News
Tribunal backlog continues to rise

Cases
Notifiable under DOTAS?

One minute with...
Angela Savin
partner, KPMG

# TAX JOURNAL

Insight and analysis for the business tax community
Issue 1435 | 15 March 2019

## Spring Statement

A full report, including:

### Tax highlights
Rhiannon Kinghall Were | Macfarlanes

### Economics view
John Hawksworth | PwC

## Off-payroll working in the private sector: what's proposed?
David Smith | DLA Piper

## Brexit and direct tax: the perspective of the remaining 27
Nicola Saccardo | Maisto e Associati

## 1.5% SDRT and no-deal Brexit
Emily McCarthy & Callum Fowers | Hogan Lovells

## Private client review
Andrew Goldstone & Katie Doyle | Mishcon de Reya

*Plus* CJEU redefines EU law rights | Changes to the QIPs regime | A radical change to trade policy

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# From the editor

The good news, for tax professionals overwhelmed with constant change, is that the chancellor stuck to his word and delivered a Spring Statement that was entirely devoid of any tax shocks. We were always promised this wouldn't be a fiscal event, but there might have been more news about the various tax consultations. Even here, things were quiet: the most eagerly awaited consultation was probably the one on off-payroll working, and that was published last week (see David Smith's review at page 17). On the day itself, only two new tax consultations were published – one on the new structures and buildings allowance, the other on a review of the aggregates levy – and both of these had been expected. There are, though, a further 16 consultations and reviews promised for the coming months – and who knows, we may end up with an emergency Budget should things not go as planned.

Brexit remains all consuming, and I'm afraid there's no relief from that here. Given the shambolic state of affairs, we focus on some tax issues in the event of a no-deal. Nicola Saccardo revisits the direct tax concerns for MNCs, while Emily McCarthy and Callum Fowers explain why the UK's 1.5% SDRT charge is unlikely to be reinstated.

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Printed by The Manson Group, St Albans, Herts AL3 6PZ.
Published by RELX (UK) Limited trading as LexisNexis, 1-3 Strand, London WC2N 5JR and 9-10 St Andrew Square, Edinburgh EH2 2AF.
www.lexisnexis.co.uk

Cover image: NEIL HALL/EPA-EFE/REX/Shutterstock

ISSN 0954 7274

# Contents

## News



## Cases



## In brief



## Insight and analysis

### Spring Statement 2019



### Analysis



### Q&A



### Briefing



## Back page

## Our pick

### Spring Statement 2019

If not quite overshadowed by the international trade department's announcement in the morning of plans for a temporary tariff regime, the chancellor's Spring Statement on 13 March still found itself competing for parliamentary oxygen between a series of momentous 'deal or no deal' Brexit votes. Underlying the upbeat tone of the growth and borrowing forecasts was the constant, low drum-beat warning of a no-deal Brexit.

The chancellor confirmed in his accompanying written statement that the government will not be making MTD mandatory for any new taxes or businesses in 2020. The focus will instead be on supporting businesses through a more gradual transition to digital reporting and record-keeping.

In a lengthy report setting out the government's record on tackling avoidance, evasion and other forms of non-compliance since 2010, the Treasury discharged its obligations under FA 2019 ss 92 and 93 to review the effectiveness and impacts of specific tax avoidance measures contained in that Act.

Other publications on the day included a 2019 update on HMRC's 'no safe havens' strategy for offshore tax compliance, detailed draft amending legislation for the new structures and buildings allowance announced at Budget 2018, and terms of reference for the review of the aggregates levy promised in February.

A further 16 consultations and reviews were earmarked for publication 'in the coming months', together with government responses to six recent consultations, including the digital services tax.

## Business taxes

### Capital allowances

The government has laid orders giving effect to the latest lists of water-efficient and energy-saving technologies qualifying for first-year capital allowances.

- The Capital Allowances (Environmentally Beneficial Plant and Machinery) (Amendment) Order, SI 2019/499, gives effect to the revised Water Technology Criteria List and Water Technology Product List from 29 March 2019. These lists specify water-efficient technologies and products which qualify for 100% first year plant and machinery capital allowances.
- The Capital Allowances (Energy-saving Plant and Machinery) (Amendment) Order, SI 2019/501, gives effect to the revised Energy Technology Criteria List and Energy Technology Product List from 29 March 2019. These lists, maintained by the Department for Business, Energy and Industrial Strategy, specify energy-saving technologies and products which qualify for 100% first year plant and machinery capital allowances.

## Stamp taxes

### Stamp duty & SDRT reliefs after Brexit

The Stamp Duty and Stamp Duty Reserve Tax (Amendment) (EU Exit) Regulations, SI 2019/515, amend references to 'EU' and 'EEA' in existing legislation to ensure that intermediary relief, stock lending relief and the exchange-traded funds exemption from stamp duty and SDRT continue to cover the UK and Gibraltar if the UK leaves the EU without a negotiated deal.

## VAT and indirect taxes

### Temporary tariffs for no-deal Brexit

The government has announced plans to implement a temporary tariff regime in the event that the UK leaves the EU without a deal. The temporary tariff would apply for up to 12 months, during which 87% of total imports to the UK by value would be eligible for tariff-free access. Tariffs would continue to apply to products deemed most sensitive to 'adjustment costs' from international markets, or important for strategic reasons. This would apply to some agricultural sectors, certain ceramics, fertiliser and refinery products, goods given preferential treatment from developing countries, and finished vehicles.

The rules for the tariff regime will be contained in 11 sets of regulations, for which the government has also published a tax information and impact note and several accompanying guidance notes.

The temporary tariff would not apply to Northern Ireland, for which a separate 'unilateral, temporary approach' to checks, processes and tariffs is proposed. This would involve limited new requirements to declare goods from the EU to meet 'essential international obligations', involving such things as dangerous substances, endangered species, rough diamonds, and dual-use or torture goods.

The UK government would continue to collect VAT and excise duty on goods arriving from Ireland. Small businesses below the VAT registration threshold would be able to report VAT online periodically, without new border processes. Irish businesses sending parcels to Northern Ireland would need to register with HMRC to pay import VAT. Northern Ireland businesses currently registered on the EU excise system would register on a UK equivalent system.

### ECOFIN agrees new VAT rules for e-commerce

The EU's Economic and Financial Affairs Council (ECOFIN) has reached agreement on a new directive and regulation forming the second part of the Commission's VAT e-commerce package, which will come into force in January 2021.

The new rules will extend the existing VAT mini one-stop shop (VAT MOSS) into a one-stop shop (OSS) covering all types of services, as well as intra-community distance sales of goods and distance sales of goods imported from non-EU countries by January 2021.

The rules introduce special provisions for online marketplaces, who will be treated as the seller when they facilitate sales of goods with a value up to €150 to customers in the EU by non-EU businesses using their platform. The same rules will apply when non-EU businesses use online platforms to sell goods from 'fulfilment centres' in the EU, irrespective of their value, allowing tax authorities to claim the VAT due on those sales. Online platforms will also be expected to keep records of sales of goods or services made by businesses using the platform.

The regulation specifies when online marketplaces are considered to facilitate such supplies, based on whether or not they are setting the terms and conditions of the supply as well as their involvement in the payment or ordering and delivery of the goods. It also specifies what kind of records are to be kept by platforms facilitating supplies of goods or services to customers in the EU.

Final adoption of the new rules must wait for the EU Parliament to give its consultative opinion, although the Commission says that member states can rely on the rules as adopted by the Council to start preparing their IT systems for the OSS.

Member states will have until the end of 2020 to transpose the new rules of the VAT directive into their national legislation. Businesses wishing to make use of the OSS can start registering in member states from 1 October 2020.

### VAT amendments for EU exit

The government has laid regulations making various changes to four statutory instruments and revoking one order, from a day to be appointed in the event that the UK leaves the EU without a deal.

Changes made by The Value Added Tax (Miscellaneous Amendments, Revocation and Transitional Provisions) (EU Exit) Regulations, SI 2019/513, include:

- ensuring partial-exemption special methods agreed before EU exit in relation to supplies of financial services will continue under the new rules;
- a transitional provision allowing EU VAT refund system claims to be dealt with after exit;
- allowing existing legislation on European Research Infrastructure Consortia to be retained with consequential amendments, meaning that TCTA 2018 Sch 8 para 94(9) and SI 2019/59 art 89 will not now be commenced;
- extending for a two-year period the recipient's joint and several liability for import VAT on certain postal packets;
- a nine-month transitional period for UK fulfilment houses who import goods from the EU to obtain HMRC approval; and
- a power to make provision in a public notice for collection of VAT from certain businesses using transitional simplified procedures.

The VAT (Special Accounting Schemes) (Supplies of Electronic, Telecommunication and Broadcasting Services) Order, SI 2018/1194, which introduced a €10,000 threshold for application of home country VAT rules to supplies of digital services, will no longer be relevant to UK businesses after EU exit and is revoked.

### VAT appeals update

HMRC has published the latest list of recent VAT cases it has lost at the First-tier Tribunal, Upper Tribunal or higher courts, indicating whether or not it intends to appeal. See bit.ly/1IyhEkv.

## International taxes

### EU adds ten jurisdictions to tax havens blacklist

The EU's Economic and Financial Affairs Council (ECOFIN) has revised the EU's list of non-cooperative jurisdictions, adding Aruba, Barbados, Belize, Bermuda, Dominica, Fiji, Marshall Islands, Oman, United Arab Emirates and Vanuatu to the blacklist.

This brings to 15 the number of jurisdictions on the annex I blacklist, the other five being American Samoa, Guam, Samoa, Trinidad and Tobago, and US Virgin Islands.

Barbados, United Arab Emirates and Marshall Islands were on the original 2017 blacklist before being moved to annex II in recognition of commitments made, which they have since failed to follow up.

A further 34 countries remain on the lower-risk annex II, where their progress towards compliance with good governance criteria will be monitored during 2019. These countries are: Albania, Anguilla, Antigua and Barbuda, Armenia, Australia, Bahamas, Bosnia and Herzegovina, Botswana, British Virgin Islands, Cabo Verde, Costa Rica, Curacao, Cayman Islands, Cook Islands, Eswatini, Jordan, Maldives, Mauritius, Morocco, Mongolia, Montenegro, Namibia, North Macedonia, Nauru, Niue, Palau, Saint Kitts and Nevis, Saint Lucia, Serbia, Seychelles, Switzerland, Thailand, Turkey, and Vietnam.

### Netherlands looks to soften tax impact of no-deal Brexit

The Dutch Ministry of Finance issued a draft decree on 8 March on tax measures intended to soften a potential no-deal Brexit.

According to Bart Le Blanc, tax partner in the Amsterdam office of law firm Norton Rose Fulbright, the Netherlands is 'looking to prevent UK companies from losing out on attractive tax benefits and exemptions in the Netherlands, for example, tax consolidation schemes, which only apply to EU residents'.

'This decree deems the UK still to be part of the EU for the current tax year FY 2019 (or at least the current financial year, if different from the calendar year), and will be beneficial for both UK and Dutch businesses that have activities in both jurisdictions. It guards against potential increased tax liabilities for UK companies that could result from the UK assuming third country status on March 29, 2019 in the event of a no-deal Brexit', Le Blanc explained.

This decree will be supplemented later this month with rules relating to VAT on goods in transit to or from the UK around the time of the UK's withdrawal, Le Blanc added.

## Administration & appeals

### Updated PCRT

The leading UK accountancy and tax bodies, AAT, ACCA, ATT, CIOT, ICAS, ICAEW and STEP, have updated the March 2017 version of their professional conduct in relation to taxation (PCRT) guidelines with a revised set of five helpsheets.

Although the fundamental principles and standards have not changed, the new PCRT helpsheets are subject to new criteria for inclusion, 'namely that they should provide guidance that supports the fundamental principles and standards that underpin professional conduct, rather than providing general or specific commentary about developments in the tax system that could best be addressed through other guidance outside PCRT'.

This edition of PCRT is effective from 1 March 2019.

### Avoidance 'spotlights'

HMRC has added spotlight 49 to the list of tax avoidance schemes it is actively investigating. This latest addition warns against further schemes marketed from offshore locations which claim to avoid the disguised remuneration loan charge by promising that loans will be 'paid off' as part of the arrangements.

HMRC reminds that the loan charge legislation disregards non-monetary repayments, as well as any repayments connected to tax avoidance arrangements.

The 'spotlight' article says these schemes may involve one or more of the following features:

- be marketed from an off-shore location such as Cyprus, Malta or Isle of Man, claiming to avoid the 5 April 2019 loan charge legislation;
- claim that entering the scheme means disguised remuneration loans are paid off;
- claim that the scheme is not disclosable under DOTAS, and may have benefited from a QC's opinion; and
- may have professional marketing material, including a website.

### Tribunal backlog continues to increase

The backlog of tax disputes waiting to be heard by the First-tier Tribunal rose to 28,800 in 2017/18, up from 25,520 in the previous year.

According to Pinsent Masons, this is a reflection of HMRC's aggressive approach under its litigation and settlement strategy and an increased number of challenges by taxpayers to the imposition of accelerated payment notices (APNs).

The backlog has now increased for three years in a row and has more than doubled from 13,460 in 2009/10. There is also currently a backlog of 154 cases in the Upper Tribunal.

The number of judicial reviews faced by HMRC increased by 36% last year to 122, up from 90 in 2016. Many of these judicial reviews involve taxpayers appealing against the imposition of APNs, which require a taxpayer to pay the full amount of disputed tax up front before a court or tribunal rules on the dispute. The tribunal does not have jurisdiction to consider whether HMRC was correct to issue the APN but can consider the penalties issued for non-payment of an APN.

HMRC has withdrawn over 6,000 APNs since the power was introduced in 2014, which may indicate that it has been 'overly aggressive' in imposing these penalties, Porter said.

## Our pick

### *HMRC v Hyrax Resourcing and others*
### Notifiable under DOTAS?

In ***HMRC v Hyrax Resourcing and others*** [2019] UKFTT 175 (5 March), the FTT granted HMRC an order that arrangements were notifiable (FA 2004 s 314A).

The case concerned arrangements which, according to HMRC, were 'the current iteration' of a contractor loan scheme previously known as K2/Lighthouse, which had been first implemented in 2014/15.

HMRC had lodged three applications under FA 2004 s 314A for an order that the arrangements were notifiable under DOTAS. It contended that shareholders and/or directors of the three respondents had, since 2004, set up companies to carry out tax planning schemes to enable their 'clients', owner-directors and consultants, to substitute for the remuneration they would otherwise have received, a small salary and a large interest-free loan, which they would not expect to repay in their lifetime.

HMRC argued that, as legislation was coming into force which was perceived as taking away the tax advantage of the previous iteration, a new iteration was introduced which was intended to avoid the new legislation. The FTT accepted that this was what had happened and referred to a webinar for K2, which did mention that the 'life expectancy' of each scheme was about four years due to the risk of it being blocked by new legislation. The tribunal also noted that the various iterations were put forward to potential users as a single but evolving scheme. Finally, the FTT added that the promoters of the scheme facilitated the transfer of end users from one scheme to the next.

However, it would not agree with HMRC's point that, because the previous iterations of the scheme had been notifiable (and had indeed been notified), the new iteration was necessarily notifiable too. The FTT therefore proceeded to review the workings of the scheme in detail. It found, inter alia, that the loans were unlikely to be repaid.

The FTT accepted that Hyrax was 'a "scheme" on any meaning of the word', so that it was an 'arrangement' for the purpose of s 318; and it rejected Hyrax's contention that the legislation required HMRC to establish tax avoidance. In the view of the FTT, Parliament had deliberately not used the expression 'tax avoidance' in the operative part of the provisions, and simply used the term colloquially in the title. The issue was therefore whether the arrangements conferred 'an advantage in relation to any tax' (s 306).

The FTT found that the scheme gave rise to a tax advantage because it was intended to avoid or reduce the charge to tax on salary. In addition, the arrangements fell within three of the hallmarks prescribed by the Tax Avoidance Schemes (Prescribed Descriptions of Arrangements) Regulations, No 2006/1543. Firstly, Hyrax took a cut (amounting to half of the tax saving) on the contract price when sub-contracting services to the end user. This meant that it was able to obtain a premium fee. Secondly, it sold 'standardised tax products'; the scheme documentation was standardised and not tailored to reflect the particular circumstances of end users. Thirdly, under the scheme, employment income was provided by a third party, a trust set up by Hyrax.

Finally, the FTT found that Hyrax was a promoter because it made the notifiable proposal available for implementation by the scheme users and because it agreed to be the counter-party to all the necessary contracts. However, the other two respondents were not promoters as they were not able to implement the scheme. HMRC's application was therefore granted in relation to Hyrax only.

Why it matters: **This lengthy decision considers all the criteria for arrangements to be notifiable; from the features of the arrangements to the hallmarks and the identification of promoters. In particular, the FTT clarified the meaning of 'tax advantage' for this purpose: 'The natural and ordinary meaning of "tax advantage" in s 318 is that it refers to a contrast in tax liability between one position and another that would otherwise have existed.' According to the FTT, the wide breadth of this definition is balanced out by the three conditions in s 306.**

## Business taxes

### When are restrictions on the movement of capital acceptable?

In ***X GmbH v Finanzamt Stuttgart – Körperschaften*** (Case C-135/17) (26 February), the CJEU ruled on the impact of standstill provisions and on the extent to which a presumption of artificiality justifies provisions which restrict the free movement of capital.

X, a German company, held 30% of the shares in Y, a Swiss company. In 2005, Y concluded a 'debt assignment contract' with Z, a German sports rights management company. The debts assigned to Y were owed under contracts under which Z had granted non-repayable subsidies to sports clubs and received 'profit participation rights' in return.

The German tax authorities considered that X had received income from the passive activity of Y, a controlled foreign company (CFC), so that part of the income derived by Y, from the debts purchased from Z, was incorporated into the tax base of X.

Under TFEU art 64(1) (the standstill provision), a member state, in its relations with third countries, may apply restrictions on movements of capital even though they contravene the principle of the free movement of capital of art 63, provided that those restrictions already existed on 31 December 1993.

The first question for the CJEU was therefore whether TFEU art 64(1) allowed the application of a restriction on movements of capital to or from third countries involving direct investment which existed on 31 December 1993, even though the scope of the restriction, in the German legislation, was extended, after that date, to include shareholdings which do not involve direct investment.

The court found that art 64 presupposes not only that the essential substantive content of the relevant restriction has been maintained, but that that restriction has also existed continuously. It therefore found that when a member state repeals or amends legislation in a manner which reintroduces an obstacle to the free movement of capital, it waives the option available to it, under art 64, to continue to apply the restrictions which existed on 31 December 1993.

The CJEU added, however, that if, as suggested, the relevant amendments had never come into force because the provisions had been amended again, then art 64 would apply as the relevant restriction would have been applied continuously.

Finally, the CJEU had to decide whether

the restriction on the free movement of capital could be justified by reasons of public interest. The court noted that the shares held by X in Y had no valid commercial justification, but rather X's primary objective, or one of its primary objectives, was to avoid the tax normally due on the profits generated by activities carried out in Germany by using Y for that purpose. It added that the relevant domestic legislation, which provides that the income of a company established in a third country with a 'low' tax rate is to be incorporated into the tax base of a company with unlimited tax liability in Germany, is aimed at artificial arrangements. However, it considered that the automatic nature of the legislation was comparable, in essence, to an irrebuttable presumption of tax evasion or avoidance, and could not be justified solely on the basis of the criteria established by that legislation.

The court thought that, in such circumstances, the relevant company should be able to produce evidence demonstrating a commercial justification. And where, in circumstances such as these, Y was established in a third country so that the German tax authorities were not in a position to check the information provided by it, the position depended on the existence of a legal framework, such as a treaty, for the exchange of information.

Why it matters: **The CJEU seems to have accepted that a presumption of artificiality, leading to a restriction on the movement of capital, is justified in circumstances where the relevant tax authorities are unable to verify the accuracy of the information provided because the CFC is situated in a third country with which no treaty framework for the exchange of information exists.**

## VAT

### What is art?

In ***Regards Photographiques v Ministre de l'action et des Comptes publics*** (Case C-145/18) (7 March), the advocate general suggested that wedding photographs can benefit from the reduced rate applicable to art.

Under the principal VAT Directive, supplies of artistic objects can be taxed at a reduced rate (arts 103 and 311). This applies to photographs, provided that they are printed by the photographer or under his control, and that they are numbered up to a maximum of 30 prints.

French law provides that only artistic creations can benefit from the reduced rate and specifically excludes photographs of family or religious functions.

Following an inspection, the French tax authorities challenged the application of the reduced rate to wedding photographs taken by Regards Photographiques. The issue was whether the French legislation was consistent with the directive.

The AG first observed that the directive defines an 'artist' by reference to the artistic creations he has generated and not the reverse. The directive therefore only refers to objects created by 'the artist' to differentiate artistic creations from copies or goods produced industrially. Under the directive, any photograph which complies with the conditions is a work of art, regardless of the identity of its author or of the subject matter of the photograph.

The AG observed the importance of the principle of neutrality when applying a reduced rate of VAT. He added that member states are therefore free to limit the application of the reduced rates to certain categories of supplies, as long as the criteria are specific and clear. He considered that the French provisions went a step further by introducing new criteria in the hope of identifying artistic photographs by reference to both the creative intention of the photograph and their artistic appeal. These criteria being necessarily subjective, they introduced an unacceptable level of uncertainty, making French legislation inconsistent with the directive.

Why it matters: **The AG opened his opinion by accepting the difficulties inherent to photography as a medium open to most (even on our phones) and used primarily to record reality. Yet he also noted that the directive did not refer once to artistic criteria and suggested that its purpose was to cover a wide range of creations without assessing their artistic or even intellectual level. Rather reassuringly, the AG thought that tax authorities could not play the role of art critics by applying subjective criteria to decide what is art.**

## Administration & appeals

### Obvious reasonable excuse

In ***K Pokorowski v HMRC*** [2019] UKFTT 86 (8 February), the FTT found that an electrician, who had become homeless, had a reasonable excuse for the late filing of his return and that special circumstances applied.

Mr Pokorowski was a self-employed electrician. Until April 2014, he shared a house in London E17 and was in work. The following facts were not challenged.

In April 2014, he travelled to Poland and his drink in a bar was spiked with drugs. On his return to the UK, he lost his job, he exhausted all of his savings, he was evicted from his house, and all of his belongings were thrown into the street, where they were lost or stolen. He eventually ended up sleeping on the street. Around Christmas 2016, he was told about a homeless shelter, and from January 2017, he was living in hostel accommodation. Later in 2017, he found a job and moved to permanent accommodation in London.

HMRC issued a notice to file a tax return for 2014/15 on 6 April 2015, which was sent to Mr Pokorowski at his London E17 address and Mr Pokorowski filed his 2014/15 tax return on 8 July 2017 on paper. HMRC imposed penalties for late filing. It submitted that the notice to file had been sent to Mr Pokorowski's last known address and that it had been his responsibility to inform HMRC of his change of address. It also considered that there were no 'special circumstances' under FA 2009 Sch 55 para 16 and that Mr Pokorowski did not have a reasonable excuse.

The FTT found: 'HMRC's decision to pursue Mr Pokorowski for penalties in the circumstances of this appeal is a scandal. For HMRC to expect a homeless person to keep HMRC up-to-date with their address is ridiculous – and just needs to be stated to show its absurdity.'

The FTT observed that the facts that Mr Pokorowski had mental health issues, which should have been obvious to HMRC, and the fact that he was homeless, constituted a reasonable excuse. In addition, HMRC's decision that his circumstances were not special was flawed; 'being homeless and having to sleep on the street has to be something out of the ordinary run of events'.

Why it matters: **The fact that this case had to go all the way to the FTT is shocking. Hopefully, this case will be an opportunity for HMRC officers to be reminded of the requirement to be merciful.**

### Case tracker update

New developments include:

- ***HMRC v Greenisland Football Club*** [2018] UKUT 440 (TCC) (VAT: clubhouse similar to a village hall?): HMRC is not appealing this further.
- ***HMRC v Newey (Ocean Finance)*** [2018] EWCA Civ 791 (VAT: advertising services): FTT hearing listed for four days from 28 June to 3 July.
- ***HMRC v Stoke by Nayland Golf and Leisure Ltd*** [2018] UKUT 308 (TCC) (VAT: whether golf club non-profit making body for sporting exemption): HMRC not appealing this further.
- ***HMRC v The Learning Centre (Romford) Ltd*** [2019] UKUT 2 (TCC) (VAT: different treatment of suppliers situated in different devolved areas): Permission granted to appeal to CA.

*See case tracker on taxjournal.com for a guide to the status of leading tax cases.*

Cases reported by Cathya Djanogly (cathya.djanogly@hotmail.com)

## Initial thoughts on the Spring Statement

**We were not expecting much about tax and true to form that is precisely what happened.**

Mr Hammond had other things on his mind, and clearly had to rewrite much of his speech at the last minute after the failure of the Brexit vote last night. Until the Brexit issue is resolved, the chancellor cannot really take a strategic look at the country's long-term financial position and we did get a hint that there could be another statement before the summer break. Perhaps we may get some concrete tax proposals at that stage.

But as ever the small print comes to the rescue. Several tax-related documents were published today and we are promised a number of documents in the next few months. The biggest surprise, which was almost hidden away, is the announcement that 'the government will not be mandating making tax digital for any new taxes or business in 2020'. We had expected that MTD for income tax to start in 2020. I may be reading too much into this, but it does now looks as if there has been a change of heart and HMRC accepts that MTD for income tax Is best introduced on a voluntary basis, at least until the robustness of the system has been thoroughly tested. No doubt we will see more detail of this in the coming weeks and months.

The other notable publication today was the report on tax avoidance. Much of this was simply listing the steps that HMRC has taken in recent years to tackle avoidance, but it also includes a number of reports on the effectiveness of some specific avoidance measures. However, anybody expecting these to reveal huge amounts of detail will be severely disappointed. Most of them simply say: 'It has not been possible to estimate the efficacy of this provision in reducing the tax gap'. This is simply because most of these measures have only just come into effect and there is not yet any real information about how they are working. There is a lesson here for those who are anxious to test the effectiveness of legislation about timing: there is a long time lag between it coming into force and the time when HMRC actually receives tax returns which might reflect that new legislation. The much awaited review of the effectiveness of the loan charge has not yet been published; that is still due to be issued by 30 March.

What about the future? There is a long list of topics where we can expect future consultations. The ones which caught my eye included a review of the effectiveness of the GAAR (the general anti-abuse rule); possible simplification of the VAT capital goods scheme; the principal private residence relief; and the social investment tax relief.

This will not go down as a major event in the history of taxation – but then it was never designed for that purpose. In any event, Brexit has completely overshadowed the speech. Mr Hammond was passionate (not a word I would associate with him) about the need to get an agreement and avoid what he portrayed as the nightmare of a no-deal Brexit. Perhaps I am getting cynical in my old age, but at times I really did think that he was launching his leadership bid! ■

***Andrew Hubbard, editor-in-chief, Tolley***

## CJEU ruling on the Parent-Subsidiary Directive and abuse of law

**Accidentally on purpose? The CJEU redefines the scope of EU law rights.**

On 26 February 2019, the Court of Justice of the European Union (CJEU) handed down its judgment in the cases of *T Danmark* (Case C-116/16) and *Y Denmark* (Case C-117/16) (reported in *Tax Journal*, 8 March 2019).

In short, the CJEU decided that national tax authorities should refuse to apply the EU Parent-Subsidiary Directive (and so should impose domestic withholding taxes) to dividends paid by a company resident in one EU member state to a 10% corporate shareholder in another EU member state in cases where the recipient is a 'conduit company'. This is based on the principle that EU law rights cannot be relied on for abusive or fraudulent ends.

While the judgment pays lip service to previous decisions (such as *Cadbury Schweppes*), which suggest that a tax-motivated reason for a choice of structure will not prevent a taxpayer from exercising an EU law right or freedom except in the relatively limited circumstances where the resulting structure is wholly artificial, the remainder of the judgment seems to represent a move away from this principle. Instead, the judgment places a far greater emphasis than previous decisions on the purpose of the taxpayer in adopting a particular structure in deciding whether the structure is abusive (and so not entitled to the benefit of EU law rights). The effect is that the guiding principle appears to bear many of the hallmarks of a principal purpose test – familiar to readers of the multilateral instrument of BEPS fame.

The case is being widely reported because of its implications for holding company structures within corporate groups and in investment holding structures used by private equity investors. But, if it does represent a move away from the older case law, there may be wider implications. For example, some of the exceptions to UK anti-avoidance rules, which had previously looked rather restrictive when tested against the CJEU case law – such as those which apportion gains of non-UK close companies to UK participators (currently in TCGA 1992 s 13 but soon to be TCGA 1992 s 3 and s 3A) and the transfer of assets abroad rules (in ITA 2007 s 720) – may prove less susceptible to an EU law challenge. ■

***Ashley Greenbank, partner, Macfarlanes***

## Changes to QIPs regime for very large businesses

**A new quarterly instalment payments regime for very large businesses will commence for accounting periods beginning on or after 1 April 2019.**

The Corporation Tax (Instalment Payments) (Amendment) Regulations, SI 2017/1072, were published in November 2017 but the impact will not be felt until this April. Businesses affected by these changes are likely to have been very focused recently on preparations for Brexit and making tax digital and these changes to the quarterly instalment payments (QIPs) regime could easily be overlooked.

In summary, for accounting periods beginning on or after 1 April 2019, very large companies will be required to make payments four months earlier than currently. For a 12-month accounting period, payments will be due in months 3, 6, 9 and 12 of the period to which the liability relates.

Only 'very large companies' are affected by the changes and these are defined in the regulations as companies whose annual taxable profits exceed £20m. This threshold is adjusted if the company is a member of a group or has an accounting period shorter than 12 months. For companies with annual taxable profits of £20m or less, payment dates will not change.

Payments of the bank levy by financial services companies or ring fence corporation tax (CT) by oil and gas companies will be unaffected by these changes. However, all other CT payments, including the bank CT surcharge, will change to the new dates.

The key impact of these changes for companies classed as very large under the new rules will be on cashflow. Not only will QIPs now be payable earlier on a regular basis, but in the first year the new regime will be applicable, the first instalment payment will be due before the final instalment of the previous accounting period subject to the old regime, and only two months after the third instalment. Businesses should make sure they are prepared for the implications this may have on cashflow. In addition, forecasting taxable profits at such an early stage in the accounting period may cause issues for businesses, especially those with fluctuating profits.

Another important issue arises for those businesses that are operating close to the £20m threshold. Where a company's annual taxable profits exceed £20m for the first time it will fall immediately into the new regime for that accounting period, i.e. there is no 'period of grace' allowing commencement from the following accounting period. This means growing businesses approaching the threshold will need to monitor the position carefully. ■

***Wendy Williams & Jay Ayrton, KPMG (KPMG's Tax Matters Digest)***

## Temporary tariff regime for no-deal Brexit

**A radical change to trade policy.**

It's a sign of the times when announcing the biggest change in the way in Britain's trade policy for 45 years doesn't get top billing on the news. But that's what happened this week: without a Brexit agreement, in just over two weeks' time, importers will pay no tariff on 87% of the goods imported into the UK by value.

There are two very significant points to make from the new rules, which run for up to 12 months, while a full review is undertaken.

First, this is a radical change. Brexit Secretary Stephen Barclay this morning billed this as a 'modest liberalisation' but it feels like anything but. Whether the reasoning was a preference for free markets; to soften the blow of 'no deal' to consumers who have been used to tariff-free EU goods; or to spell out for MPs the consequences of no deal, the UK chose not to replicate current EU tariff schedules and instead said it would sweep away tariffs on all but a handful of sectors – most notably some goods produced by the agricultural, automotive, textile and ceramic industries.

The only other major economy to have taken a similar approach in recent years is Singapore and it will be interesting to see what approach the UK takes when it is pursuing free trade deals after Brexit. For some countries there would be little upside in striking one if they already have near-complete tariff-free access to the UK already.

Who are the winners? European exporters who I've spoken to today are relieved frankly. They still face some longer lead times and costs in customs declarations, but they have escaped a tariff hit and would be able to continue largely as before. In the same vein, UK importers who might have been paying a tariff on, say, chemicals products from the US would see that bill reduced to zero.

But for a lot of UK producers the implications are serious. Many would face cheaper foreign competition while suddenly also confronting tariffs to access the EU market for the first time. Even those who retain some tariff protection against cheap imports, like meat producers, are likely to see these markets take a big hit.

The second significant point in today's announcement relates to what happens to goods which do still attract a tariff such as cars or beef and the rules concerning trade across the Irish land border. To avoid imposing a hard border, the plan says these import tariffs will 'not apply to goods crossing from Ireland into Northern Ireland'.

On the face of it, that means a company exporting textiles from Turkey into the UK could now route them via Dublin, across the border to Belfast and from there ship them to England or Wales – tariff free. For companies importing high-value goods and which face a sizeable tariff, it might be worthwhile reconfiguring supply chains, if the rule were to be confirmed.

Advice for UK importers? Analyse the relevant tariff schedules on intermediate and final goods. Importers of Italian shirts face a tariff hike but importers of US-made chemicals could see their customs bill drop. Whether you've been paying tariffs or not historically, the plan evens out treatment of EU and non-EU product. Should you now source from beyond the European Union?

Advice for all producers of physical goods in the UK? Understand what tariff protections you have had against imports up to now and whether that protection remains. ■

***Oliver Sorgniard, KPMG's UK director of indirect tax and customs***

Spring Statement 2019

# Calm amidst the chaos

**Squeezed into the middle of key Brexit votes, the chancellor was undeterred by the chaos, and delivered a calm and collected Spring Statement. Given the pressing work around Brexit, it is no surprise that the breaks have been pulled on tax policy making for now.**

**Rhiannon Kinghall Were**
Macfarlanes
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Under normal circumstances, the Spring Statement is the time for early-stage consultations or calls for evidence ahead of the autumn Budget and not a time to make significant tax or spending announcements unless the economic circumstances require it. This new approach, coupled with the amount of work the government has had to contend with since article 50 was triggered, means the chancellor kept to his policy making commitments.

It was always going to be difficult for this Spring Statement to project a vision for the future, but some may have heard the faint ring of a general election starting gun – talk of a 'brighter future' with policies on housing and the environment were an attempt to appeal to a younger generation.

One of the decisions the chancellor had to make was whether to spend the tax windfall today or to keep it as an insurance policy. Prudently, he has opted for the latter, saving the 'deal dividend' for a rainy (or sunny) day. That might come sooner than expected. An emergency summer Budget is not beyond the realms of possibility if a decision is made on the UK's withdrawal from the EU or there is a general election – both events would require a chancellor to re-evaluate the UK's economic position.

In the meantime, here's a summary of the publications and announcements that caught my eye.

## Tax avoidance and evasion

A few papers were published on avoidance, evasion and non-compliance. The 'no safe havens 2019' strategy sets out new objectives for HMRC to help in its collection of the correct amount of tax. The policy paper *Tackling tax avoidance, evasion and other forms of non-compliance* explained the government's achievement in this space rather than announce any new reforms. Annex A lists over 150 measures taken to tackle tax avoidance, evasion and non-compliance since June 2010 bringing in some £200bn extra tax. Whilst many in the tax profession know HMRC has not been idle in this field, the sheer length of the list is a good reminder of the work undertaken to date and highlights that HMRC's continued efforts are paying dividends.

One of the consequences of this volume of activity is the awareness that businesses have of these measures. The research paper *Evaluation of corporate behaviour change in response to the corporate criminal offences* brings to light some stark findings. Of the 1,000 or so businesses surveyed, only a quarter had heard of the Criminal Finances Act 2017, although larger businesses were more aware (58%) than small businesses (26%). When prompted about what this new measure entails, knowledge amongst respondents did not materially change; only 27% of businesses were aware (again, larger businesses and those in finance and insurance were most likely to report that they knew what the changes meant). This demonstrates the work needed by the government and the profession to ensure taxpayers are able to keep up with the volume of change, and businesses in particular will want to address this knowledge gap before it is too late.

## Taxing the digital economy

As the EU pulled the plug on its digital services tax and the OECD convened most of the international tax fraternity in Paris to discuss taxing the digital economy, the chancellor confirmed that the UK was pressing ahead with the introduction of its new digital services tax. We can expect the responses to the recent UK consultation to be published in the coming months. The wider development here is that the government has identified the need to adapt the regulatory environment as well as the tax system to ensure the digital economy works for everyone in society.

## Capital allowances: non-residential structures and building allowance

Draft legislation was published for this new capital allowance, first announced at Budget 2018. The introduction of this relief has been a longstanding request from business since the abolition of the industrial buildings allowance. An introductory note to the draft legislation explains how some of the elements have evolved since Budget day on issues such as disuse, demolition and leases.

## Making tax digital

The modernisation and digitalisation of the administration of tax begins in earnest next month for VAT. However, the government has said that it will not mandate making tax digital (MTD) for any new taxes or businesses in 2020. Despite these delays, taxpayers should not read this as any dent in the government's ambitions here. MTD is viewed as an important tool in the government's strategy to tackle tax avoidance, evasion and non-compliance.

## Looking ahead

The government has also set out a number of consultations or calls for evidence that we can expect in the coming months. These include a summary of responses from the recent consultation on aligning the consideration rules for stamp duty and SDRT, and the introduction of a market value rule for transfers of unlisted shares between connected parties is due to be published. The conclusions will be interesting for those involved in share transfers, with any changes expected in Finance Bill 2020.

There will also be a review of insurance premium tax. This will focus on the operational aspects to identify ways that the tax can operate more fairly and efficiently. In recent years, the government has used IPT as a 'cash cow' with a series of increases in the rate, so a review into its effectiveness will no doubt be welcome. ■

Spring Statement 2019

# Economics view

**The chancellor promises extra spending if a Brexit deal can be done.**

**John Hawksworth**
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The chancellor's Spring Statement was overshadowed politically by the Brexit votes that sandwiched it, but it struck an upbeat tone on future prospects provided a deal can be done to allow an orderly Brexit.

Much of the focus was on the new Office for Budget Responsibility (OBR) economic and public finance forecasts (see table below). UK growth picked up last summer, but has slowed since then due in particular to the drag on business investment and exports from Brexit-related uncertainty and slower global growth. The OBR revised down its 2019 GDP growth forecast from 1.6% to 1.2% to reflect these recent trends.

Looking further ahead, however, the OBR has not made any material changes to its medium-term growth projections since October. As a result, average UK growth is still expected to be around 1.5% over the next five years, with slightly higher projected growth in 2021/22 offsetting the downward revision for 2019. The OBR still expects UK growth to be below its historical average rate of around 2%, but the outlook is not that bad provided that there is a reasonably orderly Brexit with a transition period.

The OBR has also kept its projections for inflation largely unchanged, still expecting this to remain close to its 2% target rate over the next five years. This will allow real wage growth to remain in positive territory, helping to support consumer spending growth.

The OBR revised down its public borrowing estimate for 2018/19 from around £26bn in October to around £23bn now due to stronger than expected tax revenue growth in recent months.

More importantly, this public borrowing undershoot is expected to persist in future years, with borrowing in 2020/21 and later years now expected to be around £6bn lower than forecast in October. This partly reflects a view that the recent buoyancy of tax revenues will continue, and partly a downward revision in future debt interest costs due to somewhat lower market estimates of future gilt yields.

Relative to the chancellor's target of getting the structural budget deficit below 2% of GDP in 2020/21, the comfort margin has therefore risen from around £15bn last October to around £26bn in these new forecasts, although there is no room for complacency about hitting this target given uncertainty around Brexit.

The OBR also notes that forthcoming changes in the way that student loans are accounted for in the public finances could add around £12bn to the measured deficit in 2020/21. This could wipe out almost half of the chancellor's room for manoeuvre unless he also revises up his deficit target to reflect this accounting change.

Given these factors, and particularly the fog of uncertainty around Brexit, it was not surprising that the chancellor chose to bide his time for now. Only very modest public spending increases were announced in the Spring Statement (amounting to around £2bn in 2023/24, which is less than 0.1% of GDP).

The OBR still expects UK growth to be below its historical average rate of around 2%, but the outlook is not that bad provided that there is a reasonably orderly Brexit with a transition period

However, if an orderly Brexit can be achieved over the next few months, the chancellor signalled that he should be able to afford some additional expenditure in his planned three-year spending review this autumn, in addition to the extra money for the NHS announced last year.

Of course, there is no guarantee at present that the Brexit negotiations will lead to an orderly exit from the EU. Both the OBR and the chancellor warned of the serious downside risks that a disorderly Brexit could pose to the economy and the public finances. We will all have to keep our fingers crossed that this outcome can be avoided. ■

**Comparison of key OBR forecasts in March 2019 and October 2018**

| **Real GDP growth (%)** | **2018** | **2019** | **2020** | **2021** | **2022** | **2023** |
|---|---|---|---|---|---|---|
| Spring Statement (March 2019) | 1.4 | 1.2 | 1.4 | 1.6 | 1.6 | 1.6 |
| Budget (Oct 2018) | 1.3 | 1.6 | 1.4 | 1.4 | 1.5 | 1.6 |
| **CPI inflation (%)** | | | | | | |
| Spring Statement (March 2019) | 2.5 | 2.1 | 1.9 | 2.0 | 2.0 | 2.0 |
| Budget (Oct 2018) | 2.6 | 2.0 | 2.0 | 2.1 | 2.1 | 2.0 |
| **Public sector net borrowing (£bn)*** | **2018/19** | **2019/20** | **2020/21** | **2021/22** | **2022/23** | **2023/24** |
| Spring Statement (March 2019) | 23 | 29 | 21 | 18 | 14 | 14 |
| Budget (Oct 2018) | 26 | 32 | 27 | 24 | 21 | 20 |

*Excluding borrowing of public sector banks.
*Source: OBR*

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Report

# Spring Statement 2019

A report of the tax-related announcements, by Lexis®PSL Tax.

The Chancellor of the Exchequer, Philip Hammond, delivered this year's Spring Statement on Wednesday 13 March 2019. His statement, punctuated with his trademark sense of humour, was heavily overshadowed by the ongoing deliberations regarding Brexit, to which the chancellor alluded. The overall tone was upbeat about economic prospects, provided that the UK is able to negotiate a satisfactory agreement with the EU regarding the terms of its exit. No immediate tax changes were announced, although a number of proposed spending commitments were (notably in relation to infrastructure and accessing the housing market).

Immediately following the statement, the Treasury published two tax-related consultation documents. One of these contained detailed draft legislation for the new capital allowance for non-residential buildings and structures, which was first announced at Budget 2018. The second was a review of the aggregates levy (first introduced in 2002).

The Treasury also published a lengthy report on progress and plans in relation to tackling avoidance, evasion and other forms of non-compliance. A separate batch of policy papers was also released outlining HMRC's strategy for offshore tax compliance. Mandatory digital reporting for VAT takes effect from 1 April 2019 but the government indicated that this will not be extended to any other taxes in 2020. For the first year of implementation, HMRC will also take a 'light touch' approach to penalties for non-compliance with the new digital VAT regime.

A written statement published alongside Spring Statement 2019 confirmed that a number of other documents will be published in the months to come, for instance draft regulations regarding the taxation of offshore receipts in relation to intangible property and various responses to consultations. The government is also calling for evidence about how best to support the UK as a centre for the oil and gas decommissioning industry. Significant changes to the tax system have already been made to facilitate this.

## Draft legislation on structures and buildings allowance

The publications that accompanied Spring Statement 2019 included draft secondary legislation for the new capital allowance for non-residential structures and buildings announced at Budget 2018.

FA 2019 s 30 contains regulation-making powers enabling the Treasury to introduce the new structures and buildings allowance (SBA) for qualifying capital expenditure on new non-residential structures and buildings incurred on or after 29 October 2018. Key aspects of the SBA that remain as set out in the technical note published at Budget 2018 include:

- the SBA will apply at a rate of 2% per annum on a straight-line basis;
- relief will be available for new commercial structures and buildings, including conversions and renovations, but not for the cost of land;
- relief will be available for overseas structures and buildings where the business is within the charge to UK tax;
- claims can only be made when a structure or building first comes into use; and
- if a structure or building is sold, there will not be a balancing adjustment, but the purchaser will take over the remainder of the allowances.

Some aspects of the rules have been amended to reflect discussions with taxpayer representatives. For instance, relief will now be available during any periods in which a structure or building is not in use, and when a structure or building is demolished, any unrelieved expenditure may be claimed as a deduction for capital gains purposes.

The consultation on the draft legislation is open until 24 April 2019. Consultation responses will be published in May 2019, with the final legislation taking the form of a statutory instrument that is expected to be made before the parliamentary summer recess.

## Review of the aggregates levy

The government published a discussion paper on the design of the aggregates levy. The levy is being reviewed because:

- it has not been reviewed since its introduction in 2002;
- the Office for Tax Simplification's review in 2011 highlighted the levy's many exemptions and asked whether the levy could be simplified; and
- the government has committed to devolving the levy to Scotland and intends to devolve it to Wales.

The review seeks feedback on all aspects of the levy including its operation, the suitability of the levy for devolution and the impact of the levy. The review is being conducted through a working group, regional visits and written representations.

The review is open until 5 July 2019 and the government will announce next steps by the end of the year.

### Report on tackling avoidance, evasion and other forms of non-compliance

The government published a report outlining its record on tackling tax avoidance, evasion and other tax non-compliance since 2010. The report highlights, in particular, the government's focus on tackling marketed tax avoidance schemes, VAT fraud on online marketplaces, offshore tax avoidance and evasion, profit diversion by multinational companies, the hidden economy and organised crime. A detailed list of all measures the government has announced since 2010 to crack down on non-compliance is contained in an Annex A. The report also explains HMRC's strategic approach to the risk of non-compliance by customer-type and the rationale behind the 'making tax digital' reforms.

The paper then sets out, at Annex B, specific information on the predicted effectiveness of each of the tax avoidance-related provisions contained in FA 2019, both in terms of reducing avoidance and evasion, and in reducing the so-called tax gap (albeit in most cases it is stated that the relevant data is not yet available). The social and regional impact of those provisions is also noted. This information has been included to fulfil the government's obligations under FA 2019 ss 92–93, which were, unusually, included in that Act pursuant to opposition amendments.

### Policy papers on offshore tax compliance strategy

The government published six policy papers outlining HMRC's strategy for offshore tax compliance. The main objectives of the *No Safe Havens 2019* policy papers are to:

- maximise revenues and bear down on avoidance and evasion
- transform tax and payments for customers, and
- design and deliver a professional, efficient and engaged organisation

To tackle offshore non-compliance, the government intends to focus on three key aims:

- leading internationally: championing international tax transparency and exchange of information. This includes improving international collaboration between tax authorities to ensure the correct amount of UK tax is paid;
- assisting compliance: helping customers get offshore tax right first time. This includes increasing customers' awareness and understanding of their responsibilities and using new data and insights to design systems and processes to help make tax compliance simpler; and
- responding appropriately: taking a proportionate approach to risk and behaviour. This includes helping those who make mistakes, robustly challenging those who avoid or evade tax and applying sanctions to those who help them.

The papers reflect on recent developments aimed at reducing offshore tax non-compliance, including: the common reporting standard, BEPS, the diverted profits tax, corporate criminal offences, enablers of offshore tax evasion, the requirement to correct offshore tax non-compliance and the accelerated payment notices regime.

### Future developments

The chancellor's written statement lists a number of further documents that will be published over the coming months. These include the following.

#### Draft legislation and guidance

- **Offshore receipts in respect of intangible property**: draft regulations to ensure the correct application of the rules introduced in FA 2019 that target multinational groups that hold intangible property in low-tax offshore jurisdictions and use that intangible property to generate revenue from UK customers or provide sales in the UK. The government will also publish draft guidance on the operation of the provisions.
- **Hybrid and other mismatches**: draft regulations updating the definition of exempt regulatory capital instruments within the hybrid mismatch rules.
- **General anti-abuse rule (GAAR)**: draft legislation on minor procedural and technical changes to the GAAR legislation to ensure that it works as intended, together with a technical note.
- **NICs employment allowance**: a technical document inviting comments on draft regulations that restrict the employment allowance to those employers whose employer NICs bill is less than £100,000, as announced at Budget 2018.
- **Enterprise investment scheme (EIS) approved funds guidelines**: draft guidelines on HMRC's proposed policy and practice for approving funds, together with draft legislation containing powers for HMRC to set appropriate conditions and approve funds

#### Summaries of responses

- **Structures and buildings allowance**: a response to the technical note published in October 2018 on the introduction of the SBA.
- **Protecting your taxes in insolvency**: a response to the consultation on the implementation of legislation in Finance Bill 2020 to allow HMRC to be a secondary preferential creditor in company insolvencies for certain tax debts, together with any interest or penalties arising from such debts, with effect from April 2020.
- **Corporate capital loss restriction**: a response to the October 2018 consultation on the new measure announced at Budget 2018 to restrict companies' use of carried-forward capital losses to 50% of their capital gains arising in an accounting period
- **Stamp taxes on shares consideration rules**: a response to a consultation published in November 2018 on extending the market value consideration rule, adopting the SDRT definition of 'money or money's worth' for consideration for stamp duty purposes, and aligning the stamp duty and SDRT treatment of contingent, uncertain and unascertainable consideration.
- **Amendments to tax returns**: a response to the call for evidence on modernising the process whereby taxpayers make amendments to tax returns, published in November 2018. The aim of the consultation is to ensure that the process for amending a tax return is simple and transparent for taxpayers to use and to make the process more consistent across the various taxes. Additionally, tax records will increasingly be held and submitted digitally so this was an opportunity to modernise the process and create a better taxpayer experience in line with HMRC's digital agenda.

- **Digital services tax (DST)**: a response to the consultation published on 7 November 2018 on the design and implementation of the DST. The DST will introduce a 2% charge from April 2020 on the revenues generated by certain digital businesses from UK user participation.

### New consultations

- **Preventing abuse of R&D tax relief for small- or medium-sized enterprises (SMEs)**: a consultation on the application of the anti-avoidance measure announced at Budget 2018 which will introduce a limit on the payable tax credit that a qualifying loss-making company can claim from 1 April 2020.
- **CGT private residence relief**: a consultation on the changes announced at Budget 2018 to lettings relief and the final period exemption, which extend private residence relief in capital gains tax. The aim is to better target the relief at owner occupiers and to reduce the automatic final period exemption for PPR relief from 18 months to nine months, except in specified circumstances.
- **Child trust funds**: as announced at Budget 2018, the government has confirmed that, over the coming months, it will consult on draft regulations to ensure that child trust fund accounts retain their tax-free status after maturity.

### Calls for evidence

- **Insurance premium tax (IPT) operational review**: a call for evidence on improving the operation of IPT.
- **VAT partial exemption and capital goods scheme – simplification**: a call for evidence on simplification and improvement following recommendations from the Office of Tax Simplification.
- **Social investment tax relief (SITR)**: as first announced at Autumn Statement 2016 and confirmed at Budget 2018, the government has confirmed again that it will publish a call for evidence on SITR over the coming months. The government will seek evidence on why the scheme has been used less than anticipated and what impact it has had on access to finance for social enterprises.

In addition to the above, the ministerial statement also included a note on making tax digital (MTD). The statement confirms that MTD for VAT for businesses over the VAT threshold (with turnover over £85,000) will come into force from 1 April 2019. HMRC will apply a light touch approach to penalties in the first year of implementation. Where businesses are doing their best to comply, no filing or record keeping penalties will be issued. The ministerial statement says that the government remains committed to the modernisation of the tax system, but it will focus on supporting businesses to transition 'and the government will therefore not be mandating MTD for any new taxes or businesses in 2020'.

The ministerial statement also confirmed that the government will, by 30 March 2019, publish the report required by FA 2019 s 95 comparing the time limits for the recovery of lost tax involving an offshore matter, with other time limits, including those provided for by F(No.2) A 2017 Schs 11 and 12. In this report, the government will set out the rationale for the charge on disguised remuneration loans legislated in F(No.2)A2017 and its impacts. ■

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Analysis

# Brexit and direct tax: the perspective of the remaining 27

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**Speed read**

**Article 50 is set to expire on 29 March 2019. In the absence of a deal, EU law will cease to apply in relation to the UK, potentially generating significant consequences for the direct tax treatment of cross-border activities between the UK and the member states. The domestic legislation of member states sometimes provides for favourable tax regimes subject to the EU status of the companies involved, and Brexit may impact on their applicability. Brexit might also have significant impact on outbound dividend/interest flows from companies established in EU member states to companies resident in the UK.**

The deadline of the withdrawal of the UK from the EU according to article 50 of the Treaty on the European Union is set to expire on 29 March 2019. In the absence of a deal, after such date, EU law will cease to apply in relation to the UK, potentially generating significant consequences for the direct tax treatment of cross-border activities between the UK and the member states of the EU. This article, finalised on 11 March 2019, is meant to address some of the direct tax consequences that UK businesses may face in other member states because of Brexit.

## Brexit and European direct tax law

From a direct tax perspective, after Brexit the UK will be treated as a third (i.e. non-EU member) state for the purposes of:

- primary EU legislation;
- secondary EU legislation; and
- domestic legislation of EU member states that is subject to EU status.

In terms of primary EU law, the UK withdrawal will imply that the EU fundamental freedoms laid down in the EU Treaty will no longer apply in relation to cross-border economic activities between the UK and the other EU member states, with the exception of the free movement of capital which will still apply as its scope covers also cross-border activities vis-à-vis third (i.e. non-EU member) states.

In terms of secondary EU law, the UK withdrawal will trigger the non-application of the EU Directives, including, in particular, the following direct tax Directives:

- Parent Subsidiary Directive (Council Directive

2011/96/EU of 30 November 2011);
- Interest and Royalty Directive (Directive 2003/49/EC of 3 June 2003);
- Merger Directive (Council Directive 2009/133/EC of 19 October 2009);
- Directive on Administrative Cooperation (DAC) (Council Directive 2011/16/EU of 15 February 2011);
- Anti Tax Avoidance Directive (ATAD) (Council Directive (EU) 2016/1164 of 12 July 2016); and
- Directive on tax dispute resolution mechanisms in the European Union (Council Directive (EU) 2017/1852 of 10 October 2017).

In respect of direct tax Directives, it should be noted that certain provisions concerning the application of EU direct tax Directives are included in the draft withdrawal agreement of the UK from the EU published on 14 November 2018 ('the Draft Agreement'). Particularly, the provisions of Annex 4 of the Draft Agreement lay down a commitment from the UK to continue to apply the provisions of its domestic law that transpose certain Directives such as the ATAD and the DAC. The issue arises as to whether, in the light of this commitment (assuming that the Draft Agreement will be approved by both the UK and the EU), EU member states should treat the UK as an EU member state for the purposes of the application of their domestic legislation that implements the provisions of ATAD and DAC (e.g. when it comes to transfer of residence from an EU member to the UK). In this respect, it should be noted that the provisions of the Draft Agreement lay down a commitment for the UK but not a corresponding obligations for the other EU member states.

### The impact of Brexit on domestic tax regimes subject to the EU status

The domestic legislation of member states sometimes provides for favourable tax regimes subject to the EU status of the companies involved. Such favourable tax regimes were often, but not always, provided to make domestic legislation EU law compliant. For instance, over the past years, member states were often led to amend their tax legislation in order to eliminate discriminations between cross-border and domestic situations that could be considered as in breach of the fundamental freedoms in the light of the judgments issued by the CJEU. It is worth making a few examples of the aforementioned tax regimes subject to the EU status (reference will be made to Italian legislation), in order to understand how Brexit may impact on their applicability.

First, the judgment in *Commission v Italy* (Case C-540/07) concerns discriminatory taxation of outbound dividends (subject to a 27% withholding tax at source) vis-à-vis taxation of dividends distributed to resident companies (subject to 27.5% income tax at the level of the recipient on a taxable amount of 5% of the gross dividends). As a result, Italy introduced a new withholding tax rate of 1.375% for outbound dividends (not benefiting from the Parent Subsidiary directive) paid to companies liable to income tax in other EU or EEA member states. (Indeed, 1.375% is equal to 27.5% times 5%. This withholding tax rate has been further reduced to 1.2% in response to the reduction of the corporate income tax rate from 27.5% to 24%.)

After Brexit, such a favourable domestic tax regime will no longer be applicable to UK companies. In this example, the application of the favourable 1.2% tax regime should be preserved due to the application of the free movement of capital; however, depending also on the complexities of the EU law argument, relying on the free movement of capital may imply the risk of litigation with the local tax authorities.

A second example concerns horizontal tax group regimes. After the judgment in the case *SCA Group Holding* (Case C-39/13 to Case C-41/13), several member states amended their tax group regimes allowing resident subsidiaries whose shares are held directly by the same non-resident parent company to form a fiscal unity. Such amendments were made in order to avoid further infringements of the freedom of establishment, after the CJEU had stated that the group tax regime of a member state that does not allow two subsidiary companies held by a parent company in another member state to form a fiscal unity between them is in breach of the freedom of establishment to the extent that such parent company would have been able to form a fiscal unity with its subsidiaries had it been a tax resident of such member state.

Horizontal tax group regimes introduced by member states are often conditional on the EU status of the holding company. Therefore, after Brexit, sister companies held by the same UK parent may not be able to form a horizontal tax group. Moreover, Brexit may have an impact on horizontal tax groups already in place at the time of the withdrawal of the UK from the EU. Indeed, the fiscal unity might be discontinued because, after the withdrawal, the UK company will not qualify any more as company resident of an EU member state.

In order to avoid this adverse consequence, groups headed by a UK parent might consider reviewing their holding structure through the set up of a holding company resident in a European member state before Brexit. In this second example, following Brexit, the taxpayer cannot rely on the free movement of capital since the relevant freedom is the one of establishment.

Third, favourable tax regimes subject to the EU status may be provided for a purpose other than to make domestic legislation EU law compliant. For instance, Italian law provides for an exemption for outbound interest paid to EU banks in relation to medium-long term loans granted to Italian businesses. The goal of the legislation is to ease the access of Italian businesses to debt. Such a favourable tax regime will cease to apply after Brexit (a separate issue, outside the scope of this article, is whether other exemption regimes for outbound interest may remain available), and it cannot be extended by the operation of the free movement of capital since it does not imply any discriminatory treatment.

### The impact of Brexit on pre-Brexit transactions

Brexit may impact also pre-Brexit transactions. Indeed, business transactions or group reorganisations carried out before Brexit might have benefited from regimes that were subject to EU status. Brexit might impact on such transactions and might determine adverse consequences.

An example concerns exit taxation. After the judgment in *National Grid Indus* (Case C-371/10) and other judgments of the CJEU on the compatibility with the freedom of establishment of exit taxation regimes, several member states granted to companies that transferred their tax residence to other member states, and lost their tax residence in their member state of origin, the option to defer the payment of the exit tax due upon transfer. Usually, the deferral is discontinued if the company transfers from its member state of destination to a non-EU member state. Brexit might have adverse consequences for companies that transferred their tax residence to the UK and deferred the payment of the exit tax in their member state of origin. Indeed, the loss of their EU status because of Brexit might be deemed to be equivalent to a transfer of residence to a third country and, therefore, might trigger the obligation to pay immediately the outstanding amount of the exit tax.

### The impact of Brexit on cross-border dividend/interest payments in the light of the recent Danish cases

Brexit might have significant impact on outbound dividend/interest flows from companies established in EU member states to companies resident in the UK. Indeed, dividend/interest payments made by companies tax resident of another member state might be exposed to withholding tax at source without the possibility to benefit from the exemption granted by the Parent Subsidiary Directive, the Interest and Royalty Directive or by other domestic regimes of member states that reduce or eliminate taxation at source subject to the EU status of the recipient.

> Brexit might have significant impact on outbound dividend/interest flows from companies established in EU member states to companies resident in the UK

UK companies receiving dividends/interest from their EU subsidiaries should, therefore, check the provisions of the applicable double tax conventions, or the applicability of other domestic tax regimes in the respective member states of residence of the subsidiaries, in order to understand whether Brexit might trigger an increase of the tax burden on dividends/interest received from EU subsidiaries.

In order to mitigate the adverse consequences of Brexit, multinational groups might wish to review their corporate structure by creating an EU sub-holding company located in an EU member state. The use of an EU sub-holding should take into consideration the recent judgments rendered by the CJEU on 26 February 2019 in joined cases *N Luxembourg 1* (Case C-115/16), *X Demark* (Case C-118/16), *C Danmark I* (Case C-119/16) and *Z Denmark* (Case C-299/16) on the Interest and Royalty Directive ('*IRD* cases'); and in joined cases *T Danmark* (Case C-116/16) and *Y Denmark* (Case C-117/16) on the Parent Subsidiary Directive ('*PSD* cases'). Particularly, in such cases, the Grand Chamber of the CJEU laid down landmark guidance on beneficial ownership and abuse for the purpose of the aforementioned Directives.

As far as beneficial ownership is concerned, in the *IRD* cases the CJEU held that, for the purpose of the Interest and Royalty Directive, the notion of beneficial owner must be construed in the light of the Commentary on the OECD Model and its amendments. It is not entirely clear from the text of the judgment whether the 2014 changes to the Commentary should be relevant. The doubt arises from the fact that such changes took place after the introduction of the Interest and Royalties Directive and from the fact that, at one point, the CJEU seems to refer only to the changes of the Commentary on the beneficial ownership concept until 2003, but not to the 2014 changes (see para 92, which refers to OECD developments described under paras 4–6, but not to para 7). The CJEU further holds that, if the recipient of the interest is not the beneficial owner but the beneficial owner qualifies for the Interest and Royalties Directive, the benefits of the Directive are still applicable.

In the *PSD* cases, the CJEU (see para 111) seems to hold the view that the benefits of the Parent Subsidiary Directive are subject to the fulfillment of the beneficial ownership condition, despite the lack of any beneficial ownership clause in the text of such Directive.

As far as abuse is concerned, the CJEU held that member states have an obligation to deny the benefits of EU legislation in case of abuse (irrespective of the existence of domestic or treaty-based anti-abuse provisions). The CJEU also stated that abuse requires both that the purpose of the legislation is not achieved (objective element) and that obtaining the tax advantage is the main purpose or one of the main purposes of the taxpayer (subjective element). Finally, the CJEU ruled that the existence of an abuse shall be determined on the basis of a factual analysis and that the following indicia may be taken into account:

- All or almost all of the dividends/interest is very soon passed on to an entity that does not meet the requirements for the application of the Directive.
- The recipient of the dividends/interest makes an insignificant taxable profit (by passing on the income).
- The recipient of the dividends/interest lacks economic substance because it carries out limited activities. The court further states that:
  - the economic substance must be tested 'in the light of the specific features of the economic activity in question'; and
  - the economic substance must be tested in the light of, among the others, the management of the company, the balance sheet, the structure of costs, the expenditures incurred, the staff employed, the premises and the equipment.
- The recipient of the dividends/interest does not have the right to use and enjoy such income. This may be the case since either the recipient is under a legal obligation to pass the income on to another entity, or *de facto* does not have the right to use and enjoy it due to, for example, the way in which the transactions are financed and the limited equity of the recipient.
- The group structures were put in place simultaneously or shortly after the introduction of changes in law that would have created additional tax burdens if the group had not changed its structure.

The above cases highlight how the concept of abuse under EU law continues to evolve and they will have a significant impact on most international group structures and the flow of funds from EU subsidiaries to EU parent company controlled by non-EU entities. ■

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- A Brexit tax checklist: are you ready for 'no deal'? (Ashley Greenbank & Charishma Juddoo, 7.2.19)
- The long arm of Brexit (Penny Van den Brande & Ashley Greenbank, 2.8.17)

Analysis

# 1.5% SDRT and no-deal Brexit


Speed read

**The UK's 1.5% SDRT charge on an issue of shares to a clearance service or depositary receipt system is not currently being collected because it was found to be contrary to EU law. The government has said it will not reinstate this charge after the UK leaves the EU. Further comfort can be taken from the legal position: an analysis of the *Vidacos* and *BNY* cases, EU law and the European Union (Withdrawal) Act 2018 suggests that, in the event of a no-deal Brexit, the charge will still not apply.**



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Buried in Autumn Budget 2017 was the following statement: 'The government will not reintroduce the ... Stamp Duty Reserve Tax 1.5% charge on the issue of shares ... into overseas clearance services and depositary receipt systems following the UK's exit from the EU' (*Budget Report*, para 3.39). The charge is not currently collected because it was found to be contrary to EU law in two cases involving HSBC Holdings: *HSBC Holdings Plc and Vidacos Nominees Ltd v HMRC* (Case C-569/07) before the CJEU (*Vidacos*); and *HSBC Holdings Plc and The Bank of New York Mellon Corporation v HMRC* [2012] UKFTT 163 before the First-tier Tribunal (*BNY*).

Comforting as the Budget statement is, the charging provisions remain on the statute books. This raises the question of what the legal basis is for concluding that such charges will not apply in the event of a no-deal Brexit.

With just a couple of weeks to go until 'exit day' (currently scheduled for 11pm on 29 March 2019), it is reasonably clear that no specific legislation to address this will be passed, and we would not expect this to change even if exit day is delayed. If a deal with an implementation or transition period is agreed, these concerns are merely likely to be delayed until the end of that period. The answer requires close scrutiny of *Vidacos* and *BNY*, the EU law on which they rely and the European Union (Withdrawal) Act (EUWA) 2018.

This analysis of EUWA 2018 has broader application. In particular, it will be relevant whenever taxpayers rely upon directly effective provisions of EU directives following Brexit.

## *Vidacos*, *BNY* and the direct effect of the Directive

At a high level, *Vidacos* and *BNY* together established that a charge to SDRT (under FA 1986 ss 93 or 96) on the issue of shares to a clearance service or depositary receipt system anywhere in the world is prohibited by articles 10 and 11 of Council Directive 69/335/EEC (the Predecessor Directive). These provisions correspond to what are now articles 5(1) and 5(2) of Council Directive 2008/7/EC (the Directive).

EU directives such as the Directive are not directly applicable: they require implementation into domestic law. However, they can have direct effect if a number of conditions are satisfied (*Van Duyn v Home Office* (Case C-41/74)). In the UK, this direct effect is pursuant to the European Communities Act (ECA) 1972 s 2(1). In general terms, the restrictions prohibiting the UK from levying SDRT in the circumstances contained in articles 5(1) and 5(2) of the Directive are (prior to exit day) directly effective. HMRC implicitly accepts this, as shown by a statement issued following the decision in *BNY* and guidance in its *Stamp Taxes on Shares Manual* (see, for example, STSM053010).

## The impact of EUWA 2018

EUWA 2018 s 1 repeals the ECA 1972 on exit day. The supremacy of EU law, and any direct effect of the Directive, in the UK will therefore end save to the extent preserved by statute. EUWA 2018 s 4(1) is the relevant preserving provision. It has the effect that rights and restrictions under EU directives that were directly effective immediately before exit day continue to be recognised and enforced in UK domestic law after exit day.

### Recognition of the relevant restriction: the 'of a kind' requirement

This is not the end of the story, however. Section 4(1) is subject to s 4(2), which provides that s 4(1) does not preserve any rights or restrictions arising under an EU directive that are not 'of a kind' recognised by the CJEU or any UK court or tribunal in a case decided before exit day. It is therefore not sufficient for a right or restriction to arise under a directly effective provision of an EU directive. It must also be recognised by the CJEU or by a UK court or tribunal before exit day, or it must be 'of a kind' so recognised.

### Recognition of articles 5(1) and 5(2)

With this in mind, we turn to look for recognition of articles 5(1) and 5(2) of the Directive in existing case law. This may seem relatively straightforward. The restrictions arising under article 10 of the Predecessor Directive (now article 5(1) of the Directive) were expressly recognised by the FTT as having direct effect in *BNY*. (The restrictions under article 5(1) itself were also recognised by the CJEU in *Air Berlin Plc v HMRC* (Case C-573/16), although the CJEU did not expressly state that the article had direct effect.) The restrictions arising under article 11 of the Predecessor Directive (now article 5(2) of the Directive) were also expressly recognised as having direct effect in *BNY*. (These restrictions were also recognised by the CJEU in *Vidacos*, as were the restrictions arising under article 5(2) itself in *Isabelle Gielen v Ministerraad* (Case C-299/13), although again in neither case did the CJEU expressly state that the article had direct effect.)

### Interpreting the 'of a kind' requirement

Is this sufficient for all aspects of the directly effective restrictions found in articles 5(1) and 5(2) to survive the test in EUWA 2018 s 4(2)? In our view, it should be. It is hard to say they have not themselves been, and are not 'of a kind', recognised by the CJEU or a UK court of tribunal before exit day.

But there could be a counter argument. Articles 5(1) and 5(2) together in fact contain various sub-clauses. The following are particularly relevant to the issue of shares:

- article 5(1)(a): relevant in respect of contributions of capital (defined in article 3);
- article 5(1)(e): relevant in respect of restructuring operations (see article 4); and
- article 5(2)(a): prohibits member states from subjecting to any form of indirect tax the creation, issue, admission to quotation on a stock exchange, making available on the market, or dealing in stocks, shares or other securities of the same type.

Depending upon the interpretation of EUWA 2018 s 4, and 'of a kind' in particular, it may be suggested that it is not just articles 5(1) and 5(2) in general but the individual restrictions contained in those articles that need to have been or be 'of a kind' recognised prior to exit day.

How widely this provision will be interpreted remains to be seen. It would be difficult to overstate the significance of the EUWA 2018 within the UK's legal system following Brexit. There is every likelihood that it will one day come before the courts to be interpreted (probably in a context wholly unrelated to SDRT, with the inevitable uncertainty of such a decision). However, even if 'of a kind' is interpreted sufficiently narrowly that the provisions of article 5 must be assessed at a granular level, we nevertheless consider that some, if not all, of those restrictions have been, or are 'of a kind', recognised.

### Article 5(1)(a)

*BNY* concerned the predecessor of article 5(1)(a) of the Directive and, as noted above, the FTT recognised that it had direct effect. The case involved a contribution of capital in the form of 'an increase in the capital of a capital company by contribution of assets of any kind' (see article 3(c)). We consider that the nature of the restriction recognised cannot be limited to the facts of the particular case. For example, it cannot solely be a restriction on imposing SDRT under FA 1986 s 93 (as opposed to FA 1986 s 96). And surely it cannot just be a restriction on an increase in capital by the contribution of the non-cash assets (the subject of *BNY*), as opposed to cash assets. We note that, in *Energie Steiermark Holding AG v Finanzlandesdirektion für Steiermark* (Case C-339/99), the CJEU recognised that an increase in the capital of a capital company by contribution of assets of any kind included a contribution of cash.

### Article 5(2)(a)

*Vidacos* and *BNY* each considered the predecessor of article 5(2)(a). In *Vidacos*, the CJEU recognised that it prohibited the levying of an SDRT charge under FA 1986 s 96 on the issue of shares into a clearance service. Further, in *BNY*, the FTT held that it prohibited the levying of an SDRT charge under FA 1986 s 93 on the deposit of shares with a depositary receipt system. On this basis, no 1.5% SDRT charge should ever arise on an issue of shares to a clearance service or depositary receipt system following a no-deal Brexit. However, despite HMRC's statement following *BNY* (referred to above), we understand that HMRC does not accept that to be the case in all circumstances, even before Brexit.

### Article 5(1)(e)

An issue of shares as consideration for the acquisition of a target company is potentially more complicated. Such a transaction can be a restructuring operation within article 4(1)(b) of the Directive, with article 5(1)(e) in play. Under the Directive, restructuring operations are expressly not contributions of capital, so article 5(1)(a) will not apply.

The Predecessor Directive did not make this distinction. As a result, *Vidacos* (decided under the Predecessor Directive) did not consider article 5(1)(e) or an equivalent provision. However, taking a step back, under both the Predecessor Directive and the Directive there is a prohibition on charging SDRT in circumstances that, factually, are restructuring operations within article 4, as shown by *Vidacos*.

*Vidacos* involved the acquisition by HSBC of all the issued shares of a French public company, where a share exchange was included as part of the offer to the target's shareholders. While we are only aware of the facts set out in the CJEU's judgment, we consider it very likely that the same circumstances would now amount to a restructuring operation under article 4(1)(b).

It seems reasonably clear that the 1.5% SDRT charges on issues of shares … will not automatically be 'reinstated' in the event of a no-deal Brexit

In *Vidacos*, the CJEU recognised that levying SDRT on the issue of the HSBC shares as part of the acquisition was prohibited by article 11(a) of the Predecessor Directive. The CJEU therefore recognised, in circumstances akin to restructuring operations today within article 4(1)(b) of the Directive, that restrictions arose under the Predecessor Directive article 11(a) prohibiting a charge to SDRT on an issue of shares into a clearance service. This must, surely, be enough for the s 4(2) test not to be failed in respect of a similar restructuring operation.

Further, in most cases, an issue of consideration shares in this way would also fall within article 5(2)(a) in any case.

### Other types of share issue

Other share issues which are neither for cash nor in consideration of the acquisition of a target company will need to be considered on a case by case basis to assess whether the direct effect of a restriction imposed by the Directive relevant to them has been recognised by the CJEU prior to exit day or is 'of a kind' so recognised. It remains to be seen how widely restrictions recognised in pre-exit day case law can be drawn and how widely 'of a kind' can be interpreted. However, these are issues that will need to be determined in practice in the event of a no-deal Brexit.

## Conclusion

It seems reasonably clear that the 1.5% SDRT charges on issues of shares to clearance services and depositary receipt systems will not automatically be 'reinstated' in the event of a no-deal Brexit, at least in the above examples. Alongside the government's statement in Autumn Budget 2017 that it will not reintroduce such charges post-Brexit, this gives issuers and their advisers significant comfort. However, the legal analysis required to reach this conclusion (and, potentially, to convince HMRC in practice) is rather more involved than might be expected and raises a fundamental question about the breadth of the 'of a kind' requirement in EUWA 2018 s 4(2). ■

*The authors thank Adam Parry (Hogan Lovells) for his contribution to this article.*

Q&A

# Off-payroll working in the private sector: further consultation

**Speed read**

**HMRC has published a further policy paper and consultation document setting out details of the proposed reforms to the private sector off-payroll working rules due to take effect from April 2020. This confirms that the reforms will use the off-payroll working rules in the public sector as a starting point but with a number of significant changes. These include enhanced information transfer obligations, the introduction of a client led dispute resolution process and the ability for HMRC to transfer liability for unpaid income tax and NICs to different parties in the labour supply chain.**

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Following a consultation exercise carried out during summer 2018, the government announced at Budget 2018 that, with effect from 6 April 2020, changes would be made to the existing private sector off-payroll working rules (commonly known as IR35) in order to increase compliance and to bring the private sector into line with the public sector which, since April 2017, has been subject to a separate off-payroll regime.

On 5 March 2018, HMRC issued a further policy paper and consultation document aimed at providing private sector engagers and individual workers (together with other parties involved in the labour supply chain) with more certainty regarding how the IR35 rules will work from April 2020 along with details of their respective obligations and responsibilities under the new regime. (For the consultation paper, see bit.ly/2EMgrvj.)

## What is IR35 and what is changing?

The current IR35 regime applies where an individual provides their services through an intermediary (most commonly the individual's personal service company (or PSC)) to another person or entity (the client) in circumstances where, had the individual provided their services directly to the client rather than via their PSC, they would have been an employee (or office-holder) of the client.

This basic premise is not changing. What is changing is where the responsibility for determining whether the regime applies, and then subsequently applying it, sits, which the consultation has confirmed will, as a starting point, be based on the off-payroll working rules which apply in the public sector.

As a result, this will mean that, instead of the individual's PSC (as is currently the case):

- clients will be required to make a determination of an individual's employment status under the regime; and
- the 'fee-payer' (usually the organisation paying the individual's PSC) will be required to include the individual on their payroll and, broadly speaking, account for income tax and national insurance contributions (including employer national insurance contributions) on the payments made to the individual's PSC.

## What further details does the consultation provide?

The government has acknowledged that there are a number of areas in which the public sector regime could be improved and has set out various proposals in the consultation document aimed at trying to address at least some of them (and which, if adopted, would then apply to both the new private sector and existing public sector regimes).

### Provision of information

Under the public sector regime clients are required to provide a status determination to the party they contract with at the start of the contract and to also provide their reasons for that determination within 31 days of receipt of a written request from that party.

In more complicated supply chains the party the client contracts with is, however, unlikely to be the fee-payer (with the obligation to include the individual on their payroll). In addition, there is no obligation to provide a copy of the determination to the off-payroll worker.

To ensure all parties in the labour supply chain have sufficient information to allow them to comply with their obligations the government therefore intends to include a statutory obligation requiring each party in the supply chain to cascade the client's determination, together with the reasons for that determination, to the next party in the chain. In addition, the client will also be required to directly provide the off-payroll worker with their determination and, on request, the reasons for that determination.

What is not clear from the consultation is whether fee-payers who do not contract directly with the client will also have the ability to request the reasons for a determination under this process and, if they can, how the timing and logistics of this would work, particularly in more complicated supply chains. Whilst the consultation does propose an alternative, simplified, approach under which the fee-payer receives the determination (and, where requested, accompanying reasons) direct from the client, this too gives rise to potential logistical issues.

Unhelpfully, the consultation also does not address the potentially unnecessary burden imposed on clients to make a status determination where ultimately the regime does not apply, for example, where they contract with an agency which in turn contracts with the individual worker as an employee or via an umbrella company or where the agency legislation at ITEPA 2003 Part 2 Chapter 7 applies to the engagement. As the obligation to operate PAYE transfers to the client if they fail to pass on a status determination, or if they fail to take reasonable care in arriving at that determination, they are likely to take a cautious approach to all of their off-payroll labour arrangements, resulting in additional administration and potentially wider implications for the flexible labour market.

### Non-compliance

To encourage compliance with the above extended information requirements the proposed legislation will also provide that, where HMRC does not receive any tax due, liability will initially rest with the party that has failed to fulfil its obligations until such time that they are met. So, for example, if an agency failed to send on a status determination to a fee-payer it, rather than the fee-payer, would be liable for any income tax and national insurance contributions due until such time that it passed on the determination.

More significantly, if HMRC is unable to collect the outstanding liability from that party, for whatever reason, it is proposed that the liability would then transfer back to the first party or agency in the chain (by-passing any intermediate parties in the chain) and if recovery was still not obtained, liability would then transfer back to the client.

HMRC's justification for this approach is to provide a clear incentive for all parties to comply with their respective obligations and to encourage parties to contract with reputable and compliant firms.

### Resolving status disputes

To ensure clients give due consideration to the facts of a particular engagement and to alleviate potential concerns around the making of blanket status determinations it is also proposed that clients will be required to put in place a process for resolving disagreements relating to status determinations.

The ultimate design and operation of this would be for each client to determine, to fit in with their wider business processes but, as a minimum, would require the client to give consideration to any evidence put forward by an individual worker and/or fee-payer and to advise that party of the outcome of that consideration and the reasons for it.

## Will the proposed reforms apply to the whole of the private sector?

No, the proposed changes will not apply to small organisations.

Whether or not a client is small will be determined, for corporate clients, in line with the definition contained at s 382 of the Companies Act 2006. This requires satisfaction of two or more of the following requirements in a financial year:

- annual turnover of not more than £10.2m;
- balance sheet total of not more than £5.1m;
- no more than 50 employees (taken as an average over the year).

If a corporate client does not qualify as small under this test, or under the test for small groups in the Companies Act 2006 s 383 (or is excluded from qualifying despite meeting the requirements under either test as a result of the application of the Companies Act 2006 s 384) it will be subject to the new IR35 regime.

For non-corporate clients, two alternative tests have been proposed, both of which exclude the balance sheet requirement. Under the first option the client would not be considered small (and therefore would be subject to the new IR35 regime) if it had 50 or more employees, or if it had turnover in excess of £10.2m. Under the second option it would not be considered small if it had both 50 or more employees and turnover in excess of £10.2m. Whilst removal of the balance sheet requirement is understandable, as it may not be suitable for all non-corporate clients, it is not clear why a different employee requirement is being proposed than applies for corporate clients under the Companies Act tests.

When an organisation ceases to be (or becomes) small for an accounting period, the new regime will apply (or cease to apply, as the case may be) from the start of the tax year following the end of that accounting period.

If a client is small the existing IR35 regime will continue apply to the engagement, with the individual's PSC retaining responsibility for determining whether the regime applies and, if it does, subsequently applying it.

## What support will be provided by HMRC?

HMRC launched the 'check employment status for tax' (CEST) service in 2017 to help clients determine the status of their off-payroll workers. Responding to concerns raised regarding the CEST's ability to provide accurate status determinations HMRC is currently working with stakeholders to enhance the service and to improve its accompanying guidance.

In addition, HMRC is developing an education and support package intended to provide each party in the labour supply chain with the information and guidance they require to apply the off-payroll working rules. It is intended that this will be made available to affected parties, so they can 'act on the changes in time for April 2020'.

## What next?

The consultation closes on 28 May 2019 with draft legislation expected in Summer 2019.

Given the potentially significant impact of these reforms it is important that organisations take advantage of the time available prior to 6 April 2020 to fully prepare for their introduction.

As a starting point this will include the identification and review of existing off-payroll engagements to determine which are likely to fall within the scope of the reforms. This in turn will allow consideration of the potential financial implications (such as additional employer national insurance and apprenticeship levy liabilities).

A review of contractual terms will also be required to ensure responsibility for potential liabilities is addressed and appropriate protections are included. Where relevant wider reviews of labour supply chains may also be required, particularly where there is the possibility for unpaid liabilities to be transferred back down the supply chain.

Internal systems and processes will also need to be reviewed to ensure they are set up and ready to deal with the reforms. This could include procurement and on-boarding policies, payroll (including payroll software) and HR. In particular, appropriate systems will need to be in place to ensure that status is considered and decisions made on a consistent basis, relevant information is cascaded and acted on within appropriate time frames and processes are in place for dealing with potential disputes. ■

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- News: Off-payroll working rules in the private sector (6.3.19)
- Off-payroll working: lessons from the BBC's experience (Chris Thomas & Catherine Robins, 11.1.19)
- Off-payroll working in the private sector (Ian Hyde & Chris Thomas, 31.5.18)

Briefing

# Private client review for March

## Speed read

In *Smith v Stanley*, the court considers whether it has jurisdiction to set aside the trustees' deed terminating a life interest made in reliance upon incorrect tax advice. In *Negka v HMRC*, the FTT confirms that if information has been voluntarily disclosed to HMRC by the taxpayer in another context it will be difficult for HMRC to show careless omission by the taxpayer as the basis for a discovery assessment against them. A consultation opens on the proposed 1% SDLT surcharge for non-residents. In *P N Bewley Ltd v HMRC*, the FTT considers the definitions of 'dwelling' and 'residential' for the purposes of establishing the applicable SDLT rate.

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### *Smith v Stanley*: whether to set aside trustees' action based on incorrect tax advice

In *Smith v Stanley* [2019] 2 WLUK 174, the testator's will created a life interest trust for the benefit of the widow with a discretionary trust in remainder. The trustees made the decision to enter into a deed of appointment bringing the life interest to an end and creating a discretionary trust over the funds in favour of the existing discretionary beneficiaries.

The termination of a life interest following which a relevant property trust continues is a chargeable lifetime transfer. As a result of signing the deed the trustees incurred an unexpected 20% inheritance tax liability on the value of the appointed funds. The trustees had signed the deed under the misapprehension that the deed of appointment would be treated as a potentially exempt transfer and, as such, there would be no immediate tax charge. This misapprehension was the result of incorrect professional advice. The trustees applied to the court to set aside the deed of appointment.

The court drew a distinction between a decision made with the object of avoiding tax (which would most likely not be set aside) and a decision informed by incorrect advice that resulted in an unforeseen tax charge. There was no intention to avoid tax specifically, the trustees' objective was to terminate the widow's life interest, but they would not have done so had they thought an immediate tax charge would arise. Thus, although the court confirmed that the deed of appointment terminating the widow's life interest was valid and effective, it was set aside for mistake. In reaching their decision, the court considered which course of action would be in the best interests of the beneficiaries, concluding that to allow the deed and the resulting tax charge to stand would deplete the trust fund to the detriment of the trust beneficiaries.

#### Why it matters

This case, which cites *Pitt v Holt* [2013] UKSC 26 and the more recent cases of *Van der Merwe v Goldman* [2016] EWHC 790 (Ch) and *English v Keats* [2018] EWHC 673 (Ch), is the latest in a string of decisions in recent years on the jurisdiction of the court to set aside the actions of trustees. The case reiterates that the court will not set aside decisions that are made with the aim of avoiding tax. If, however, trustees rely on professional advice that there is no tax to pay and take this advice into account when making a decision with a different objective, the court may have jurisdiction to set aside the trustees' action depending on the circumstances of the case.

### *Negka*: reasonable care

In *Negka v HMRC* [2019] UKFTT 82 (TC), the taxpayer claimed a relief for maintenance expenditure on a property that she intended to rent out commercially as part of her rental business. HMRC made a discovery assessment when they determined that the expenditure was not 'wholly and exclusively' for the rental business as the taxpayer had in fact been living in the property during the relevant period. Although the taxpayer subsequently conceded that she was not eligible for the relief, to issue an assessment under TMA 1970 s 29 and charge penalties for the resulting unpaid tax, HMRC had to show that the taxpayer's actions which resulted in underpayment were either deliberate or as a result of carelessness. HMRC submitted that the taxpayer had brought about the situation carelessly because she failed 'to take reasonable care to avoid bringing about that loss or situation', i.e. she had been careless in failing to disclose her living arrangements when she asked HMRC for guidance about claiming the rental expenses. It was made apparent to the tribunal, however, that the taxpayer had in fact previously disclosed to HMRC that she was living in that property at the relevant time but as part of a discussion about establishing that the property was her principal private residence for the purpose of principal private residence relief (PPR).

The tribunal considered that 'the test to be applied is what a reasonable hypothetical taxpayer would do in these circumstances'. As such it was 'not correct to look at Ms Negka's failure to mention that she was living in the property in isolation, but to consider all the circumstances of the case'. The fact that the taxpayer had previously voluntarily disclosed to HMRC that she was living at the property (albeit in the context of another conversation), that she had repeatedly asked HMRC for advice about claiming expenses before a tenant has moved in and that she received confirmation from HMRC that she could claim the rental expenses if the property was available to rent, and that she knew that PPR and rental of a property are not mutually exclusive, were all relevant factors.

On this basis the tribunal concluded that the taxpayer 'did not fail to take reasonable care and that she took the steps of a prudent and reasonable taxpayer'. As such, all penalties were cancelled.

#### Why it matters

The case is a useful commentary on the requirements for determining carelessness by a taxpayer, the standard that a taxpayer is expected to meet when making self-assessments, and the extent to which a taxpayer can expect HMRC to refer to information disclosed previously in a separate context when dealing with the matter in question.

### SDLT surcharge on purchase of residential property by non-UK residents

The consultation on the proposal to charge an extra 1% SDLT on the purchase of residential property in England and Northern Ireland by non-UK residents was issued on 11 February 2019 and will end on 6 May 2019. It is proposed that the surcharge will apply to non-UK resident individuals, non-UK resident trustees and non-UK resident companies. Thus, the scope of its application will naturally be determined by the definition of 'non-resident' as it relates to each of these types of taxpayer.

As the residence status of the purchaser must be determinable as at the date of the transaction, the statutory residence test which uses the tax year as a whole as the period of reference to determine tax residence for income and capital gains tax is unsuitable. Instead it is intended that all individuals who spend fewer than 183 midnights in the UK in the 12 months ending on the date of the transaction will be treated as non-UK resident for the purpose of this charge. If in the subsequent 12 months following the transaction the taxpayer is UK resident (i.e. spends 183 days or more in the UK), they can apply for a refund. Where only one joint owner is non-UK resident under the test, the surcharge will still apply.

The 12-month test will also apply to determine the residence status of trustees (and settlors, where relevant) for the purpose of establishing the residence status of trusts. A company's residence will be determined in the usual way although UK resident close companies that are controlled by one or more non-UK resident individuals will also fall within the scope of the charge.

It is intended that the surcharge will be in addition to the existing applicable SDLT rates such that, for example, it can apply in addition to the existing 3% surcharge that applies to second or multiple property owners. The top rate of SDLT for the balance of consideration over £1.5m would therefore be 16%.

#### Why it matters

The government has acknowledged that the proposed new surcharge is specifically intended to deter foreign buyers still further from the UK property market with a view to mitigating market inflation, such that there is competitive pricing for domestic buyers. How the new rules will work in practice will depend upon the specific drafting of the legislation. The intention is to make the rules 'as simple as possible for taxpayers and conveyancing solicitors to apply' but with a definition of residence that differs from both the pre-2013 rules and the statutory residence test within the context of seemingly ever-changing legislation relating to UK residential property and overseas buyers, one wonders how 'simple' these rules will ever be.

### *Bewley*: whether building was a dwelling

In *P N Bewley Ltd v HMRC* [2019] UKFTT 65 (TC), HMRC disputed an SDLT return filed by the appellant in respect to its purchase of a bungalow and contended that the 3% supplemental surcharge was applicable. It was the appellant's case that the bungalow was not suitable for use as a dwelling and the surcharge should not therefore apply.

The bungalow had been occupied by an elderly lady some time before it was purchased by the company. Following acquisition, the bungalow was demolished. A demolition survey commissioned by the company confirmed the finding of asbestos and the subsequent investigation required the removal of the heating system and 'breaking into floors, through walls, voids [and ceilings].' The bungalow was described in the survey as 'a derelict bungalow in poor internal condition' and could not subsequently be refurbished.

HMRC submitted that 'dwelling' should take its ordinary meaning which does not require the property to be 'mortgageable, meet the better homes standard or to be of standard construction, and a dwelling does not change its nature because it falls into dilapidation'; that the building came within the meaning of residential property and the company intended for the plot to be used as a residential plot; that the fact that no buyer could be found to refurbish the property was not relevant; that planning permission was indicative of the intention that the property was to remain a residential property; and the presence of asbestos did not prevent its renovation or reoccupation, as the critical risk only came during demolition.

In reaching its decisions, the tribunal emphasised that only the factors in play at the point of purchase were relevant. As such, the company's intention as to the use of the property, whether or not the property could be renovated and occupied, and the obtained planning permission should not be taken into account as none of these matters were directly relevant to the state of the property at the point of purchase.

The tribunal confirmed that the 'sole issue' to be decided was whether or not 'the bungalow … was, at the date of completion, suitable for use as a single dwelling' concluding that the bungalow was unsuitable for dwelling use and, as a result, the property could not be classed as residential. The applicable rate of SDLT was therefore determined by the non-residential property scale and the 3% surcharge was not applicable.

#### Why it matters

This case provides helpful and detailed guidance on the definition of a 'dwelling'. However, does it open up a planning opportunity? If the question of whether or not a property, assuming it is not then actually used as a dwelling, is 'suitable' for such use must be tested at the point of completion, does this inadvertently create scope for a dwelling to be made 'unsuitable' for use at that stage in order to secure, artificially, non-residential SDLT rates for the buyer?

The official transcript is also an interesting read as a critique on whether the legislation which imposes higher rates of SDLT on additional residential property has had the desired effect of 'supporting home ownership and first-time buyers' given first residential dwelling company acquisitions do not reap any relative benefit. The tribunal considered that the relevant provision 'is a blanket untargeted anti-avoidance provision' and, on that basis, 'in the circumstances of this case where there can be no avoidance, we should be slow to find that a corporate purchase is liable to the higher rates of SDLT, especially by a developer as in this case who was to and did create a habitable and suitable dwelling on the site.'

### What to look out for

Chargeable gains realised by non-UK residents on the disposal of all UK real property (including commercial property) will be brought within the scope of UK tax from 6 April 2019. ■

For related reading visit www.taxjournal.com

- SDLT: non-UK residents in the crosshairs (Mark Fielden & David Coates, 7.3.19)
- When is a dwelling not a dwelling? (Andrew Hubbard, 13.2.19)

# One minute with...

## Angela Savin

KPMG

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**What's keeping you busy at work?**
I joined KPMG at the start of the year, and the team was very busy with profit diversion enquiries involving a range of international tax issues, stemming from HMRC's focus on diverted profits tax.

The launch of the profit diversion compliance facility signals the clear direction of travel – enquiries of this nature will be a really hot topic for the foreseeable future. The practical aspects of producing a report for the facility – how far back are you investigating, who are you going to interview, how are you going to access information stored in an IT system you upgraded from five years ago – should be grappled with as early as possible. Consistency of approach is critical, ensuring that the same position is taken regarding profit allocation to all taxing authorities and across all taxes. For example, a significant claim for R&D allowances on the one hand, may not sit well with a low royalty payment, on the other.

**If you could make one change to tax, what would it be?**
The prevalence of main purpose tests in domestic legislation, and now principle purpose tests in double tax treaties, leads to real uncertainty for taxpayers. The bar for the application of main purpose tests has primarily been set by cases involving marketed avoidance – which means that translation and application of those authorities to commercial transactions can be challenging. In today's environment of increasingly forensic investigation, everyone should properly document decision making at the time of undertaking any transaction or restructuring where 'purpose' may be relevant. What's the alternative? I think that when the GAAR was introduced all advisers hoped that TAARs would stop multiplying – and of course, that has not happened. I remain convinced, though, that a more formulaic approach to targeted anti-avoidance rules, together with the GAAR, would produce a better balance between protection of revenue and taxpayer certainty.

And if I can sneak in a second change, the First-tier Tribunal should be given jurisdiction to hear judicial review. It makes no sense for a modern legal system not to allow all relevant matters to be heard together.

**What advice would you give to a trainee tax lawyer?**
You need to be a good general lawyer to be a good tax lawyer. Time and again in reported cases you see examples of the tax analysis being applied before the legal reality of the transaction is properly understood.

**Has a recent case has caught your eye?**
*Trigg* involved the taxpayer presenting arguments relying on the purposive construction of the qualifying corporate bond (QCB) legislation, and HMRC arguing for a literal, restrictive interpretation of the pure statutory construct of a QCB. This is a reversal of the more usual positions of taxpayers and HMRC on purposive construction. At the Court of Appeal, the taxpayer was ultimately successful, but that success was not on the purposive construction points. Although that may be the right outcome in *Trigg*, it does seem to me that the courts need to take care to ensure that HMRC are not perceived to have more success in purposive construction arguments.

**What should we be looking out for in 2019 in the disputes arena?**
We are encountering more challenges in settling 'business as usual' tax disputes. It does feel that there is a change in approach from HMRC at an operational level with a greater focus on taxpayer behaviour and HMRC internal governance. Perhaps this is a function of the 'more forensic' approach to enquiries that HMRC publically state is here to stay. In terms of areas, other than profit diversion, allowances and incentives for companies seem to be a particular focus.

**You might not know this about me but...**
I have practiced yoga for a long time, which teaches great patience, a much underestimated virtue. Plus, there is nothing like standing on your head to give you – quite literally – a different perspective on something! ■

# What's ahead

### March

**19** **Compliance:** File monthly CIS return.

**20** **Consultation:** HMRC call for evidence closes on electronic sales suppression.

**21** **Compliance:** File online monthly EC sales list; submit supplementary intrastat declarations for February 2019.

**25** **Cases:** UT scheduled to hear taxpayer's appeal in *Hanuman Commercial Ltd v HMRC* (VAT: whether novation of a contract for the sale of land is an exempt supply of land); and in *Lunar Missions v HMRC* (VAT: whether crowdfunding sums were pre-payments or consideration for single purpose vouchers).

**31** **Compliance:** Companies House should have received accounts of private companies with 30 June 2018 year ends and plcs with 30 September 2018 year ends; final date to reclaim tax paid by a close company on a loan to a participator under CTA 2010 s 455 if loan repaid during the year ended 31 March 2015; HMRC should have received CT SA returns for companies with accounting periods ended 31 March 2018; claims for VAT partial exemption special method must receive approval if to be backdated to 1 April 2018 (March year ends); end of CT61 reporting period; end of chargeable period for annual tax on enveloped dwellings.

### April

**1** **Legislation:** The Value Added Tax (Amendment) Regulations 2018 come into force; gains made by non-resident companies on immovable property will be taxable from this date; the dates on which very large companies are required to make instalment payments will be brought forward by four months; special rate of plant and machinery allowances will be reduced from 8% to 6% for corporation taxpayers.
**Cases:** UT scheduled to hear taxpayer's appeal in *Development Securities v HMRC* (whether uncommercial transaction renders Jersey companies UK tax resident).

*For a 'what's ahead' which looks further ahead, see taxjournal.com (under the 'trackers' tab).*

**Coming soon in Tax Journal:**
- Apprenticeship levy: the case for reform.
- How to handle a domicile enquiry.
- *Farnborough Airport*: losing control?

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## Editor's picks

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| **Post Deals Portfolio Companies – Partner/Director**<br>London<br>£150,000 – £500,000<br>harris glubb CONSULTING | This client has a very successful PE orientated transaction tax practice and is currently winning a lot of post deals work with the portfolio companies. The business is keen to hire a tax specialist who has a proven ability of developing work in this market in the UK. The role will be to take over existing work as well as developing and executing a strategic plan focused around building a service offering to portfolio companies. **Ref TJ091** |
| **Employment Tax Accountant**<br>London<br>£55,000<br>HUMAN CAPITAL PARTNERS | A multi $bn international Healthcare provider looks to appoint an experienced and driven employment tax accountant. Reporting to the indirect tax officer, the successful candidate will play a key role in providing support to the business in improving employment tax compliance and process change matters, whilst implementing the development of robust compliance systems and processes. **Ref TJ092** |
| **UK Corporate Tax Specialists**<br>Berkshire<br>£competitive<br>DHL | Deutsche Post DHL is looking for 2 candidates: one permanent and one 12 month maternity cover. The UK tax team is responsible for all corporate, indirect and employment tax matters within the UK The roles available are specialist corporate tax roles. Are you keen to manage the increased compliance requirements and complexities in the area of corporate tax, withholding tax, transfer pricing and tax risk management? **Ref TJ093** |
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| **Employer Consulting/Reward Partner Role – Mid Tier**<br>London<br>£150,000 – £200,000<br>GOODMAN MASSON | A highly successful and profitable mid-tier accountancy firm, is looking to recruit an employer consulting/reward partner. This is an opportunity to build a practice and suits someone who is ambitious and entrepreneurial and feels that they ahve the existing contacts and network to generate business alongside leveraging the firms existing client base. You will be a director or partner in a big 4 or top 10 or consulting firm and will have proven business development skills. **Ref TJ095** |

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