust. The loans had not been repaid. The question was whether there had been a payment of earnings by MGM to the employees. The conclusion was that the payments made to the employees were loans, not earnings, and could not be displaced.

It, therefore, is important to note that, although an element of the arrangements were identified in the Rangers case as 'tax avoidance', the courts were unable to ignore the fact that genuine loans had been made and subsequently found in favour of the taxpayer.

HMRC have very publicly stated that tax avoidance schemes do not work and this is being proven in the courts. Although HMRC have had many successes in the tax tribunals this case does show that the courts are willing to recognise certain types of tax planning even if they are part of a 'scheme'.

If you would like to understand more about this and how these changes could potentially affect you, please contact your usual UHY adviser or a member of our tax investigations team.

Heather Williams, senior manager, London

Our VAT round-up

In this issue of Tax Update, we are providing a summary of some of the recent VAT issues, a number of which could have significant implications for you and your business.

Holding companies

HMRC have been investigating holding companies lately, as well as UK companies that trade entirely overseas. The focus is to challenge the companies' entitlement to be registered for VAT in the UK and their reclaims of input VAT. A common theme has been the presence (or not) of service agreements and proper invoicing to support the services being provided. Without proper implementation, HMRC have an open door to challenge the VAT position and attention to detail is essential to support the business activities in question.

Golf clubs

The saga continues. Following the win in the Bridport case, many golf clubs expected their claims against HMRC for VAT wrongly accounted for on non-member fees to be refunded to them. Alas not. In a fit of pique, HMRC are invoking the defence of unjust enrichment and denying a refund to clubs where they cannot repay the VAT to the non-members who were wrongly charged VAT in the past. This is clearly impossible for many clubs and HMRC expect to issue further guidance shortly. We understand, however, that further appeals are being lodged against this approach by HMRC, so it is likely to be some time yet before the matter is finally resolved.

Tri-partite agreements and input tax recovery

HMRC have recently won the Airtours case where the company sought to reclaim input tax on advisers' fees for due diligence work. The company had sought bank financing and the Court ruled that, despite the tri-partite agreement, the services were provided to the bank and the company could not reclaim the VAT. We recommend that any such tri-partite arrangements are looked at carefully and agreements drafted to meet VAT requirements to ensure that the VAT can be reclaimed.

Property surrenders

Following the Robinson Family case, HMRC have now amended their policy on surrenders of property interests. The details are complex but, in brief, where leasehold interests are surrendered to the landlord together with any sub-tenancies, the surrender could now qualify as a transfer of a going concern with VAT benefits for both parties. As always, the facts will be vital but we will be pleased to advise you if you feel you are in this position.

VAT groups

The long-awaited Skandia decision has been released by the European Court, to much consternation. The implications for multi-national companies with overseas branches in VAT groups could be significant and are likely to impose VAT costs within the one company where there were no such costs before. With the added complication that some EU countries recognise VAT groups and some do not, any clients who may be affected should seek advice on their cross-border VAT position to determine the potential implications.

Partial exemption

Lastly, a quick note to flag that HMRC are looking at partially exempt businesses more closely and routinely challenging their input tax reclaims. Many long-established principles for partial exemption methods are being cast aside in the relentless pursuit of revenue and we would advise businesses to review their partial exemption position before HMRC do. It goes without saying that it is better to defend on solid ground than fight a rear guard action on the retreat.

If you would like to discuss your VAT situation in relation to any of the issues above, or indeed have any other VAT issues you would like to discuss further, please contact your usual UHY adviser.

Simon Newark, partner, London

Ongoing tax planning and the Autumn Statement

The Finance Act 2014 runs to a mere 646 pages and is the second longest to be published despite the ongoing efforts of the Office of Tax Simplification. In addition to the subjects covered within this Tax Update, several major changes have been introduced for partners (especially LLP members); Annual Investment Allowances, Business Premises Renovation Allowance, Remittance Basis, Car Benefits, Social Investment Tax relief, etc.. Below we highlight some of the key changes to be aware of.

Members of LLP's now face the risk of being treated as employees for income tax and NIC purposes without the associated employment rights. Many do not appreciate how narrow the definition of how their profit share or involvement with the LLP is measured in order to remain self-employed. Unless your profit share is mainly measured by reference to the firm-wide profits we suggest you discuss your position with your usual UHY adviser. In addition, the profits shared by non-individual members of partnerships may well end up being assessed to income tax on the associated individual. Again, you need to consider these risks carefully.

It has been announced (subject to legislation) that the period for the temporary increase in relief for capital expenditure will be extended to 31 December 2015. We strongly recommend you consider making use of the exceptionally high level of relief (£500k per annum) on plant and machinery, before the limit returns to £25k per annum.

Changes have been made as to what qualifies for Business Premises Renovation Allowance, but the period for balancing adjustments has been reduced from seven to five years.

Dual contracts of employment for non-UK domiciled workers have come under attack for the artificial separation of duties between the UK and overseas. If the applicable overseas tax rate is less than 65% of the UK rate, the income may nevertheless be taxed in the UK.

Whilst announcing new higher rates for the car BIK in 2015/16 and 2016/17 generally, the previous uplift (3%) for diesel engine cars has been abolished and the zero or low emission cars now face increasing rates.

Income tax relief of 30% is now available for social investments into qualifying community interest companies, societies or charities, provided the shares or qualifying debt are held for at least three years.

The Autumn Statement will be presented by the Chancellor on 3 December 2014. Follow us on Twitter for live commentary on the announcements after which we will prepare a more detailed summary of the announcements and their impact, and would be happy to talk these through in relation to your own individual circumstances. If you would like to know more about the opportunities which may be available to you, please contact your usual UHY adviser.

Roy Maugham, partner, London

"Unless your profit share is mainly measured by reference to the firm-wide profits we suggest you discuss your position with your usual UHY adviser."

Stop Press!

We recently became aware of a scam that was circulating some time ago but appears to have re-surfaced. An apparent German publishing company is seeking annual payments for publishing companies' VAT registration numbers in a compulsory European database. There is no such obligation and you can ignore the demand. If you receive one of these letters please forward it to us or send it to your local Trading Standards office who we understand have received these before.

Pension planning

The 2014 Budget proposed new flexible draw-down rules for pension schemes from 6 April 2015.

Instead of consulting before introducing the legislation, the Taxation of Pensions Bill has now been published, subject to consultation. So whilst many of the proposals allowing the fund to be withdrawn rather than being paid into an annuity may remain, much of the detail could change.

If you would like to know more about the flexible draw-down rules or indeed have any questions about your pension scheme in general, please contact your usual UHY adviser.

Roy Maugham, partner, London

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