Offence	Penalty[1][2]		
	70%	35%	20%
	105%	52.5%	30%
	140%	70%	40%
	100%	50%	30%
	150%	75%	45%
	200%	100%	60%
For failures before 1 April 2010 (TMA 1970, s. 7; Tax Reporter: 181-525)	Tax geared up to 100% of the tax, subject to mitigation		
Failure to keep and retain tax records (TMA 1970, s. 12B; Tax Reporter: 181-900)	Up to £3,000 per year of assessment		
False statements to reduce interim payments (TMA 1970, s. 59A[5]; Tax Reporter: 182-725)	Up to the difference between the amount correctly due and the amount paid		
Failure to comply with an information notice (FA 2008, Sch. 36, para. 39 and 40; Tax Reporter: 186-550ff.)			
• standard amount	£300		
• continued failure	daily penalty of £60		
Tax-related penalty where significant tax is at risk (FA 2008, Sch. 36, para. 50)	tax geared amount decided by Upper Tribunal		
Inaccurate information/documents in complying with an information notice (FA 2008, Sch. 36) Inaccuracy careless or deliberate	Up to £3,000 for each inaccuracy		
Errors in returns			
Errors in returns for periods starting 1 April 2008 where return is filed on or after 1 April 2009 (FA 2007, Sch. 24; Tax Reporter: 184-850)[6]	Percentage of potential lost revenue		
	Category 1[7]	Category 2	Category 3
• careless action	30%	45%	60%
• deliberate but not concealed action	70%	105%	140%
• deliberate and concealed action	100%	150%	200%
Reductions for disclosure (maximum reduction weighted according to quality of disclosure determined as:	Standard penalty	Prompted disclosure Minimum	Unprompted disclosure Minimum
• 30% for telling,	30%	15%	0%
• 40% for helping and	45%	22.5%	0%
• 30% for giving access)	60%	30%	0%
	70%	35%	20%
	105%	52.5%	30%
	140%	70%	40%

Offence	Penalty[1][2]		
	100%	50%	30%
	150%	75%	45%
	200%	100%	60%
Incorrect return or accounts (fraudulently or negligently); periods starting before 1 April 2008 where return is filed before 1 April 2009 (TMA s. 95, 95A; Tax Reporter: 184-875)	Tax geared up to 100% of the tax, subject to mitigation		
Offshore asset moves (FA 2015, Sch. 21) Additional penalty for offshore asset moves from specified territory[8] to non-specified territory on or after 26 March 2015 following an original deliberate failure penalty under: FA 2007, Sch. 24, para. 1; FA 2008, Sch. 41, para. 1; or FA 2009, Sch. 55, para. 6.	50% of the original penalty		

Notes

(1) Interest is charged on penalties not paid when due. The due date is 30 days after the notice of determination of the penalty is issued.

(2) Defences of 'reasonable excuse' or 'special circumstances' may be available.

(3) Late return penalties are cumulative, e.g. for a return six months late, there are two penalties.

(4) The two fixed £100 penalties are reduced if the total tax payable by assessment is less than the penalty which would otherwise be chargeable.

(5) The case A minimum applies if HMRC become aware of the failure less than 12 months after the time when the tax first becomes unpaid by reason of the failure, otherwise the case B minimum applies.

(6) No penalty for inaccuracies that occur despite taking reasonable care.

(7) FA 2015, s. 120 and Sch. 20 introduces a new category of penalty, category 0, which it is anticipated will come into force from April 2016. The new category of penalty will carry the lowest level of penalty equivalent to those currently in category 1 (i.e. 30%, 70% and 100%) and the penalty percentages for category 1 penalties will be increased to 37.5%, 87.5% and 125% respectively.

(8) See below for table of specified territories.

Offshore penalties – territory categories

The table below shows which territories are classified in 'category 1' and 'category 3' for the purposes of penalties for offshore non-compliance. Territories not listed here (other than the UK) are in 'category 2'. Penalties for domestic (UK) matters fall into category 1.

Territories are allocated into one of the categories depending upon the level of information exchange arrangements with the UK, with category 1 territories having the highest level of information sharing arrangements so penalties are the same as for penalties involving domestic matters, whereas territories in categories 2 and 3 have correspondingly poorer information exchange arrangements.

From April 2016, a new category of territory will be introduced, category 0. The new category of penalty will apply to overseas territories making information exchange arrangements with the UK that meet the new Common Reporting Standard. It is envisaged that most or all territories currently in category 1 will, over time, make arrangements so as to fall within category 0 (FA 2015, Sch. 20).

would reduce the income on which he is chargeable below the amount of income tax which he is entitled:

(1) to charge against any other person; or

(2) to deduct from any payment he is liable to make.

Valuation of benefits

The amount of a payment or other benefit is:

(1) in the case of a cash benefit, the amount received; and

(2) in the case of a non-cash benefit, the 'cash equivalent' of the benefit.

The 'cash equivalent' of a non-cash benefit is whichever is the greater of:

(1) the amount which would be chargeable to tax if the benefit were an emolument of the employment chargeable to tax under ITEPA 2003 (see 250) (which would catch a benefit which has risen in value since acquisition); or

(2) the cash equivalent of benefits under non-approved pension schemes (see 422), which largely follows the counterpart rules for employee benefits (see 382).

Notional interest treated as paid if amount charged in respect of beneficial loan

Where a person is taxable under the present provisions on the cash equivalent of a beneficial loan, relief is given which mirrors that available to employees for 'notional interest' payable on a beneficial loan that attracts interest relief (see 406).

Giving effect to the charge to tax

Tax under the present provisions is charged on the employee or former employee, whether or not he or she is the recipient of the payment or other benefit. After the death of the employee or former employee, any outstanding charge is attached to his or her estate (as previously).

Reporting requirements

Employers must provide a report by the 6 July after the tax year in which any termination award is made. (This relaxes the previous requirement of a report within 30 days of the tax year end.)

For more details of the rules concerning ex gratia payments, see 422.

Legislation: ITEPA 2003, s. 401–404; *Income Tax (Pay As You Earn) Regulations* 2003 (SI 2003/2682); *The Tax and Civil Partnership Regulations* 2005 (SI 2005/3229)

Cases: *Colquhoun* [2010] TC 00348

Tax Reporter: ¶437-000

428 The treatment of damages

An employee may commence or threaten legal proceedings for wrongful dismissal or breach of contract. Any payment made in settlement of such a claim is treated as a payment in compensation for loss of office and is chargeable as a specific termination payment, and the usual exemptions apply to it where appropriate (see 424).

Damages for wrongful dismissal or for breach of contract are to put the innocent party in the same position that he would have been in had the contract been carried out. In most instances, the employee would have been liable to tax on the payment. A deduction can accordingly be made to allow for tax from such payments so that the employee is in no better position than he would have been in had there been no breach of contract. This is known as the rule in *Gourley's* case.

Limitations to the Gourley rule

The following limitations to the *Gourley* rule should be noted:

- income tax is only deducted if such tax would have been deducted had there not been a breach of contract; and
- the damages, etc. themselves must not be the subject of a charge to tax.

In the case of damages for wrongful dismissal and breach of contract, the taxpayer would have paid tax on the payments as wages or salary if there had been no breach of contract, but such damages are charged to tax allowing the first £30,000 to be tax-free (see 424). The excess over £30,000, therefore, does not fall within the *Gourley* rule, whereas the first £30,000 does.

Cases: *British Transport Commission v Gourley* [1956] AC 185

Tax Reporter: ¶437-000

PENSIONS

450 Introduction

6 April 2006 was the effective date of a major reform of the taxation treatment of pension schemes. From that date, a single unified tax regime applies in place of the eight previous regimes. This regime applies to all types of schemes and to all members of those schemes, regardless of when they joined. Under the unified regime, there are no limits on the amount that an individual can save in a registered pension scheme. However, there are limits on the amount of pension savings that qualify for tax relief.

Legislation: FA 2004, Pt. 4

Tax Reporter: ¶375-250

of them. Such a transaction could cause the settlor to be liable to income tax on the amount lent or repaid up to the amount of accumulated trust income or, as to any excess, future trust income, not otherwise distributed to beneficiaries, of the next ten years.

A payment by way of a loan or repayment of a loan by a company in which the trustees own shares is also caught under these rules if within five years before or after it, there is an associated payment by the trustees to the company (e.g. a loan or subscription for shares).

Liability to income tax is not affected by the fact that the trustees charge the payment to capital rather than income. The important point is the nature of the receipt in the recipient's hands. If the payment is to maintain a particular historical income level or has the character of income purposes, then it is treated as income. A single lump sum is likely to be of capital whereas a succession of smaller payments income.

It should not be automatically assumed that income tax treatment is unfavourable. If beneficiaries are liable to rates of tax lower than those borne by the trustees, trustees will be able to make distributions without further income tax liability and the beneficiary may even be eligible to make repayment claims. This may be preferable to making distributions of capital involving possible CGT or inheritance tax liabilities. However, capital payments treated as income, as with all other income payments, require a tax credit which is, in turn, deducted from the tax pool (see 991). If the consequence is that the balance on tax pool becomes a negative, then extra tax has, in turn, to be paid over to HMRC.

Tax Reporter: ¶351-100

1007 Treatment of trust beneficiary's income

A beneficiary's share (as grossed up: see 210) of the income of a trust fund forms part of his total income (see 244) in the tax year in which it arises. The income is from the trust and not from the underlying property; hence, except in relation to discretionary trusts (see below), the grossing up process is at the *basic rates* by virtue of the deduction at source being under the normal rules for payments out of profits chargeable to income tax, etc. in the hands of the trustees (see 1368 and 1370).

Example

In 2014–15, Dwight is entitled to a personal allowance of £10,000 (see 1851). His only income is taxable trading income of £13,000 and trust income of £3,000 (received under deduction of basic rate income tax). His total income is thus £16,750 (i.e. £13,000 + (£3,000 × $^{100}/_{80}$)) and his tax liability should be £1,350 (i.e. 20% × (£16,750 − £10,000)). As Dwight has already suffered £750 by deduction, he must pay the balance of £600 to HMRC.

Although trustees are not entitled to deduct management expenses in calculating the trust's tax liability (see 987), such expenses are deductible in ascertaining the beneficiary's income.

A discretionary beneficiary who receives, as income, payments from a trust is treated as receiving an amount net of a rate equivalent to the rate applicable to trusts for the year of payment (see 991).

Cases: *Macfarlane v IR Commrs* (1929) 14 TC 532

Tax Reporter: ¶353-200

1009 Claims in respect of trust beneficiaries' income

Claims on behalf of incapacitated persons are made by the trustees. In other cases, claims must be made by the beneficiary in receipt of income. Claims for repayment relating to trust income which forms part of the beneficiary's total income as it arises must be made, after 1 April 2010, and subject to some transitional measures within four years of the end of the tax year in which the income arises. Those transitional rules are no longer applicable.

The 1 April 2010 revision applies to Self-Assessment taxpayers who sent HMRC a Self-Assessment tax return for the 2007–08 year, and who needed to make a claim for that year. The claim had to be made by 5 April 2012. Slightly different rules applied if the taxpayer was outside Self-Assessment (which might be the expected position for most incapacitated persons). The revised time limits for repayment claims did not take effect until 1 April 2012 so, if outside Self-Assessment, a claim for 2005–06 had to be made before 31 January 2012. For 2006–07, the deadline was 31 March 2012 and for 2007–08 the revised time limit is now fully operational with a, now passed, 5 April 2012 deadline for claims. So 2010–11 is now the earliest year for which a claim can now be made but the claim must be made before 6 April 2015 otherwise they will be out of time.

Tax Reporter: ¶353-200

1010 Trusts with vulnerable beneficiary

On 6 April 2004 a special tax regime for certain trusts with vulnerable beneficiaries began. Under the provisions, certain trusts and beneficiaries are able to elect into the regime and, where a claim for special tax treatment is made for a tax year, no more tax will be payable in respect of the relevant income and gains of the trust for that year than would be paid had the income and gains accrued directly to the beneficiary.

Income and gains arising from the property held on qualifying trusts for the benefit of a vulnerable person are eligible for the new tax treatment. The special treatment does not apply in cases where the settlor is regarded as having an interest in the property from which the qualifying trust's income arose.

Broadly, the amount of income tax relief under the new regime is the difference between two amounts. The first of those amounts is what (were it not for these rules) the income tax liability

1375 Gross or net: manufactured dividends or interest

Manufactured payments are made by one party to a transaction in securities to a second party. They take the place of 'real' payments of interest or dividends that the second party would have received but for the transaction. They arise in a variety of situations, but in particular when stock is lent or sold under a repurchase agreement. From 1 July 1997, the previous complex legislation concerning manufactured dividends was replaced by simplified provisions. Regulations about manufactured interest and dividends provide detailed rules about how the tax due each quarter from those involved is to be accounted for (see below).

Manufactured interest on UK securities

Manufactured interest is any payment by one of the parties to a contract (or other arrangement) for the transfer of UK securities to the other party, which represents a periodical payment of interest on those securities. In relation to the manufacturer, the interest is treated for tax purposes as if it were an annual payment to the recipient, but is neither annual interest nor an amount payable wholly out of profits or gains brought into charge for income tax purposes. The manufacturer is liable to make an annual return of such payments.

A payer who is resident and trading in the UK should deduct tax from the payment at the lower rate, unless the payment relates to either manufactured gilt interest or other interest which is normally paid gross. The gross amount of the payment is deductible in computing the amount of his profits for tax purposes and in the recipient's hands the manufactured interest is treated as if it were real taxed interest. However, if the payer is not resident and trading in the UK, the recipient must account for income tax of an amount equal to that which the payer would have had to deduct had he been resident and trading in the UK.

The interest manufacturer must provide a tax voucher to the recipient showing the gross and net amounts of the manufactured interest, the tax deducted and the date of payment.

Accounting for tax

The machinery for collecting income tax on company payments applies, with modifications, to payments of manufactured interest on UK securities received by UK-resident companies (or non-resident companies which receive such payments for the purposes of a trade carried on by them in the UK through a branch or agency) from non-resident interest manufacturers. The recipient companies (or any person claiming title through them) are treated as if the payment received had borne income tax by deduction. Provision is made for liability for tax in circumstances where the interest manufacturer in question is in receipt of the real interest of which the manufactured interest is representative.

Manufactured interest on gilts

Tax does not have to be deducted from manufactured interest on gilt and certain other securities, either by the manufacturer or the recipient.

Manufactured dividends on UK equities

A manufactured dividend paid by a UK-resident company is treated in the same way as its real counterpart, subject to treatment as a dividend (with a responsibility to account for ACT until its abolition from 6 April 1999: see 3000). In all other cases, an amount equivalent to the ACT which would have been due had the payer been a UK-resident company must be paid over to HMRC. This should be paid by the manufacturer, if he has a presence in the UK, or the recipient.

In either case, the payer must provide a voucher to the recipient in the same way as if the manufactured payment were a real dividend. The voucher should show the amount of the manufactured dividend, the date of payment and the amount of tax credit to which the recipient is entitled.

Provided that the dividend manufacturer is UK-resident and is not a company, the amount of the manufactured dividend actually paid, together with an amount equal to the notional ACT, is allowed as a deduction in computing profits for income tax. However, where the payer is a non-resident company, no deduction is allowed.

Accounting for tax

Provision is made for accounting for tax in relation to manufactured dividends on UK equities other than manufactured dividends paid by UK-resident companies. The tax accounted for on manufactured dividends on UK equities by UK branches of non-resident companies can be set off against corporation tax on their profits.

Manufactured dividends representative of foreign income dividends

A manufactured overseas dividend is a payment, representative of an overseas dividend, made by one party to a transfer of overseas securities to the other. The payment was treated as a foreign income dividend (see 1350) made by the manufacturer until 5 April 1999 (when the foreign income dividend scheme was abolished). The manufacturer was not liable to account for ACT on it.

The recipient of a manufactured overseas dividend was treated for tax purposes as having received a foreign income dividend. He too was not liable to account for ACT on the amount received.

Where the dividend manufacturer was UK-resident and not a company, he was entitled to deduct, in computing his profits for tax purposes, an amount equivalent to the net manufactured payment made. He could not deduct an amount equal to the notional ACT on the payment.

The payer had to provide a tax voucher to the recipient in the same way as if the payment had been a real foreign income dividend. The voucher showed the amount of the manufactured dividend, the date of payment and the fact that the dividend carried no entitlement to a tax credit, etc.

Claimant's death

A deceased claimant's executors could request that any of the married couple's allowance for the year of death which could not be used against his income be transferred to his surviving spouse or civil partner (Independent Taxation Manual IN 492). (The legislation contained no provision to require them to do this in the event of their neglect or refusal). Any election to transfer half or all of the married couple's allowance to a spouse or civil partner will be effectively nullified in the year of the claimant's death. All allowances so transferred will revert to the claimant's estate in the year of his death. Any balance of allowance that could not be used by the claimant's estate is automatically transferred to his widow.

Divorce/dissolution

The married couple's allowance is only due for a tax year at any time during which the couple were married or civil partners and living together.

Divorce or the dissolving of a civil partnership may usually be preceded by separation, the implications of which on the availability of the married couple's allowance are discussed above. It is separation rather than divorce or dissolution itself which will trigger the loss of the married couple's allowance.

Tax Reporter: ¶156-500

1874 Personal allowances for those born on or before 5 April 1938

The basic personal allowance for 'those born after 5 April 1938' is set at £10,600 for the 2015–16 tax year (£10,000 for 2014–15). It will rise to £11,000 for 2016–17 and to £11,200 for 2017–18.

For tax years up to and including 2012–13, entitlement to the basic personal allowance was by reference to an individual being 'aged under 65' throughout the tax year (i.e. by not having attained age 65–74, or age 75 and over, during the tax year so as to trigger entitlement to a higher age-related personal allowance). As part of the withdrawal of the higher age-related personal allowances, from 2013–14 onwards, turning age 65 (or age 75) during the tax year would no longer trigger entitlement to a higher category of allowance. Those higher allowances would continue to be available only to those individuals who had attained age 65 (or age 75) by 5 April 2013 (i.e. individuals who were born on or before 5 April 1948) and individuals who were born after 5 April 1948 (i.e. who would turn age 65 or age 75 on or after 6 April 2013) would remain entitled to the basic personal allowance only, irrespective of their age. Accordingly, the basic personal allowance was re-entitled from 'aged under 65' to 'for those born after 5 April 1948', with effect for the tax year 2013–14 and subsequent years.

From 2015–16 onwards, the higher category of allowance for those 'born after 5 April 1938 but before 6 April 1948' (i.e. individuals who had triggered entitlement to the 'aged 65 to 74' allowance (of £10,500) by 2012–13) was removed from statute as the basic personal allowance of £10,600 had surpassed it. Effectively, the two categories of allowance have been merged so that individuals who were either 'aged under 65' or 'aged 65 to 74' as at 5 April 2013 (i.e. who were born after 5 April 1938) are now entitled to the same personal allowance, which has been correspondingly re-entitled as the 'personal allowance for those born after 5 April 1938', with effect for the tax year 2015–16 and subsequent tax years.

The personal allowance is available to reduce or extinguish taxable income. Any unused allowance cannot be carried forward or back. From 2015–16 onwards, a portion of an individual's unused personal allowance can be transferred to their spouses or civil partners in certain circumstances, but otherwise, the personal allowance cannot be surrendered to another taxpayer. Thus, any personal allowance which cannot be transferred or used in the tax year to which it relates is wasted.

Legislation: ITA 2007, Pt. 3, Ch. 3

Tax Reporter: ¶156-000

1878 Blind person's allowance

An allowance of £2,290 for 2015–16 (£2,230 for 2014–15) is available to a person who proves that he is a registered blind person for all or part of a tax year. For the amount of the allowance for recent years, see Key Data.

A person who becomes entitled to the blind person's allowance by being registered blind will also be granted the allowance for the previous tax year, if, at the end of that year, he had obtained proof of blindness subsequently used to qualify for registration. This concession is intended to prevent people losing the allowance because of delays in the registration process.

Where a blind person is unable to utilise the whole of the allowance because of an insufficiency of income, any excess may be transferred to his or her spouse, or, from 2005–06 onwards, his or her civil partner. The spouse or civil partner must be living with the claimant for the whole or any part of the tax year, and, for new claimants after 6 April 2007, that spouse or civil partner must satisfy the residence condition (ITA 2007, s. 56). Where a claimant was entitled to the allowance before 6 April 2007, the residence condition did not have to be satisfied until the start of the 2009–10 tax year.

Prior to the introduction of the *Income Tax Act* 2007, it was possible for the allowance to be transferred to a non-resident spouse or civil partner who was a commonwealth citizen or an EEA national, which is not one of the qualifying residence conditions now specified in ITA 2007, s. 56. That ability has now been restricted to cases where the claimant is also non-resident and able to claim personal allowances as a commonwealth citizen or EEA national.

that are brought in as assessable income, not the net profits or gains according to commercial principles.

Losses or outgoings of a capital nature, even though incurred in the course of producing assessable income, are not generally deductible. Expenses or losses of a private or domestic nature are not deductible at all.

As to the treatment of trading stock for tax accounting purposes, see 652ff.

The Taxes Acts seldom *expressly* allow deductible expenses, though it is provided that only deductions which are expressly enumerated in the Acts are allowable. The usual form is that the Acts set out what is disallowed, and by implication what is not disallowed is allowed (see 2059); however, certain transactions are effectively ignored, e.g. certain stock lending arrangements are ignored on both the expenditure and income sides (see 646).

In order to be allowable, an expense must normally be of a revenue nature (see 2053) and incurred wholly and exclusively for the purposes of the trade (see 2056).

Timing

Unless a business is using the new cash basis (see 589) from 2013–14, a long-established principle requires that, for tax purposes, expenditure should be taken into account when it is incurred (unless there is some overriding statutory provision or principle developed in the cases to the contrary).

There are special rules for spreading certain pension contributions (see 2062) and there is some uncertainty regarding lease rentals (see 2077).

Purely contingent liabilities cannot be recognised but statistical estimation of facts which had happened but were unknown does seem to be permissible. Hence, for example, the Privy Council has held that a figure for anticipated liability under warranties given with vehicles sold to remedy defects manifesting themselves within 12 months was deductible in computing profits.

Provisions for anticipated losses or expenses

A business makes a 'provision' where it expects to pay out money in the future and takes that probable expense into account when working out its current profits. The legislation requires a business to pay tax 'on the full amount of the profits or gains of the year of assessment' (no more and no less), and the courts until recently (see 2077) took the firm view that, for tax purposes, neither profit nor loss could be anticipated.

Legislation: ITTOIA 2005, s. 7(1), 200(4)

Cases: *Patel* [2015] TC 04225; *Herbert Smith v Honour (HMIT)* [1999] BTC 44; *Jenners, Princes Street Edinburgh Ltd v IR Commrs* (1998) Sp C 166; *Commr of Inland Revenue*

(New Zealand) v Mitsubishi Motors Ltd [1996] BTC 398; *Gallagher v Jones (HMIT); Threlfall v Jones (HMIT)* [1993] BTC 310; *BSC Footwear Ltd v Ridgway (HMIT)* [1972] AC 544; *Duple Motor Bodies Ltd v Ostime (HMIT)* [1961] 1 WLR 739

2053 Capital or revenue expenditure

Revenue expenditure is allowable as a business expense provided it is incurred 'wholly and exclusively for the purposes of the trade, etc.' (see 2056) and is not specifically disallowed in the Taxes Acts (see 2059). Usually, there is no problem in distinguishing between expenditure on revenue account and expenditure on capital account. Thus, the cost of purchasing (whether by a single payment or by way of instalments of the lump sum cost) business premises is capital expenditure, while rent paid for business premises is revenue expenditure, and the cost of alterations, additions, improvements or renovations is capital, while the cost of repairs is revenue.

There is clearly some overlap between the various 'tests' below which have been suggested by the courts.

Note that the capital versus revenue issue will not be the same for those businesses using the cash basis (see 589).

Fixed and circulating capital

Fixed capital and circulating capital should be distinguished. Fixed capital represents those assets which are retained and used in order to make profits, e.g. machinery used to make cars in a car factory is part of the fixed capital. Circulating capital on the other hand represents those assets which are bought and sold in the ordinary course of trade, e.g. machinery bought and sold by a trader in machinery is part of the circulating capital and the cost of it is deductible. In one case, £733,649 claimed as the cost of winding up a North Sea Oil operation was held to be a non-deductible capital expense as the cost related to the profit-making structure of the business, i.e. fixed capital.

The cost of 'creating, acquiring or enlarging the permanent … structure of which the income is to be the produce or fruit' is of a capital nature, while 'the cost of earning that income itself or performing the income-earning operations' is a revenue expense. Applying these dicta, the Privy Council has held that interest paid by a Hong Kong development company on a loan obtained for a capital project was a payment on capital account, which was therefore not deductible from its taxable profits: the fact that interest is income in the recipient's hands and a recurring and periodic payment does not necessarily mean that it is a revenue expense.

With respect to operations after 6 April 1989, expenditure on making good landfill sites for waste disposal qualifies as a revenue deduction for persons holding disposal or waste management licences (unless capital allowances are available): expenditure on preparing a site is written off according to the proportion of site capacity filled with waste in the appropriate period, and expenditure on making good a site is allowed as a trading expense in the period

Type of payment	Include in gross pay for NIC purposes?
Maternity suspension payments made under the *Employment Rights Act* 1996 to an employee suspended from work on maternity grounds	Yes
Meal allowances and vouchers	
• cash payments for meals	Yes
• vouchers redeemable for food and drink or a cash alternative	Yes (see 2580)
• vouchers provided for food and drink provided on your business premises or any canteen where meals are generally provided for your staff	No
• vouchers redeemable for meals only	No
Medical suspension payments made under the *Employment Rights Act* 1996 to an employee suspended from work on medical grounds	Yes
Mobile phone vouchers to obtain one mobile phone for private use	No
Mortgage payments met directly by you for employees	
• mortgage provided by you or mortgage contract is between you and mortgagee	No, but there may be a liability for Class 1A, see 2650.
• mortgage contract is between employee and mortgagee	Yes
Parking fees at the normal place of employment paid for or reimbursed to employees	No
Payments in kind (but not readily convertible assets – see 2566)	
• which can be turned into cash **by surrender** such as Premium Bonds, and so on	Yes
• which can be turned into cash only **by sale** such as furniture, kitchen appliances, holidays and so on	No, but there may be a liability for Class 1A, see 2650ff.
Payments you make to an employee whilst he or she pursues a claim for **damages against a third party** for loss of earnings following an accident	
• employee must repay you, even if the claim for damages is unsuccessful	No
• employee not required to repay you	Yes, but if the employee later receives damages and repays you, NICs can be refunded

Type of payment	Include in gross pay for NIC purposes?
Pensions from:	
• registered pension schemes	No
• employer-financed retirement benefits schemes	No, if the payment satisfies certain conditions
Personal bills paid for goods and services supplied to employees, club memberships and so on	
• contract to supply goods and services is between you and the provider	No, but there may be a liability for Class 1A, see 2650ff.
• contract to supply goods and services is between the employee and the provider	
– payment made direct to the provider	Yes
– payment made or reimbursed direct to the employee	Yes
Phone calls and/or rental cost – Employer is the subscriber	No, but there may be a liability for Class 1A, see 2650ff.
Employee is the subscriber but, **employer meets the cost of calls and/or rental**:	
• phone used exclusively for business use	No
• phone used exclusively for private use	Yes
• phone used for both business and private use	Rental: yes – on the full amount of the
	Calls: yes – on the full amount of the cost of private calls. Any amount in respect of business calls, supported by appropriate evidence, can be excluded
Premiums for health cover, pensions, annuities and so on	See 'Insurance premiums' above
Prize money paid in cash to employees for competitions you run in connection with your business, which are not open to the public	Yes
Readily convertible assets: remuneration provided in non-cash form such as stocks and shares, gold bullion, commodities, fine wine and so on.	See 2566
Redundancy payments	See 2588
Relocation payments	See 2590
Retirement benefits schemes – payments you make into such schemes	

For the majority of companies which do not have complex borrowing or lending arrangements and are not attempting to exploit the loan relationship rules for tax avoidance, the legislation is simple to apply and is generally helpful. However, the rules behind the simple principle of taxing/relieving the profit and loss account entry are inevitably complex. They are found in CTA 2009, Pt. 5.

Money debts

'Money' is defined to include money expressed in a currency other than sterling. A money debt is a debt settled in money, or by the transfer of a right to settlement under a debt which is a money debt. 'Money', which is not defined further, must be taken to have its ordinary meaning. It would not, therefore, include physical commodities or a barter arrangement. 'Debt' includes a debt the amount of which falls to be ascertained by reference to matters which vary from time to time.

A transaction for the lending of money

The rules provide the following guidance on the meaning of this term:

- where an instrument is issued to evidence any money debt, the debt is taken to have arisen from a transaction for the lending of money. This is intended to catch a situation where the original transaction is not one for the lending of money so the debt would not otherwise be a money debt arising from a transaction for the lending of money and bring the debt into the loan relationship provisions by virtue of the issue of the security. The instrument must be issued for the purpose of representing a security, and not simply documenting a transaction (such as a contract for a monthly service charge payable in arrears). An example would be a sale of shares in a company where the vendor receives part of the consideration in loan note;
- a debt arising from rights conferred by shares in a company does not arise from a transaction for the lending of money;
- 'loan' includes any advance of money.

According to the Revenue press release announcing the publication of the original draft legislation (REV 21 of 28 November 1995), a loan relationship would arise from any debt 'which, under general law, is a loan'. So any transaction which would generally be regarded as lending would qualify, e.g. unsecured loans, overdrafts, drawn-down credit facilities, in addition to all securitised debts. Neither the duration of the financing, nor the form of payment for the loan – interest, discount, premium, or any combination – is relevant. Finance leases are excluded for, whatever their economic character, they are not loans for legal purposes.

From 6 April 2005, references to loan relationships include references to 'alternative finance arrangements' for the taxation of lending under Shari'a law.

HMRC have confirmed that straightforward commercial contracts and invoices do not represent a security, and therefore, not a transaction of lending money. However, it would seem possible for such a transaction to become a transaction of lending – for example, where a debtor is granted extended time to pay.

Any instrument which represents a pure equity interest in a company cannot be a loan relationship. The reference to 'shares in a company' is qualified by CTA 2009, s. 476, in that the term 'share' is deemed to mean any share under which entitlement to receive distributions may arise. It must therefore be taken to include preference shares. Building society shares are not shares for this purpose (CTA 2009, s. 476) so debits and credits on those shares are taken into account under the loan relationship rules. Equity instruments which have some debt-like characteristics, such as convertibles, may rank as loan relationships but are subject to special rules.

The special commissioners have decided that, on the proper construction of the FA 1996 basis for the taxation of profits or losses arising from loan relationships, receipts from the making of contracts for financial futures by a number of life insurance companies were not subject to the loan relationship regime. Although tax considerations played a decisive part in the choice of structures, the transactions were genuine and not shams and the deliberate tax-efficient structuring of the business did not affect the commercial and legal characterisation of what was done (*HSBC Life (UK) Ltd v Stubbs (HMIT)* and related appeals). The mere economic equivalence of a transaction to a loan did not show that it was a loan. The authorities showed that the concept of 'loan' or 'lending' might vary from statute to statute if a particular meaning was adopted. By specifically referring to the concept of 'a transaction for the lending of money', CTA 2009, s. 302(1)(b) intended to confine a concept whose extent might otherwise be uncertain within well-known and ascertainable bounds. It was impossible to conclude that any of the parties to the transactions thought that they were lenders or borrowers, or that they intended that to be the case. They plainly intended to enter into the legal relationships which the documentation showed that they established, and they took care to enter the relationship of buyer and seller of financial futures and not that of lender and borrower. The fact that, in doing so, they were clearly anxious to fall within one tax regime rather than another was beside the point.

Relevant non-lending relationships

The application of the loan relationship legislation is extended by CTA 2009, s. 481 to money debts not arising from a transaction for the lending of money (referred to as a 'relevant non-lending relationship') where the debt is one:

(a) on which interest is payable (or receivable);
(b) on which a foreign exchange gain or loss arises;
(c) for creditor companies, in relation to which an impairment loss arises, or, with effect from 22 April 2009, where a release debit arises, in respect of a business payment;
(d) for debtor companies, from 22 April 2009, in relation to which a trading deduction or a UK or overseas property business deduction has been allowed to the company and which is released; or
(e) on which a discount arises to the company

In relation to (c) above a business payment means a payment which, if it were paid, would fall to be brought into account for tax purposes as a receipt of a trade, UK property business or overseas property business. For example, a provision against trade debtors would fall into this category. As to the reasons for the extension in (d) above to some debtor company relationships from 22 April 2009, see below.

Legislation: TCGA 1992, Sch. 7AC, para. 38; TCGA 1992, Sch. 7AC, para. 33; TCGA 1992, Sch. 7AC, para. 4(1)(b)

Tax Reporter: ¶760-150 and ¶760-100

TRANSACTIONS INVOLVING A NON-RESIDENT COMPANY

TRANSFER OF FOREIGN BRANCH TO FOREIGN COMPANY

3460 Transfer of assets to a non-resident company

If a company decides to transfer the business of a foreign branch to a company not 'resident in the UK' (see 3020) any net chargeable gain made on the transfer can be rolled over for a potentially indefinite period to the extent that shares are received in return. The net chargeable gain is the aggregate of chargeable gains arising from the transfer after the deduction of allowable losses so arising.

This rule only applies if the transferor is a UK-resident company which carries on a trade through a foreign permanent establishment. The transferor must transfer the business and all its assets in the branch to a non-resident company and must hold not less than 25% of the ordinary share capital of the transferee company after the transfer.

Where applicable, the transferor can choose between this deferral and the relief by reference to notional tax in the home territory, if it is within the EU (see 3490).

Time when deferment ends

The deferment of tax will come to an end when the shares are disposed of or the assets transferred are disposed of (see 3465, 3470 and 3475).

When there is a disposal of this kind, the deferred gain is chargeable to corporation tax along with the consideration for the disposal.

Portion of gain chargeable

If shares are received by the transferor as part consideration for the transfer, only a fraction of the gain is taken into account when the deferment comes to an end. The fraction is the proportion which the market value of the shares bears to the total consideration.

If the shares received by the transferor company represent the whole of the consideration for the transfer, the whole of the gain can be deferred.

Example

Company A merges its US branch with S Inc (incorporated in US) in 2011. Total consideration for transfer of assets in US branch (market value):

	£
£1 shares in the merged US company issued to A to value of	40,000
Cash payment	60,000
	100,000

Assume the net gain to A on transfer (ignore indexation) is £30,000. Shares form only part of the consideration.

Therefore, fraction of gain deferrable is

$$\frac{\text{market value of shares}}{\text{market value of total consideration}} = \frac{£40,000}{£100,000} = \frac{4}{10}$$

The gain deferred is £30,000 × 4/10 = £12,000.

Legislation: TCGA 1992, s. 140(1)–(3)

Tax Reporter: ¶758-850ff.

3465 Disposal or part disposal of foreign transferee's shares by transferor

If, following relief on the transfer of assets to a non-resident (see 3460), the transferor disposes of all or a part of the shares issued to him, and the disposal takes place on or after 6 January 2010, the whole or the appropriate proportion of the deferred gain is deemed to accrue to the transferor company in addition to any gain or loss that actually accrues on the disposal of the securities. For disposals before that date, the consideration which the transferor company received for the disposal was increased by the appropriate proportion of the deferred gain so far as not previously brought back into account. In both cases, the fraction of the gain brought into account on the part disposal is the proportion of the market value of the shares disposed of to the market value of the shares held immediately before the disposal.

Example

Assume the same facts as contained in the example in 3460.

In 2012, shares issued to A rose in value to £60,000. A decided to sell 15,000 at market value which is £22,500.

Fraction of capital gain brought into account:

$$\frac{\text{market value of shares disposed of}}{\text{market value of total shares prior to disposal}} = \frac{£22,500}{£60,000} = \frac{3}{8}$$

The gain brought back into charge is 3/8 × £12,000 = £4,500

Example 2

From Example 1 above, Gross plc has a corporation tax liability for the nine-month accounting period ended 30 September 2011 of £2.5m. Its instalments are calculated as follows:

CTI = £2,500,000

n = 9 months

			Cumulative total of tax paid
First instalment:	$\frac{3}{9} \times 2{,}500{,}000$		
Lesser of CTI and formula	= 833,333.33	due 14 July 2011	833,333.33
Second instalment:	$\frac{3}{9} \times 2{,}500{,}000$		
	= 833,333.33 A		
Balance of tax after first instalment	1,666,666.67 B		
Lesser of A and B	833,333.33	due 14 October 2011	833,333.33
Third instalment:	$\frac{3}{9} \times 2{,}500{,}000$		
	= 833,333.33 C		
Balance of tax after first and second instalments	833,333.33 D		
Lesser of C and D	833,333.33	due 14 January 2012	833,333.33
Total tax paid in instalments			2,500,000.00

If, using the same corporation tax liability, Gross plc instead ended its accounting period on 15 May 2011, its instalments would be reduced in number as follows:

CTI = £2,500,000

n = 4.5 months

			Cumulative total of tax paid
First instalment:	$\frac{3}{4.5} \times 2{,}500{,}000$		
Lesser of CTI and formula	= 1,666,666.67	due 14 July 2011	1,666,666.67
Second instalment:	$\frac{3}{4.5} \times 2{,}500{,}000$		
	= 1,666,666.67 A		
Balance of tax after first instalment	833,333.33 B		
Lesser of A and B	833,333.33	due 29 August 2011	833,333.33
Total tax paid in instalments			2,500,000.00

Repayments of excessive instalments

Any instalment payments already made will normally be repaid if a company decides on reflection that they ought not to have been paid and the aggregate amount already paid exceeds the aggregate amount which should have been paid using the revised total liability. A claim can be made for repayment of the excess amount. Such a claim must give the amount being reclaimed and the grounds for making the claim. The commissioners may determine the amount which should be repaid where an assessment is under appeal prior to determination of the final liability. An application to the commissioners for such a determination will be treated like an appeal.

Repayments will carry interest (see below). Repayments of excess instalments may also be surrendered within a group.

Miscellaneous requirements

The following matters are also covered by the regulations:

- HMRC's right to request such information, including copies of books, documents and other records, relating to the calculation of instalments as they may 'reasonably require'; and
- the right of inspection of any records so required.

For arrangements for groups of companies, including arrangements whereby one company will be able to make instalment payments on behalf of the group, see 3770.

Legislation: TMA 1970, s. 59D, 59DA, 59E and 87A; ICTA 1988, s. 826A; *Corporation Tax (Instalment Payments) Regulations* 1998 (SI 1998/3175)

Tax Reporter: ¶811-050ff.

Example

Andy gives as a wedding present to his daughter a plot of land which has planning permission for a house. The gift is subject to a restriction in favour of Andy that no building may be built on the land. His daughter accepted the gift knowing about the restriction.

The land is valued as follows:

	£
Land with planning permission	50,000
Land with restriction	(10,000)
Increase in value on extinction of restriction	40,000
Market value of restriction	£12,000

On making the gift, Andy is treated as making a disposal of £50,000 less the lower of:
(1) £12,000 (market value of the restriction);
(2) £40,000 (increase in value on extinction of restriction),

i.e. A is treated as making a disposal for £38,000.

Legislation: TCGA 1992, s. 18(6)

Tax Reporter: ¶503-800

5142 'Connected persons' for CGT

Individuals

A person is connected with an individual if he is:

(1) the individual's spouse or civil partner;

(2) the individual's relative;

(3) the spouse or civil partner of a relative of the individual;

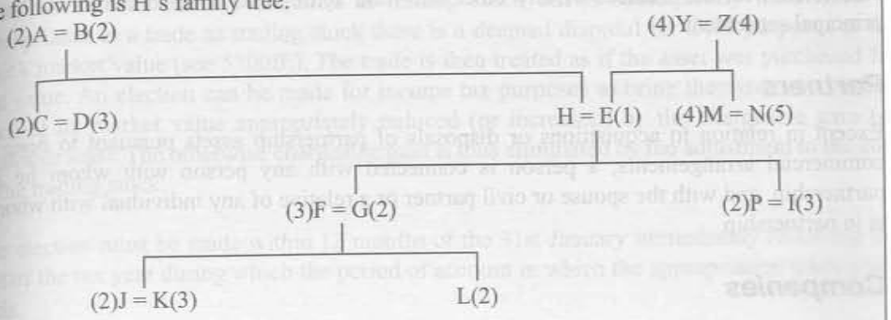
(4) a relative of the individual's spouse;

(5) the spouse or civil partner of a relative of the individual's spouse or civil partner.

'Relative' means brother, sister, ancestor or lineal descendant.

Example

The following is H's family tree:



H is connected with all persons shown in this family tree in the manner indicated by the numbers which reflect his relationship with them as shown by (1)–(5) above.

Trustees

The settlor of a settlement and any trustee of the settlement are connected (TCGA 1992, s. 286(1), (3)). The terms 'settlement' and 'settlor' were originally imported from what is now ITTOIA 2005, s. 620. Thus a settlement is 'any disposition, trust, covenant, agreement, arrangement or transfer of assets' involving an element of bounty.

For periods prior to 6 April 2006, a settlor was 'any person by whom the settlement was made'. However, *Finance Act* 2006 replaced that imported definition with a general definition applicable for most capital gains purposes. In essence, it still refers to a person who 'makes' a settlement, but expands to deem other actions to be making a settlement also.

Also with effect from 6 April 2006, a specific definition of 'trustee' is now provided for 'connected persons' purposes. Where there would otherwise be no trustee, any person in whom the settled property is vested or who is charged with the management of that property is to be treated as a trustee.

A trustee is also connected with any other person who is connected with the settlor, e.g. a fellow trustee in relation to the same trust, members of the settlor's family (see previous subheading), a person with whom the settlor is in partnership, a company controlled by the settlor (or by him/her and other persons connected with him/her) or any person with whom he/she acts to secure control of a company, etc.

A trustee is connected with any body corporate which is a close company (or a company which would be close, if UK-resident), and of which the trustees are participators or a body controlled (within the meaning of ITA 2007, s. 995; CTA 2010, s. 1124 for corporation tax) by a such a company.

they are sometimes used where a company is sold for amounts which depend on the future profitability of the company's business. This postponement of the tax charge can be overridden by an election by the vendor of the shares.

Legislation: TCGA 1992, s. 138A

Cases: *National Westminster Bank plc v IR Commrs; Barclays Bank plc v IR Commrs* [1994] BTC 236

Tax Reporter: ¶555-000; ¶561-550; ¶561-600

SHARE IDENTIFICATION

5820 Need for share identification rules

Where shares of the same class in the same company have been acquired at different times and at different prices, some form of identification rules are needed to establish which of those shares have been sold, where a sale takes place which is of less than the full amount of the total holding.

For all in-date years there are three sets of identification rules applicable to:

(1) disposals from 6 April 2008 onwards by individuals and trustees;

(2) disposals in the years up to 5 April 2008 by individuals and trustees;

(3) disposals by companies.

Tax Reporter: ¶556-500

5826 Identification rules for individuals and trustees: 2008–09 onwards (and years to 2007–08 inclusive)

Disposals on or after 6 April 2008 are to be identified with acquisitions in the following order:

(1) same-day acquisitions;

(2) acquisitions within the following 30 days on the basis of earlier acquisitions in that period, rather than later ones (a FIFO basis); and

(3) securities within the expanded 's. 104 holding' (see below), which specifically does not include acquisitions under (1) and (2) above.

Where the number of securities which comprise the disposal exceed those identified under the above rules, that excess is identified with subsequent acquisitions beyond the 30-day period referred to above.

Same day transactions

Before a disposal is identified with any previous acquisition or pool, it is matched, as far as possible, with acquisitions on the same day which are made in the same capacity. For this purpose, all acquisitions on the same day are treated as if they were made by a single transaction and all disposals on that day are similarly treated as made by a single transaction.

A 'bear' transaction is one whereby the taxpayer disposes of shares or securities which he intends to acquire but does not hold at the time of the disposal. In such a case, unless the taxpayer is a company and the disposal is identified with acquisitions according to other 'prescribed period' anti-avoidance provisions, the disposal is matched with the first shares or securities of that type subsequently acquired by the taxpayer in the same capacity. If there remains a balance of unmatched shares or securities, they are identified with the next subsequent acquisition, and so on.

HMRC have confirmed (*Tax Bulletin 52*) that this same-day rule, which treats a disposal as being identified with an acquisition on the same day, does not serve to frustrate a 'negligible value' claim. Concern had been expressed that the interaction the same-day rule and such a claim, which deems there to be a disposal and an immediate re-acquisition, would mean that, on the deemed disposal, neither a gain nor a loss would arise because the securities disposed would be treated as being those deemed to have been re-acquired. It also follows that where a deemed disposal and re-acquisition would give rise to a gain, that gain cannot be avoided by relying on the same-day rule.

Alternative treatment of shares acquired on the same day

Because of the general identification rule, employees who acquired shares under an approved share option scheme at a low base cost and, on the same day, acquired other shares of the same class at a higher value, would find that the acquisition costs would be averaged.

Where an individual:

- has acquired two or more holdings shares on or after 6 April 2002 as a result of transactions on the same day and in the same capacity, referred to as the 'relevant shares';
- those shares are all of the same class; and
- some of those shares were acquired under an Enterprise Management Initiative or an approved share option scheme, without incurring a charge to income tax,

he may elect an alternative identification rule to apply on any subsequent disposal of any of the relevant shares.

The time limit for the election is the first anniversary of 31 January next following the end of the tax year in which the first disposal of any of the relevant shares is made; in other words, 22 months after the tax year concerned. Once made, the election will apply to that disposal and all subsequent disposals of the relevant shares.

6244 Extent of exemption under private residence relief

To obtain complete exemption from CGT under the private residence provisions (see 6220), the house must have been the individual's only or main residence throughout the period of ownership, except for the whole or any part of the last 18 months of ownership.

The final period exemption was reduced from 36 months to 18 months with effect for disposals made on or after 6 April 2014 with an exception for individuals who are disabled or in a care home and with no other property who continue to be entitled to a 36-month final period exemption.

'Period of ownership' is determined by reference to the first interest obtained in the property and may include that of a spouse but does not include any period before 31 March 1982 (TCGA 1992, s. 223(7)(a)).

In determining the amount of relief attributable to NRCGT gains on disposals on or after 6 April 2015, 'period of ownership' excludes periods prior to 6 April 2015 unless an election has been made for the NRCGT gain to be calculated using the retrospective basis of computation (see 5717) (TCGA 1992, s. 223(7)(b) and (7A)).

By concession, where there is a short delay in taking up residence, the period before taking up residence will be treated as a period of occupation for the purposes of the relief in the following circumstances:

- where an individual acquires land on which a house is built which is then used as the only or main residence; or
- where an existing property is purchased but before using it as the only or main residence, the individual arranges for alterations or redecorations or completes the necessary steps for disposing of the previous residence.

The concession applies to a period of up to one year unless there are good reasons outside the individual's control in which case the period may be extended up to a maximum of two years.

Where the house has not been the only or main residence throughout the period of ownership (exclusive of the last 18 or 36 months), only a fraction of the gain is not liable to CGT. That fraction is:

$$\frac{A + B}{C}$$

A is the period after 31 March 1982 during which the house was the individual's only or main residence (but not including the last 18 or 36 months (as applicable) of the period of ownership);

B is the last 18 or 36 months of ownership (plus up to 24 months initial period); and

C is the total period of ownership after 31 March 1982.

Example

Jack buys a house on 1 June 2004 for use as his only residence. He lives in the house for seven years and six months (90 months) before moving out and immediately occupying a nearby flat which he also owns. He elects for the flat to be his only or main residence from 1 December 2011 (date of initial occupancy). Jack does not return to live in the house and it remains empty until he sells it on 31 May 2015, making a gain of £82,500. The chargeable gain covering Jack's 11 years (132 months) of ownership is calculated as follows:

	£
Indexed gain	82,500
Private residence exemption	
Using $\frac{A + B}{C}$ formula above	
A = 90 months	
B = 18 months	
C = 132 months (11 × 12)	
$\frac{90 + 18}{132} \times £82,500 =$	(67,500)
Chargeable gain	15,000

The gain is also apportioned where part of the dwelling-house is used exclusively for the purposes of a trade, business, profession or vocation and the consideration may be apportioned where otherwise necessary. HMRC no longer apply the rule-of-thumb that one-third of a farmhouse is used for business purposes – each case must be considered on its particular circumstances.

Relief may be adjusted where there is a change in the extent to which a property is used as an individual's residence, etc. There are also provisions relating to periods of absence which may be treated as periods in which the property was used as the individual's only or main residence (see 6247).

Legislation: TCGA 1992, s. 222(7), (10), 223(1), (2), (5)–(7), 224(1), (2), 225E

Other Material: ESC D49, *Private residence relief: short delay by owner-occupier in taking up residence*

Tax Reporter: ¶546-450; ¶546-650

6245 Private residence relief: non-qualifying tax years

For disposals on or after 6 April 2015, a residence will be treated as not being occupied as a residence for a tax year (the 'deeming' rule) when it is located in a territory in which neither the person making the disposal nor their spouse or civil partner is tax resident and they (either the

(see 7008) or pre-1978 protective trusts or historic buildings funds (see 7371) applies, on becoming:

- property held for charitable purposes only without limit of time;
- the property of a political party qualifying for exemption (see 7195);
- the property of a body mentioned in 7198 (national purposes, etc.); and
- the property of a body not established or conducted for profit.

Legislation: IHTA 1984, s. 76

Other Material: *HMRC Inheritance Tax: Customer Guide* available on the HMRC website at www.hmrc.gov.uk/cto/customerguide/page1.htm

Tax Reporter: ¶645-300

7017 Initial interest of settlor, spouse or civil partner

If a settlor or his spouse, or civil partner, is beneficially entitled to an interest in possession in property immediately after it becomes comprised in the settlement, the property will be treated as not being comprised in the settlement on that occasion. However, where any of the same property becomes held on trusts under which neither of the spouses or partners is beneficially entitled to an interest in possession, that property will be treated as becoming comprised in a separate settlement.

A 'spouse of a settlor' includes a widow or widower of a settlor.

Legislation: IHTA 1984, s. 80

Other Material: *HMRC Inheritance Tax: Customer Guide* available on the HMRC website at www.hmrc.gov.uk/cto/customerguide/page1.htm

7020 Property moving between settlements

Where property ceases to be comprised in one settlement and becomes comprised in another, it will be treated as remaining comprised in the first settlement unless any person has become beneficially entitled to that property and not merely to an interest in possession in it.

Legislation: IHTA 1984, s. 48(6), 81

Other Material: *HMRC Inheritance Tax: Customer Guide* available on the HMRC website at www.hmrc.gov.uk/cto/customerguide/page1.htm

7023 Distributions within two years of death

Where property comprised in a person's estate immediately before his death is settled by his will and a chargeable event occurs within the period of three months to two years after his death, IHT will not be charged if no interest in possession has subsisted in the property. This is a relieving provision which disapplies the exit charge which would otherwise apply: for deaths occurring before 10 December 2014, it could not apply during the first three months after the death as there would be no exit charge in any case during this time.

In addition, the distribution was treated as if it were made under the will and is thus effectively 'back-dated' to the date of the testator's death. This 'two-year discretionary trust' can be a favoured tax planning device which may be employed to use up the nil-rate band available to the testator, while the residue of the estate is left to (e.g.) the testator's spouse. Alternatively, the will may create a discretionary trust over the whole estate, so that it can be distributed after the testator's death in the manner then considered to be the most tax-efficient.

Where capital is appointed, under a will, for deaths on or after 10 December 2014, then IHTA 1984, s. 144 will be amended, reversing the *Frankland* decision, where property was left in trust, and subsequently appointed to either the surviving spouse or civil partner of the deceased, then the appointment will be treated as having been made by the will not withstanding that the appointment was within the first three months after death (under the previous position, a charge to tax could have arisen as the spouse/civil partner exemption would not but for this change have been available).

Distributions out of a trust for a charity or other exempt body (see 7014), an employee trust (see 7005) or a national heritage maintenance fund (see 7371ff.) made within two years of the deceased's death are already exempt from any charge. Such distributions will be treated as taking place at the date of death so reducing the deceased's chargeable estate.

Legislation: IHTA 1984, s. 144; Finance (No. 2) Bill 2015, cl. 14

Cases: *Frankland v IR Commrs* [1997] BTC 8045

Other Material: *HMRC Inheritance Tax: Customer Guide* available on the HMRC website at www.hmrc.gov.uk/cto/customerguide/page1.htm

Tax Reporter: ¶676-900

7040 Property becoming comprised in maintenance funds

The transfer into trust of various historic buildings or works of art, etc. is either exempt from IHT or conditionally exempt from IHT (see 7346ff. and 7371ff.). There are special modifications to the trust regime to cater for these arrangements where other trusts are involved.

Legislation: VATA 1994, Sch. 4, para. 7; *Value Added Tax Regulations* 1995 (SI 1995/2518), reg. 9, 27, 30

Other Material: Notice 700, *The VAT guide*

Website: www.hmrc.gov.uk

7766 Self-supplies

In some circumstances a business can be treated as making supplies to itself. This arises in certain cases specified in statutory instruments, in certain cases relating to land, and in other instances covered below. In these cases the business must account for tax on the self-supply, but can then treat it as input tax as if the supply had been obtained from another trader. This might seem self-defeating, in that the tax would simply appear on both sides of the VAT return and cancel out, but the effect would be felt by partially exempt businesses that can't recover all the input tax charged to it.

(1) Self-supply of motor car

VAT suffered on the purchase of a motor car cannot be recovered if the car is to be put to any non-business use (such as private mileage, including home to work travel by an employee). Input tax on car purchase is recoverable if the car is to be used wholly for business purposes. However, if VAT is recovered on this basis and the car is subsequently put to non-business use, a self-supply arises.

(2) 'Self-supply' of residential or charitable building (a change of use charge)

A charge to VAT occurs when zero-rating under VATA 1994, Sch. 8, Grp. 5 has been obtained on the purchase or construction of a building for relevant residential or charitable use and, within ten years, the building is put to a non-qualifying use. These provisions are in VATA 1994, Sch. 10, para. 36.

(3) Self-supply of construction services

A self-supply arises if certain works of construction are carried out by a business without using outside contractors. If the value of the works is £100,000 or more, and they would have been positive-rated if bought in, a self-supply arises.

(4) Self-supply on acquisition of business by group

A self-supply arises where a business is transferred, as a going concern, to a VAT group of companies. This is intended to counter certain planning techniques which were previously available. The relevant provisions are in VATA 1994, s. 44.

If the group is partially exempt either during the prescribed accounting period (i.e. VAT return period) in which the supply takes place, or in the 'longer period' (see 8110ff.) which includes it, then a self-supply takes place. However, there is no self-supply if it can be shown that all of the assets transferred were acquired by the transferor more than three years before the transfer.

Legislation: VATA 1994, Sch. 10, para. 36; *Value Added Tax (Self-supply of Construction Services) Order* 1989 (SI 1989/472); *Value Added Tax (Cars) Order* 1992 (SI 1992/3122), art. 5

Website: www.hmrc.gov.uk

VAT Reporter: ¶12-795

7768 Reverse charge supplies

In some instances where a supply is made, it is treated as if it had been made by the customer rather than by the person who made the supply (the 'reverse charge'). This is relevant where the supply is made across an international boundary (see 7820).

The effect is that the customer (if registrable for VAT somewhere in the EC and this includes the UK) must account for output tax on the supply and can treat the same amount as potentially recoverable input tax. The input tax may, or may not, be deductible in full depending on the use to which the supplies are put (i.e. the normal VAT rules apply).

The reverse charge has become particularly important since 1 January 2010 under the new VAT package (see 7820).

Reverse charge supplies also count when considering whether the taxable turnover of the person carrying on the business exceeds the VAT turnover limits, making registration necessary (see 7792ff.).

See also 8492 in respect of the introduction of reverse charge accounting in relation to the supply of certain goods of a kind used in missing trader intra-Community fraud (MTIC).

Further to EU Directive 2013/43/EU introducing the Reverse Charge Mechanism, HMRC have confirmed that the UK will continue to apply the reverse charge for mobile telephones, computer chips and emissions allowances in their current forms. The Reverse Charge Mechanism allows these measures to run until the end of 2018.

Legislation: VATA 1994, s. 8, s. 7A and Sch. 4A

Other material: HMRC Brief 36/13

VAT Reporter: ¶13-350

Other Material: Notice 700/50, *Default surcharge* – new version (December 2011)

Website: www.hmrc.gov.uk

VAT Reporter: ¶60-450

8520 The penalty regime for errors from 1 April 2009

HMRC introduced a new penalty regime for errors, which applies across all the major taxes including VAT. Penalties are linked to the behaviour that gives rise to the error. People who take reasonable care when completing their returns will not be penalised. If they do not take reasonable care, errors will be penalised, and the penalties will be higher if the error is deliberate. Disclosing errors to HMRC early will substantially reduce any penalty due.

'Reasonable care' varies according to the person, the particular circumstances and their abilities. Every person is expected to make and keep sufficient records for them to provide a complete and accurate return. A person with simple, straightforward tax affairs needs only keep a simple system of records, which are regularly and carefully updated. A person with larger and more complex financial tax affairs will need to put in place more sophisticated systems and maintain them equally carefully. HMRC believe it is reasonable to expect a person who encounters a transaction or other event with which he is not familiar, to take care to check the correct tax treatment, or to seek suitable advice. HMRC expect people to take their tax seriously.

The new penalties apply to errors on VAT returns and also (among others) to corporation tax and income tax.

The penalties apply to returns or other documents for return periods starting on or after 1 April 2008 that are due to be filed on or after 1 April 2009.

The penalty charged will be a percentage of the extra tax due. The rate depends on the behaviour that gave rise to the error. The less serious the behaviour, the smaller the penalty will be. The charges are as follows:

- Reasonable care: no penalty;
- Careless: minimum penalty 0% up to maximum of 30%;
- Deliberate: minimum penalty 20% up to maximum 70%; and
- Deliberate and concealed: minimum penalty 30% up to maximum 100%.

Finance Act 2008 extended the new penalties for incorrect returns across most taxes, levies and duties, for incorrect returns for periods commencing from 1 April 2009 where the return is due to be filed from 1 April 2010.

Legislation: FA 2007, Sch. 24

Other Material: Notice 700/45 *How to correct VAT errors* (July 2015 edn)

8522 Repayment supplement

A repayment supplement is added to certain late repayments of VAT shown as repayable on a VAT return. Any overpayment may often be offset against any underpayment by the taxpayer of tax, penalty, interest or surcharge.

In order to qualify for such a supplement, the return or, as regards local authority, etc. refunds, claim must have reached HMRC by the proper due date for its submission.

Repayment supplement is then due if HMRC fail to issue the written instruction directing the making of the repayment within 30 days of the later of:

- the end of the period concerned; and
- the date when HMRC received the return.

In determining whether the instruction is issued within the 30-day period, certain periods are ignored. These periods are those taken in making reasonable enquiries about the return, or correcting errors in the return, and periods in which the trader has failed to submit other returns, or pay the tax due on them or on assessments issued by HMRC, or comply with the conditions concerned with the production of documents or the giving of security.

If the return overstates the amount of the repayment due by more than the greater of 5% and £250, no supplement is payable.

The supplement is the greater of 5% of the repayment due or £50. There is a table of rates in the Key Data section.

Legislation: VATA 1994, s. 79

VAT Reporter: ¶60-650

8528 The misdeclaration penalty

This has now been replaced by the new errors penalty regime (see 8520 above) from 1 April 2009.

8544 Interest on underpaid VAT

The legislation provides for charging 'default interest' on assessable VAT paid late.

These provisions do not apply to tax properly shown on a VAT return, but paid over late, such late payments being covered by the default surcharge provisions (see 8516ff.) or dealt with as a breach of regulations (see 8510).