AAT tax update podcast notes - 30 April 2014

In this month's edition of the tax update podcast we look at:

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1. HMRC are using credit and debit details to check business income

Computers can process enormous amounts of data. Legislation issued in 2013 has given HMRC with powers to request data from Merchant Acquirers. Merchant Acquirers are financial institutions that process all credit and debit card transactions on behalf of UK businesses. There are eight major Merchant Acquirer businesses operating in the UK. HMRC has now received the first sets of data from the Merchant Acquirers providing monthly credit and debit card income from UK businesses. HMRC uses the data to:

- check businesses are declaring all of their income
- increase their understanding of the behaviours and compliance profile of businesses who receive credit and debit card income
- improve fraud detection

Compliant businesses have nothing to fear from this development. But it smacks to me of big brother is watching and if there is a mismatch between declared sales and amounts banked, HMRC will use variances to target their enquiry resources.

2. PAYE for employers: Employer Bulletin Issue 47

Issue 47 of the Employer Bulletin (PDF) is now available and at 44 pages it is a worthwhile read. Aimed at employers and agents, it contains important information and news about topics which may affect payroll obligations to HMRC.

3. Overnight subsistence allowances paid to lorry drivers

Following discussions with the Road Haulage Association, the lorry drivers' overnight subsistence allowance rate remains unchanged: £26.20 for drivers with sleeper cabs and £34.90 for drivers with non-sleeper cabs. Where the employer knows that the driver uses the sleeper cab, the amount paid free of tax should not exceed a reasonable reimbursement of:

- evening meal and breakfast
- washing facilities
- upkeep of bedding in the cab.

Where there is documentary evidence to show that the employee necessarily spent the night away from home and his or her permanent workplace (if any), HMRC accepts that a payment of 75% of the figure shown at **EIM66110** does no more than reimburse the expense incurred when the driver uses the sleeper cab overnight.

4. HMRC publishes draft legislation and guidance on deemed employees of LLPs

On 16 April HMRC published for 'consultation' **four pages of draft legislation and four pages of explanatory notes on certain members of a Limited Liability Partnership (LLP)** - salaried members - to be treated for the purposes of the Social Security Contributions and Benefits Act 1992 (SSCBA) as employed in employed earners employment. The consequence of this is that a Class 1 or Class 1A National Insurance contributions (NICs) charge arises on their earnings or benefits from that employed earner's employment.

5. Controlled Foreign Companies (CFC) Rules - Guidance on Finance Bill 2014 proposed amendment

Guidance on the **proposed amendment to the CFC rules in Clause 286 Finance Bill 2014 was published on 17 April.** CFC rules protect the UK from artificial diversion of profits without taxing profits that genuinely arise outside the UK.

The draft legislation will apply if a CFC's creditor relationship is connected with an arrangement that has a main purpose of diverting into a CFC non-trading finance profit streams that were previously received by a UK resident company. Where achieving this diversion is not a main purpose of the arrangement, the draft legislation will not apply.

In particular, the proposed rule will not affect the ability of businesses to use CFC finance companies for new investment outside the UK or their freedom to restructure existing lending from CFC finance companies. There are 17 pages of guidance on this and more guidance will be issued over the summer.

6. Technical Note on the taxation of corporate debt and derivative contracts

HMRC has published a **14 page Technical Note** (PDF) providing an update on the 'Modernising the taxation of corporate debt and derivative contracts' consultation. Historically, the complexity in the loan relationships and derivative contracts regimes has consistently provided opportunities for attempts to avoid tax. Reactive measures to counter this avoidance have contributed to further complexity and to some loss of structural clarity in the regime, tending to leave further potential loopholes. This growing complexity has increased compliance costs for some businesses and has made it difficult in some cases for compliant groups and companies to be certain about tax treatments, undermining the international competitiveness of the UK tax system. Change has started in Finance Bill 2014 and more will follow in 2015 so if you want to keep abreast of policy thinking follow the link.

7. An old master painting was plant and its sale for £9.4 million exempt from Capital Gains Tax (CGT)

CGT is an area which still produces surprises but the decision in **HM Revenue and Customs v The Executors of Lord Howard of Henderskelfe [2014] EWCA Civ 278** was such a surprise. Being a unanimous decision of the Court of Appeal, it is legal precedent unless and until it might be overturned on an appeal to a higher court such as the Supreme Court or new legislation is introduced.

Lord Howard of Henderskelfe died on 27 November 1984. Included in the personal estate that devolved onto his executors was a valuable portrait painted by Sir Joshua Reynolds in about 1775. The picture was of Omai, a South Sea islander. On 29 November 2001, the executors sold the picture at auction at Sotheby's to an unconnected purchaser for a hammer price of £9.4m, from which commission and value added tax totalling £220,900 was deducted. The price represented a substantial gain over the value of the picture at Lord Howard's death 17 years before.

Castle Howard, located in North Yorkshire, has, since 1950, been owned by Castle Howard Estate Limited ('the company') and still is so owned, and it is the company that ran and runs the trade of opening the house. The painting was on display in the Castle which was open to the public throughout the life of the late Lord Howard and during the period of executry up to the date of sale in 2001.

The issue was whether the gain was chargeable to CGT or, as the executors contended, the gain was exempt because the 226 year old painting was a wasting asset with a predictable life of less than 50 years. The upper tribunal had decided in favour of the taxpayer that the painting was plant.

The company has carried on the trade of opening part of Castle Howard and its grounds to the public since 1952, and the trade includes the exhibiting of the works of art to the visiting public. Lord Howard owned several works of art. During his life he permitted the company to use many of them, including the picture, for such exhibition. He arranged with the company that it would bear the costs of the insurance, maintenance, restoration and security of the works. There was, however, no formal lease or licence under which the company was permitted to exhibit them, nor was there any provision for the payment by the company to Lord Howard of any hire or rental fee. The arrangement was terminable by Lord Howard at will. Following his death, the executors continued the arrangement on the same terms. The picture was displayed by the company throughout the period of the executors' ownership save for three periods totalling about seven months when it was exhibited in Paris, London and York. Apart from a short period after Lord Howard's death, and the period from 1997 onwards when only two of the three executors were the directors, the executors were the same individuals who were the directors of the company.

The exemption to be found in ss44 & 45 TCGA 1992 is a classic example of bad law producing unintended consequences. The likely explanation for the introduction of the exemption was probably not so much with a view to benefiting taxpayers with a new exemption on gains on the disposal of tangible movables as to foreclose their opportunity of achieving allowable losses on such disposals.

There are numerous cases which consider the definition of ‘plant’ but the principle was clarified in *Yarmouth v. France* (1887) 19 QBD 647. The question there was whether a vicious horse owned by an employer was 'plant' within the meaning of section 1(1) of the Employers' Liability Act 1880, a question that had to be answered affirmatively if the employee whose leg the horse had broken was to be entitled to compensation from his employer. Lindley LJ said, at 658:

'There is no definition of plant in the Act: but, in its ordinary sense, it includes whatever apparatus is used by a business man for carrying on his business, - not his stock-in-trade which he buys or makes for sale; but all goods and chattels, fixed or movable, live or dead, which he keeps for permanent employment in his business …'.

The picture was being used for the promotion of the company's trade and that in the company's hands it passed the 'permanence' test referred to by Lindley LJ. The Upper Tribunal held that the picture was 'plant' within section 44(1)(c) and thus a deemed 'wasting asset' within the meaning of section 44.

HMRC argued that even if the picture was plant in the hands of the company, it was not plant in the hands of the executors since they were not carrying on the trade that engaged its use. When they sold the picture they were not, therefore, selling any plant, nor therefore were they selling a 'wasting asset' within the meaning of sections 44 and 45(1).

HMRC argued that the picture could not be 'plant' within the meaning of section 44 because the section contemplates that what is plant is an asset with a limited life that wastes away with use. An 'old master' such as the picture, which on its 226th birthday proves to be worth £9.4m, cannot fit such a description.

The problem with it is that what is 'plant' is not identified by the predictable life of a chattel. It is identified by whether or not the chattel passes the *Yarmouth v. France* test; and an item is capable of doing so whatever its predictable life. Once an item qualifies as 'plant', it is '*in every case'* deemed by section 44(1)(c) to be a wasting asset; and for HMRC to argue that an item of plant enjoying unusual longevity is not plant at all is to advance an argument that the section expressly excludes and which amounts to no more than a pointless beating of the air. On the facts of this case, section 44 may have proved inconvenient to HMRC. They must, however, take the rough with the smooth; and this case may be an example of the rough.

It surprised me that the gain was exempt. Now we are all faced with the challenge of advising wealthy clients of this particular loophole until the law is changed!

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

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30 April 2014