AAT Tax Update 14 October 2013

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1. Refurbishment of a dilapidated property was a supply of services for VAT

Khoshaba t/a Cinnamon Café v Revenue & Customs [2013] UKFTT 481 concerns whether preregistration expenditure could be recovered. The issue was whether the costs incurred in refurbishing and converting a property previously used as a hairdresser into a café were a supply of services or goods. If the supply was for services, the input VAT incurred was out of time but if it were goods it could be recovered.

Mrs. Khoshaba obtained a lease of premises which had previously been used as hairdressers. She had the premises converted by her husband's building company in order to operate a café, which commenced trading on 4 June 2007. Initially it was not VAT registered.

HMRC investigated her business in July 2010 and decided that it ought to have been registered with effect from 1 October 2008. There has been no appeal against that decision.

The first VAT return covered the period from 1 October 2008 to 31 May 2011. In this return some £46,757 worth of input tax was reclaimed (against a declared liability to output tax of some £48,000). HMRC required the taxpayer to breakdown and justify this input tax reclaim.

The main issue in dispute was an invoice which included £22,050 in VAT from Lindfield Building Contractors Ltd, Mrs Khoshaba's husband's company. The invoice was dated 30 July 2007. This was more than six months before the effective date of registration but less than 3 years before that date. It was accepted that the effect of the Value Added Tax Regulations 1995 Regulation 111(2) was to permit a taxpayer to recover pre-registration input tax incurred on supplies to the business in the four years prior to registration in so far as they were supplies of goods but only six months in so far as they were supplies of services.

The conversion of the property took approximately 4 months to be completed after possession of the premises was given by the landlord. The first month was spent in planning, making estimates, doing surveys and appointing architects and surveyors. The physical work to the shop took about two and half months.

The work to the ground floor shop involved ripping out the hairdressing fixtures such as the sinks, removing load bearing walls and replacing them with structural beams, replacing and enlarging the existing toilet facilities (including the necessary drainage works), re-plumbing and re-wiring the entire premises.

Once this was work was done and made good, counters and units which were built to order by a joinery company were installed. Fridges were purchased and installed. New wood flooring was laid.

A new air conditioning system was sub-contracted, and the sub-contractors installed it. A canopy and shutters at the front were also commissioned by Lindfield and installed by the company which made them.

The tribunal concluded that a significant part of Lindfield's invoice represented the cost of goods and a significant part represented the cost of services. The first question is whether Lindfield made a single supply to the appellant or a number of supplies. In other words, did it supply the prefab goods separately to the works of refurbishment of the premises? The tribunal concluded that this was a single supply in the sense that the elements which comprised the supply were so closely linked that they objectively formed a single indivisible economic supply.

At paragraph 36, the tribunal went on to conclude that the supply was the service of providing a refurbished shop; it was not a supply of goods (the pre-fab units) with incidental installation works. The claim to recover input VAT did not fulfil the requirements of Regulation 111(4) because the invoice was for services which were provided more than six months before the registration date and therefore HMRC were correct to refuse to exercise their discretion to allow the recovery of the pre-registration input tax on the Lindfield invoice.

There were other subsidiary issues to this case but in the context of a non-compliant taxpayer whose failure to register at the right time will suffer penalties, the decision demonstrates that in tax the strict interpretation of the law can be expected. In a project similar to that of Mrs. Khoshaba, an intended trader registration might have enabled all of the input tax on the **services** obtained to be recovered.

2. HMRC publish their views on the employment status of actors on TV

On 23 July 2013 the Court of Appeal unanimously confirmed the decisions of the FTT and UT that most actors appearing on TV in a series are to be treated as if they are employees and the 'employer' has to account for secondary NIC. HMRC have now published their views in a briefing note 29/13 which can be **read in full.**

Employment status is a difficult technical area and mistakes will prove costly so it is important to get it right. It is a matter of contractual arrangement and it is possible, with the right advice, to arrange whatever status is desired.

You can read the full text of the ITV decision on the British and Irish Legal Information Institute's website: **ITV Services Ltd v Commissioners for HMRC**

All national broadcasters, film companies, theatre managers, independent production companies, their representative bodies and agents in the Film & TV Production Industries, Equity, individual entertainers and any other companies engaging entertainers to whom this judgment may also be relevant are encouraged to read this briefing.

3. HMRC updates its strategy on agents

Since 1 April 2013, HMRC has had new powers to investigate and if appropriate impose civil penalties on dishonest agents. I think that it is important to realise that these powers need not concern agents doing honest work on behalf of their clients.

I mention this area because, like having an insurance policy, one hopes that the worst never happens but if it does it is as well to be prepared. Human beings make mistakes and while HMRC makes lots of mistakes, many of the officers within HMRC are professional cynics and view the mistakes of others as negligence or even worse dishonest.

These are civil penalties but the rights and protections of the Human Rights Act are available and triggered by HMRC alleging dishonest conduct. Being a civil penalty matter, the evidential requirement is to prove on the balance of probability (rather than beyond reasonable doubt) but the onus lies with HMRC to prove their allegations.

A tax agent is an individual who, in the course of business, assists clients with their tax affairs.

Dishonest conduct is when an individual acting as a tax agent does something dishonest with a view to bringing about a loss of tax. Dishonest is not making a mistake. Dishonest requires the person knowingly doing something that they knew was wrong – so it is quite a high hurdle.

Only specialist officers in HMRC can issue a conduct notice. Anyone receiving one should seek expert advice as quickly as possible. The consequence of a conduct notice might potentially be that the specialist officer can then:

- ask for access to your working papers
- charge penalties if they do not get access to your working papers when they ask for them
- charge you a penalty for dishonest conduct of between £5,000 and £50,000
- publish details about you if you are charged a penalty for **dishonest conduct** of more than £5,000

HM Revenue & Customs (HMRC) relationship with tax agents
HMRC has updated their guidance on the Tax Agent Strategy - including an update on the Agent and Client Statistics pilot. I recommend reading this because it should reassure those who work conscientiously to guide their clients through the 'jungle' of complex tax law.

4. HMRC publishes statistics analysing tax yields from the 4 countries in the UK

HMRC collected £470bn in 2012/13. Over the last decade IT, CGT & NICs (Income tax, Capital Gains Tax and National Insurance Contributions) have made up on average 55 per cent of total receipts. VAT (Value Added Tax) and Corporation Tax (CT) are the next biggest, contributing an average 19 per cent and 9 per cent of total receipts respectively.

HM Revenue & Customs (HMRC) Tax Receipts Between England, Wales, Scotland & Northern Ireland

This publication apportions total UK tax receipts to England, Wales, Scotland and Northern Ireland. It attempts to measure the true economic incidence of taxation, based on the underlying activity, which can often differ from how or where the **tax receipts** are collected.

5. HMRC launch new campaign to encourage voluntary disclosure

On 4 October 2013, HMRC launched their latest campaign entitled: "Health and Wellbeing Tax Plan". You can **read the details here.**

This HMRC guide tells you about the Health and Wellbeing Tax Plan voluntary disclosure opportunity which runs from 7 October 2013 to 6 April 2014. It will be of interest to you if you or your client work in the field of health and wellbeing and you want to bring your tax affairs up to date.

The disclosure opportunity is available to a professional working in the following areas:

- physical therapy - e.g. physiotherapist, chiropractor, chiropodist, osteopath, occupational therapist
- alternative medicine or therapy - e.g. homeopathy, acupuncture, nutritional therapy, reflexology, nutrition
- other therapy - e.g. psychology, speech therapy, arts therapy

This list is not exhaustive.

This is a lengthy read running to about 8 chapters and **a couple of appendices.**

Derek Allen
14 October 2013
The views expressed in these podcasts are Derek Allen's personal views and do not necessarily represent AAT policy or strategy.