Proskauer

UK Tax Round Up

November 2019

UK Case Law Developments

More decisions on IR35

This month has seen two more decisions on whether broadcast presenters providing their services to the BBC and ITV respectively would or would not have been employees had they provided their services directly rather than through personal service companies.

The Upper Tribunal (UT) and the First-tier tribunal (FTT) came to differing decisions in the cases of *Christa Ackroyd Media Limited v HMRC* and *Canal Street Productions Limited v HMRC*. While the two decisions can be justified on their respective facts, the cases highlight the difficulties that can arise when trying to determine whether an individual would or would not be an employee of their client were they to contract with the client directly. This question is going to be of increasing importance to many businesses from next April when the IR35 rules applicable to medium- and large-sized organisations engaging workers through intermediaries will change fundamentally to place the onus of employment or self-employment determination on the client company (as discussed in our recent Tax Blog.

The significant difference in the two cases was seemingly in the duration and extent of the services provided by Ms Ackroyd and Ms Fospero respectively. Ms Ackroyd provided her services to the BBC as presenter of the Look North programme under a contract for seven years through which she was engaged to provide her services for a minimum of 225 days per year while Ms Fospero was engaged to work as a cover news presenter for ITV on the Daybreak and Lorraine programmes under a contract that lasted from April 2012 to April 2014 and through which Ms Fospero was engaged on an ad hoc, as needed basis albeit with commitments to provide her services and not undertake other competitive work when she was so engaged.

Both cases go into considerable detail on how the three basic requirements for employment (as opposed to self-employment) should be applied to the working arrangements in question. These requirements are:

1. mutuality of obligation under which the individual agrees to provide their personal services to the client and the client agrees to pay for those services;
2. control under which the client has control over the basis on which the individual performs their services; and
3. other relevant factors which might point away from an employment arrangement even where the mutuality of obligation and control conditions are satisfied.

While the cases considered these requirements in detail, it is not clear from either of them why the difference in application of the detailed technical analysis to the facts resulted in employment on the part of Ms Ackroyd and self-employment on the part of Ms Fospero. Rather, it appears that the decisions were taken on a broad view of the arrangements as a whole. So, in the case of Ms Ackroyd, the UT stated at one point that the arrangements looked like long-term arrangements such as would be entered into between an employer and their employee, whereas the overall impression of the arrangements between ITV and Ms Fospero was that she was free to engage in, and did engage in, other activities alongside her arrangements with ITV in the manner that a self-employed contractor would.

It is to be hoped that, given the future increased importance of employment/self-employment decisions for companies, a clearer exposition of the basis on which the mutuality of obligation, control and other relevant factors should be applied will be forthcoming from HMRC or the courts in the near future.

Shares with preferential rights didn't qualify for EIS relief

In *Foojit Limited v HMRC,* the FTT considered whether or not certain shares qualified for EIS relief. This is the latest in a number of recent cases that have considered similar issues when companies have more than one share class with slightly different rights.

EIS is available for certain investments in newly issued ordinary shares of qualifying companies when, among other things, the shares do not carry any present of future "preferential right" to dividends (of a type set out in the rules) or to the company's assets in a winding up.

The taxpayer company issued B ordinary shares to some investors in the expectation that the investors would be able to claim EIS relief. The B shares carried no preferential right to the company's assets on a winding up but did carry a right to a priority dividend in an amount equal to 44% of the company's profits available for distribution. Under the EIS rules, shares do not qualify if they carry a "preferential right" to a dividend referred to in section 173(2A) ITA 2007. These are dividends where the amount of any dividend, or the date on which the dividend is payable, depends to any extent on a decision of the company, the holder of the share or any other person.

The relevant terms of the company's articles relating to dividends stated that the company shall in priority to the payment of any dividend on other shares pay the holders of the B shares a prior dividend equal to 44% of the profits available for distribution. They did not say anything about when such dividend had to be paid or that it was in any way automatic if the company did have profits available for distribution.

Following the decision in *Flix Innovations Ltd v HMRC*, the FTT stated that the EIS provisions are "closely articulated" and, therefore, should be applied prescriptively to the extent possible within their overall purpose so that it was unlikely that in enacting the rules Parliament would have intended to permit small or insignificant preferential rights to be ignored.

Applying this general approach to the rules, the FTT decided that the B shares' preferential right to a dividend of 44% of the company's distributable profits did depend to an extent on a decision of the company since it was not the case that there would be an automatic declaration of a dividend if there were distributable profits. The right to the preferential dividend only arose if the company decided to declare a dividend.

The case is another example of how strictly the complex and detailed requirements for EIS relief to be available will be scrutinised and applied by HMRC and that the courts are likely to support such an approach to the rules. Taxpayer companies would, therefore, be advised to take specialist advice in this area where they are seeking to issue shares that qualify for EIS relief.

Ability to conform UK law to EU law

In *Trustees of the P Panayi Accumulation and Maintenance Trusts Ns 1-4*, the FTT considered the extent to which it could insert words into UK law in order to conform it to EU law.

The case concerned the application of the UK's capital gains tax exit charge under section 80 TCGA 1992 arising when the UK resident trustees of a family trust retired and were replaced by Cypriot trustees so that the residence of the trust moved from the UK to Cyprus.

Under section 80 the exit charge relating to the market value of the trust's asset at the time it moved its residence was subject to immediate tax in the UK.

Various decisions of the ECJ have considered the lawfulness of such a provision in the context of the EU's freedom of establishment principle and have considered that while, in principle, it is proportionate for one Member State to protect its tax revenues by seeking to tax the value of assets moved to another Member State, it is not proportionate for the tax to be levied immediately. Rather, case law has shown that it would be proportionate for the exit charge to be spread over five years.

Given the terms of section 80 and the relevant tax payment provisions in the Taxes Management Act 1970 (TMA 1970) the question for the FTT was whether they could conform the relevant UK tax legislation so that it met the requirement under UK law that it complied with EU law in this regard.

The FTT considered two issues:

1. first, whether it was possible to comply UK law with EU law; and
2. second, which provision under UK law would require amendment so as to satisfy such compliance.

The trust had argued that the relevant provision for compliance was section 80 TCGA 1992 and that it was not possible to write additional words into that provision without doing excessive damage to UK law, so that the only method of compliance would be to disapply section 80 altogether.

HMRC argued, on the other hand, that the UK law could be amended so as to comply with EU law by including compliant payment deferment provisions into section 80.

The FTT decided that the relevant provision that would require amendment was section 59B TMA 1970 rather than section 80 TCGA 1992 since section 80 simply stated that a tax liability arose on exit of the trust (which was compliant with EU law) whereas section 59B required that tax to be paid immediately (which was not).

Given the overarching requirement to comply UK law with EU law to the extent possible, the FTT also decided that it could read words into section 59B requiring the tax to be paid in five annual instalments following the trust moving to Cyprus.

The case gives an interesting discussion on what is and is not possible in order to comply UK law with EU law. This will be relevant at least until the end of the transition period on 31 December 2020 to the extent that the UK does agree to leave the EU before then.

Judicial review granted on reliance on HMRC statements

In *R (oao Cobalt Data Centre 2 LLP and Cobalt Data Centre 3 LLP) v HMRC*, the UT has granted the appellant taxpayers the right to apply for judicial review on an assessment raised on them by HMRC that was not in accordance with statements made by HMRC to the Enterprise Zone Property Unit Trust Association (EZAUTA) in 1994 on which costs could be treated as paid "for" an interest in an enterprise zone.

The case related to what might be considered to be tax avoidance schemes under which the LLPs acquired interests in properties in enterprise zones that might generate profits over a period of about 15 years but generated large income tax deductions for the individual members of the LLPs immediately.

Notwithstanding this, the UT granted judicial review on the basis that the published statement made by HMRC to the EZAUTA was "clear, unambiguous and devoid of relevant qualification", was given to an identifiable group (those persons interested in investing in enterprise zones) and, even though it has since been agreed that HMRC's statement did not accord with the law, there were no good reasons to allow HMRC to resile from its practice since, when the statement was made, the law was not clear.

The case is interesting because, contrary to other recent cases relating to reliance on HMRC statements, it upheld the taxpayer's right to rely on such statements (or at least make a claim for judicial review in respect of them) when the statement was sufficiently clear, unambiguous and relevant to the taxpayer's expected tax position.

Also of interest is that the UT's approach to the question (and to a substantive question of whether the LLPs were carrying on a business with a view to profit) was not swayed by the fact that the relevant arrangements might have been considered to relate to tax avoidance and that the LLPs didn't expect to make a profit for a good number of years.

Other UK Developments

HMRC clarifies when contractors at risk of retrospective IR35 enquiry

In connection with the changes to the IR35 rules from next April (referred to above), HMRC has published a policy paper stating that it will only use any information that they receive from companies undertaking an assessment of the employment/self-employment status of workers that they engage through intermediaries to open enquiries into the historic IR35 position of such workers if they have reason to suspect fraud or criminal behavior on the part of those workers in the past.

From April next year, all medium- and large-sized companies who engage workers through intermediaries will have to prepare a "status determination statement" for each such worker to assess whether the worker should be treated as an employee or self-employed person, provide that statement to the worker and operate employment tax obligations based on the assessment. To date this assessment has been carried out by the intermediary, which has also had all employment tax payment obligations. This change is likely, for practical and risk management reasons, to lead to a large increase in assessment of employment status. This has raised concerns that HMRC might use this increased application of employment status to workers engaging through an intermediary to open historic cases that they have not challenged under the existing IR35 rules.

This statement by HMRC provides comfort to the thousands of workers that have used personal service companies, often at the demand of their clients, that their past treatment as self-employee contractors will not be looked into by HMRC.

Review of the disguised remuneration loan charge delayed

The previously announced review into the highly contentious disguised remuneration loan charge that because effective at the end of September has been delayed until after December's General Election.

The Government's review into the disguised remuneration loan charge was announced in September (as reported in our UK Tax Round Up). The Chancellor has now announced that it will be delayed until after the General Election, notwithstanding HMR's statement that it has set a January 2020 deadline for settling claims under the loan charge.

Given the significance of the loan charge for thousands of people, it is hoped that the review will be picked up rapidly after the General Election so that those individuals affected can obtain certainty on their position before their tax payments become due at the end of January.

Calls for abolition or reform of entrepreneurs' relief

Sir Edward Troup, the ex head of HMRC, has called for whichever party wins the upcoming General Election to abolish entrepreneurs' relief in its entirety.

Mr Troup said that the relief was costing the country £2 billion a year in lost tax yet provided "no incentive for real entrepreneurship". He went on to say that the relief had a "minimal impact on encouraging entrepreneurship in the UK" and that "there are lots of things getting in the way of people becoming great entrepreneurs in this country, but the fear of tax on future gains in not one of them".

This has been reflected in the main parties' manifestos for the upcoming General Election. The Labour Party has stated that it will abolish entrepreneurs' relief and "consult on a better form of support for entrepreneurs which is not largely just a handout for a small number of people". The Conservatives have said that they will "review and reform" the relief. The Liberal Democrats have said nothing about it.

HMRC guidance on taxation of cryptoassets

HMRC has published a useful policy paper on the taxation of transactions involving cryptoasset exchange tokens (such as bitcoin) by companies and other businesses and updated its guidance for individuals following the publication of the Cryptoassets Taskforce's final report and guidance.

The guidance confirms that:

1. cryptoassets are not currency;
2. any calculation of taxable profits or losses must be in sterling, so that exchange tokens without a sterling value must be converted using the appropriate

exchange rate at the time of acquisition and disposal; and

3. whether activities involving exchange tokens constitute trading or investment depends on the normal tests to be applied to those activities. This means that a careful consideration will need to be given to each different type of transaction relating to exchange tokens and the circumstances surrounding them.

The guidance also updates HMRC's previous guidance on the VAT treatment of bitcoin and similar crypto currencies and confirms its view that the transfer of exchange tokens is not subject to stamp duty or SDRT because exchange tokens are unlikely to meet the definition of stock or marketable securities.

Other Developments

OECD publishes public consultation document on GLoBE Proposal Pillar Two

The OECD has published a consultation document on its proposals for Pillar Two of the Global Anti-Base Erosion Proposal (GloBE). This is part of the programme of work for addressing the tax challenges resulting from the digitalisation of the economy. Responses to the consultation on Pillar One of the programme addressing the allocation of taxing rights between jurisdictions was published on 15 November.

Pillar One considered the allocation of taxing rights between jurisdictions and puts forward various proposals for new profit allocation and nexus rules where digital sales are made from low tax jurisdictions. Pillar Two focuses on developing rules that would ensure that a minimum amount tax was paid where other jurisdictions have not exercised their primary taxing rights or the payment is otherwise subject to low levels of effective taxation. Although these proposals derive from concerns about the taxation of the digital economy, the OECD recognises that is difficult to ringfence the digital economy and, therefore, the scope of GLoBE is not limited to highly digitalised businesses.

The Pillar Two proposal is intended to operate as a top up to a minimum fixed rate of tax (that is yet to be agreed). The proposal is based around four rules seeking to ensure that all profits are subject to effective tax at an agreed minimum rate in one jurisdiction or another.

The rules would be implemented through changes to domestic law and tax treaties and would incorporate a rule to avoid the risk of double taxation that might otherwise arise where more than one jurisdiction sought to apply the rules to the same structure or arrangement.

The consultation document considers matters such as the importance of a consistent tax base, the use of financial accounts to determine income, possible permanent and temporary adjustments to such accounting results, the effect of blending results on volatility, how to allocate income between branches and head offices, how to allocate income of a tax transparent entity and credit for taxes that arise in another jurisdiction.

Given this concerted effort by the OECD coupled with jurisdictions such as France and the UK recently introducing unilateral rules on the taxation of companies making digital sales in those jurisdictions, it seems likely that this move to introduce internationally accepted rules governing how digitally-derived profits should be taxed will only grow stronger over the coming year or so.

A public consultation meeting on the Pillar Two proposal will be held on 9 December. The ambitious long term goal is to reach a consensus view during 2020.

Related Professionals

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