Tax update – 30 November 2016

AAT Tax Update 30 November 2016
In this Month's edition of the Tax update we look at:

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1. Self employed status and the Uber decision

Watching the news at the end of October, I listened to the contrasting arguments about whether the decision that taxi drivers who worked for Uber should be considered workers and will be entitled to holiday pay, paid rest breaks and the national minimum wage - among other rights including rest breaks, have protection from discrimination and cannot be dismissed for whistleblowing.

The 40 page decision affects some 30,000 drivers on London and another 40,000 throughout the country although the two named drivers were a test case. The dispute concerned minimum wage and working time regulations and the tribunal considered a considerable amount of contractual evidence. The claimants considered that UBER instructs manages and controls the driver. Uber argued that the drivers are self employed and free to choose whether to accept a job or not and each driver was in control of the route taken and the manner of transport.

In the Supreme Court decision in 2011 of Autoclenz, the Court recognised that the negotiating position of the parties may not be equal and also that the contractual wording may not reflect reality. In that case the freedom of the workers was restricted and the right of substitution was apparently a sham. In reality the workers were subject to control and had to accept the terms of their employers.

In the published judgement, the tribunal made it clear that it thought Uber's argument that it had 30,000 self employed businesses working for it in London was fairly ridiculous and that the written contractual arrangements were not reflected in reality or practice. Uber is likely to appeal this decision and this is a persuasive authority only.

However, several years ago the HMRC published a document consulting on how HMRC would challenge what it perceived as false self employment in the construction industry sector. HMRC believed that over 300,000 workers in the construction sector were wrongly categorised as self employed. In addition I anticipate that couriers and delivery drivers may find themselves affected by this decision. A newsletter to clients might be appropriate along with an invitation to review any contracts for service in the light of the underlying principles which emerge from this decision.

If someone's employment status for PAYE still isn't clear, you can use HMRC's Employment Status Indicator . If in doubt sort it out.

https://www.judiciary.gov.uk/wp-content/uploads/2016/10/aslam-and-farrar-v-uber-reasons-20161028.pdf

2. Martial Arts instructor was an employee and not a partner of Karate World

Continuing the theme of looking at status, in Ashton v Revenue and Customs [2016] UKFTT 727 the issue was HMRC's decision to treat Mr Ashton as a self-employed partner of Karate World, a martial arts instruction business, rather than as an employee of Karate World for the tax years 2008/09, 2009/10 and 2010/11. The usual dispute on status involves HMRC arguing that an individual is an employee because the NIC liability is much greater. For this reason, it is a judgement of some interest to research how HMRC argue that an individual is self employed.

Mr Ashton trusted Mr Thompson the proprietor of Karate world and the alleged employer: he had started training with Mr Thompson at the age of 10, had gone on to compete in World Championships with him, and was accustomed to following Mr Thompson's lead. At the time of the change to a partnership in 2003 in the business, the appellant was around 21/22 years old. Accordingly, the appellant did not question Mr Thompson's decision that the appellant should be self-employed, rather than an employee – he accepted Mr Thompson's view that this was the best way to run the school, and had no reason to question otherwise.

Mr Ashton was paid £1,333 each month and would receive a bonus payment based on the performance of the school where he worked. The appellant received a smaller basic pay than staff at other schools, but received a better bonus as the school did better than other schools in the business. The bonus was paid if the school met certain targets for the month, both financial targets and enrolment targets. Requests for holidays originally had to be submitted in January each year, because cover had to be arranged between the schools and so two people could not be away at the same time. After a while this became too difficult to arrange and so the schools all shut down for two weeks in the summer and two weeks at Christmas, and all staff had to take their holidays at that time. It was sometimes possible to take a couple of days at other times, but it was difficult to organise cover. At least two weeks' notice had to be given for any requests for days off in order to be able to organise cover.

Mr Ashton had received full pay for the two weeks' sick leave when he had his appendix removed, receiving both basic pay and bonus payments. Mr Ashton took no financial risk in the business; he had no access to partnership bank accounts. He accepted that he was a signatory on a partnership savings account, which he believed had been set up to take the profits split from the various schools. A percentage of profits from each school was paid into the account in order to pay bonuses to the chief instructor in a school if that school met its targets. The appellant explained that he had nothing to do with the account and that he didn't know why he was a signatory.

Mr Ashton was expected to provide his own uniforms, training shoes, and weapons for particularly types of martial arts. He was expected to buy high quality weapons. On the basis of the evidence received and oral testimony the tribunal found the facts as follows:

(1) The appellant had been an employee of the predecessor business operated by Mr Thompson

(2) The appellant completed his tax returns for the relevant tax years on the basis that he was a partner in Karate World.

(3) The appellant did not receive partnership accounts or a copy of the partnership agreement for Karate World. The appellant did not take part in any partnership meetings.

(4) The appellant was paid a basic amount each month and would receive a bonus amount for each month in which the school in which he taught achieved a particular turnover figure.

(5) The appellant was expected to meet business expenses on his own account, other than mileage, rather than having such expenses met by the partnership as a whole.

(6) The appellant was a signatory on a partnership savings account but did not have any control over the operation of that account.

(7) The Karate World partnership business was controlled by Mr Thompson, setting both the content of classes and the way in which classes were to be taught.

The tribunal ruled that Mr Ashton was an employee despite having declared himself to be self employed and completing documents which included CWF1 self-employment registration and self-assessment returns which were prepared on a self-employment basis as a partner in Karate World. There was mutuality of obligation, he did receive holiday and sick pay and he was subject to control. On the balance of probability, he was an employee.

http://www.bailii.org/uk/cases/UKFTT/TC/2016/TC05456.html

3. Which family member (Father or daughter) is assessed for BIK?

This tax case reads like a novel which involved a family feud between two half-sisters who had the same father. The family company paid care home fees for Mrs Baylis, wife of one employee and mother of another.

In Baylis v Revenue and Customs [2016] UKFTT 725, Sarah Baylis was the daughter and she had signed a contract for the care home fees to care for her mother. An issue was whether she did so as an agent of the company of which she was a director or whether she did so in her own capacity. The evidence was clear that she lacked the economic means to pay the care home fees herself and that when she signed the contract she acted under the instruction of her father who owned and directed the company when he was younger and more able.

The lack of clarity in the case arose because old age seems to have denied Mr Baylis the ability to give any evidence on the matter. Mr Baylis had a second family and his daughter by that second family was the finance director of the company. She denied that the company should allocate the benefit in kind to her father and argued that as her half-sister had signed the contract the benefit should be allocated to Sarah Baylis.

The tribunal judge, Anne Redston, decided that:

(1) Ms Baylis had contracted with the care home as agent for VWML; and

(2) the resulting benefit in kind charge did not fall on Ms Baylis. This is because, where two employees are potentially liable to tax on an "employment-related benefit" provided "for a member of an employee's family or household", the legislation sets out a hierarchy, under which "spouse" takes priority over "parent". I also rejected HMRC's submission that employers can decide which of two employees are to suffer the tax charge.

It follows that Ms Baylis is not liable to tax on VWML's payment of her mother's care home fees in 2009/2010 and 2010/2011 which potentially involved extra tax was £9,649.95 for the first year and £27,533.22 for the second.

The remaining part of the assessments under appeal related to the following sums said to have been paid by VWML to settle certain personal expenses incurred by Ms Baylis:

(1) credit card payments of £1,411 for 2009-10 and £6,475.10 for 2010-11; and

(2) other third party payments of £3,000 for 2010-11.

Ms Baylis's case was that any such personal expenses were covered by dividends already included in her tax return. The tribunal judge agreed with Ms Baylis.

HMRC seems to have made a real mess of preparing for this case and HMRC should hang its head in shame at its failures.

VWML runs a marina business on the river Thames. It owns substantial moorings as well as four acres of land. Mr Baylis was its Managing Director from 1977 until December 2011. The company's shareholding was complex, involving trusts and seven classes of shares, labelled using the letters of the alphabet ("alphabet shares"). The use of alphabet shares allowed VWML to pay differential dividends to each class of shareholder.

The other daughter was a qualified chartered accountant who trained with one of the large accountancy firms. In the late summer of 2011 she began working at VWML as an unpaid administrative assistant. Ms Baylis was concerned that his other daughter would want to take a financial role within VWML. Mr Baylis had a heart attack and was an octogenarian. On 2 December

2011, Mr Baylis stepped down as managing director and resigned as Company Secretary. On the same day, his other daughter was appointed company director, managing director and Company Secretary.

An acrimonious legal battle between the two half-sisters began in December 2011, after Ms Baylis became ill. On 4 December 2012, VWML's directors signed a disclosure report to HMRC ("the Disclosure Report"). The company was allocating the care home fees to Ms Baylis.

HMRC seem to have failed to test the credibility and strength of the evidence presented. The case is of interest to tax practitioners because it looks at the law of agency in some detail before concluding that Ms Baylis acted as the company's agent when she signed the care home contract.

http://www.bailii.org/uk/cases/UKFTT/TC/2016/TC05454.html

4. Taxpayers are entitled to rely on professional advice and not be penalised

Carrasco & Anor v Revenue and Customs [2016] UKFTT 731is an interesting decision because it considers whether a couple who erred in their tax return had taken reasonable care but made a mistake. Mrs Carrasco had inherited in June 1988 from her mother 33 Smith Terrace, Chelsea, London.

The property had been let before Mr and Mrs Carrasco , accompanied by teenage children and family pets, moved into the property on 29 June 2010 and resided there until 22 July 2010. Acting upon the advice of their retained accountants the appellants executed a principal private residence election on 23 April 2012 to the effect that the subject property was their principal private residence until 22 July 2010.

Acting upon the advice of their then accountant and tax adviser the couple timeously filed self-assessment returns in which they each declared their appropriate capital gains, but reduced those gains by excluding from the computation the gain attributable to the rise in property prices over the immediately preceding three year period.

HMRC undertook an enquiry into the appellants' capital gains tax returns and disallowed the reduction referable to the principal place of residence deduction. HMRC issued Penalty Notice to the first named appellant in the sum of £16,918.78p and a Penalty Notice to the second named appellant in the sum of £6647.58p.

Mrs Carrasco disclosed that at or about the time when the relevant self-assessment returns were being completed she was undergoing a course of chemotherapy. She said that she placed reliance upon her professional tax advisers and accountants. This case becomes interesting because of the judgement at paragraph 21 which states:

"It is reasonable to start from the position that tax laws and tax rules in this country are generally complex and often convoluted. There can be no doubt that a person might need to rely upon the expertise of an accountant or other professional adviser who has (or who professes to have) expertise in tax matters when filing a tax return, whether that return relates to income tax, capital gains, corporation tax or a multitude of other individual taxes. The average man in the street cannot reasonably be expected to have a working knowledge of tax legislation, notwithstanding the artificial legal presumption that individuals are presumed to know the law. Whilst many individuals might have a working knowledge of the most basic principles attaching to the better-known taxes, it is not to be expected that such persons will have a detailed working knowledge of the intricacies surrounding even the most common taxes, such as income tax, VAT and/or capital gains tax."

This decision is not a precedent but might be a helpful persuasive authority in appeals against penalties. There is overwhelming evidence that HMRC are now seeking penalties in cases where it is

not appropriate. Tax is complex and mistakes which are innocent should not be penalised. Paragraph 25 states:

"In our judgement when a person seeks appropriate professional advice from somebody who is a professed expert in the applicable discipline, it will almost always be reasonable for the person who has sought out such advice to rely upon that advice provided only that that person has selected a seemingly competent professional adviser, unless there are factors to the knowledge of the recipient of the advice which indicate to him/her that it ought not to be relied upon. In our judgement such factors would have to be reasonably obvious rather than subtle or such as might only be picked up by a fellow professional"

The appeal against the penalty succeeded.

http://www.bailii.org/uk/cases/UKFTT/TC/2016/TC05460.html

5. Avoidance: AAT and other give guidance

Tax avoidance is an emotive topic. I struggle personally with where the watershed lies between sensible tax planning to achieve the commercial objective and egregious unacceptable avoidance. That watershed is ill defined and poorly understood but what is clear is that an adviser should help a client navigate the complexities of tax legislation. A failure to advise a client of how to achieve the commercial objective and claim all the available reliefs might render the advisor liable to pay compensation to the client.

The seven major professional bodies including AAT have published guidance on Professional conduct in Relation to Taxation (PCRT). Members should not engage or encourage tax avoidance activity. HMRC has endorsed the code. The new PCRT will come into effect during March 2017 and includes five new standards that will prevent the creation, promotion or encouragement of tax avoidance schemes.

There is a lot of helpful guidance in this document including how to deal with disclosures and how to help client correct errors. The 55 pages of PCRT must be required reading for every member.

https://www.tax.org.uk/sites/default/files/PCRT%20Effective%201%20March%202017%20FINAL.pdf

Not surprisingly, the government and HMRC are delighted with the development.

https://www.gov.uk/government/news/updated-code-of-conduct-will-discourage-number-of-avoidance-schemes

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There will be a general tax podcast updating AAT members on recent developments and decisions available on the website on 31 December 2016.