Tax update 31 January

In this edition of the tax update we look at:

1. buying and selling listed shares at a loss held to be trading
2. electronic filing deadline of 31 January
3. interesting administrative changes in tax
4. peer to peer interest payments may be made gross
5. Ministry of Justice fee rates for tax tribunal

1. Buying and selling listed shares at a loss held to be trading

The latter half of 2015 saw a considerable fall in the stock market. The First- tier Tribunal decision in Ali v Revenue and Customs (INCOME TAX/CORPORATION TAX : Losses) [2016] UKFTT 8 will be an interesting and welcome development for many taxpayers. It is a decision about which HMRC will not like.

Mr Akhtar Ali was a successful pharmacist who had also derived income and gains from high frequency buying and selling listed shares. When this activity incurred losses, he claimed relief for the losses incurred against his profits from the pharmacy. HMRC opened an enquiry and disallowed the losses from share transactions and then assessed not only the additional tax but also assessed a penalty alleging that Mr Ali's returns had been submitted without taking reasonable care.

Mr. Ali appealed against the following (set out, for convenience, in tabular form – a blank box indicates that the item in question is not applicable to the tax year in question):

Year	Additional tax per closure notices issued on 22 September 2014 under s28A(1) & (2) Taxes Management Act 1970	Penalty assessment notified on 12 September 2014 under Schedule 24 Finance Act 2007	Penalty determination issued on 22 September 2014 under s95(1)(a) Taxes Management Act 1970
2006-07			£3,258.00
2007-08			£2,806.00
2008-09		£9,176.61	
2009-10	£24,486.40	£3,672.96	
2010-11	£115,751.80	£17,362.77	
2011-12	£34,837.00	£5,225.55	
2012-13	£103,568.22	£15,535.23	

The amounts of loss disallowed by HMRC were £61,216 in 2009/10, £273,264in 2010/11, £69,674 in 2011/12 and £243,770 in 2012/13.

Now if I pause at this point, it is to declare that I remember the assurances given by HMRC during the consultation process that a mistake would not be penalised. Tax is complex and mistakes are inevitable. Case law is clear that a mistake in interpreting complex tax law is not negligence or carelessness so long as the decision taken by the taxpayer was reasonable even though incorrect. Therefore was Mr. Ali's claim to relieve the losses incurred from his share dealing activities reasonable?

For the tax years up to 5 April 2005 the appellant's tax returns dealt with the profits or losses from his share activities under capital gains tax rules. He described his share activities in the period from 1995 to 2002 as "investing" in shares, as he would buy shares and hold them for a few months. His early losses gradually turned to profits. In 2000, he made around £200,000. This increased his confidence and he gradually increased the scale of his activities with regard to buying and selling shares. During this period he started to "trade options", using one of the strategies he had learned. He described himself as gradually building up expertise in buying and selling shares.

The appellant stated that around 2005 he decided to become a “day trader” by buying and selling shares whose prices were moving rapidly on the market. He had access to “live” prices through a software system called “Synergy”. He said he undertook this activity on a commercial basis, to make a profit. At this stage, he did not enter into derivatives such as call options to hedge his positions; rather he bought and sold shares within short time periods. He began employing locums at his pharmacy to free up his time for “day trading.” He carried on his activities in an upstairs office in the same building as the pharmacy.

Following a VAT visit to his pharmacy in April 2006 HMRC wrote a letter, dated 11 August 2006 which included the following paragraph:

> “2. Dealing in Shares
> You have advised that in the past you have dealt and made substantial amounts of money from dealing in shares. As you are a sole proprietor this income would need to be declared through your VAT return would you continue to make any money this way. Trading in shares is actually Exempt from VAT and as such should you continue to trade and incur expenses in relation to this you may not be able to recover VAT on some of your expenses. If you continue to trade in this manner you would be deemed to be a Partially Exempt company for VAT purposes and would be required to carry to quarterly and annual Partial exemption calculations …”

In many cases, Mr. Ali would hold the shares for only a few minutes or hours. His dividend income was negligible. The total number of transactions carried out by the appellant in six of the seven tax years in question was as follows:

Year	Yearly	Weekly (average)	Daily (average)
2006-07	980	21	4
2007-08	950	21	4
2008-09	1,370	30	6
2009-10	1,825	40	8
2010-11	2,320	50	10
2011-12	775	17	3

In olden days, one could be confident that in all dealings with the Inland Revenue, the officers would act reasonably and exercise reasonably sound judgement. Assurances given at the consultation stage would be reliable and this is especially important regarding the penalty regime to be found in Schedule 24 of FA 2007. I was appalled that HMRC had assessed penalties in this case. That was unacceptably poor judgement on the part of the officer(s) responsible. The problem is that there is no sanction against the misconduct of these officers whose lack of judgement and misconduct amounts to maladministration.

It was entirely appropriate that Mr. Ali’s return be challenged and the outcome of the current year loss offset remains speculative because a decision of the FTT is not legal precedent and would only be persuasive if used in argument in a similar case. However, irrespective of whether Mr. Ali’s claim for loss relief was right or wrong, he had a reasonable ground for making that claim and a penalty was never eligible. The officers responsible for the penalty assessment are guilty of maladministration and at the very least they require further training. HMRC need to consider this case carefully and take steps to ensure that the maladministration does not recur.

Experienced tax practitioners would recognise that many of the badges of trading were present in relation to Mr. Ali’s share dealing activity. Unlike Salt v Chamberlain (summarised below), Mr Ali was dealing in thousands of transactions in each year. In principle, HMRC will challenge loss claims if HMRC have reasonable grounds for considering that the transactions were speculation or gambling. Cases considered in argument included:

Graham v Green [1925] 2 KB 37, [1925] AER 690 – gambling is an irrational activity the profits from which are not liable to income tax
Cooper v Stubbs [1925] 2 KB 753 - speculating on cotton futures was not trading but the profits were taxable under Case VI
Lewis Emanuel & Son, Ltd v White (1965) 42 TC 369 - a company's activities are presumed to be trading and in this cases loses on share dealing were allowed
Salt v Chamberlain [1979] STC 750 - Losses on 200 speculative transactions incurred over a period of years by an individual were not allowed
Cooper v C & J Clark Ltd [1982] STC 335 – a loss incurred in dealing in securities by a company was incurred in a separate trade and the loss allowed
Wannell v Rothwell [1996] STC 450 – the loss incurred in dealing in shares and futures was not a trading loss because the individual was disorganised and the activity lacked the framework to be trqading
Dr K M A Manzur v HMRC, - a retired doctor was denied loss relief on his loss making share transactions even though he made over 200 deals in a year

Hindsight suggests that Mr Ali lacked skill but the tribunal found as a fact that he conducted the share dealing activity in a commercial way trying to make a profit. He was trading and the loss was allowable against his other income. That is a finding of fact for which the tribunal has concluded so the decision should be final.

2. Electronic filing deadline - 31 January

I hope that all my readers had a relaxing approach to the deadline and no problems. In the real world, the unexpected can happen and last minute provision of necessary information can lead to delays.

I suggest that if you have any clients who were dilatory, a review of the reasons for the delay might be worthwhile. If the client has no reasonable excuse for the delay or has a history of persistent delay, now maybe a good time to consider suggesting to the client that they find another tax adviser.

HMRC record and compare the filing performance of tax advisers. An adviser who has an unusually high number of late filing clients will be marked down compared to the norm. Your reputation is precious and does not need to be damaged by dilatory clients so a review may be worthwhile.

3. Interesting administrative changes in tax

While noting (with some surprise) that Lin Homer had been made a Dame in the honours list, I also noted that it was announced she is leaving her post as CEO of HMRC in April 2016. I wish her well for the future.

She inherited an organisation which was failing performance standards repeatedly and any reasonable person would recognise that she faced a difficult task if her leadership was to achieve improvements. I wish I could congratulate her on successfully improving performance standards but it seems (to me at least) that there is still a very long way to go before HMRC performance standards get anywhere near approaching an acceptable level.

Complaints have the potential to be addressed and resolved by the adjudicator and I note also that Judy Clements OBE will be replaced as adjudicator in April 2016. Helen Megarry will 'succeed' as the Independent Adjudicator for HMRC, the Valuation Office Agency and the Insolvency Service. I wish Ms Megarry well in her new role and I hope that she can criticise constructively so that necessary improvements to HMRC performance standards are achieved.

4. Peer to peer (P2P) interest payments may be made gross

In the period before the government makes any necessary changes to the legislation, interest payments made on P2P loans may be made without deduction of tax.

This will apply to interest payments made by:

- a UK borrower to a UK P2P platform
- a UK P2P platform whoever made to
- any intermediary to or from a UK P2P platform

In each case the P2P platform must be authorised by the Financial Conduct Authority (including interim authorisation).

5. Ministry of Justice New Fee rates for Tax Tribunals

Who pays to correct HMRC's mistakes? The Ministry of Justice has published the response to the consultation it issued in 2015 and the proposals to introduce new fee rates for tax tribunals. In my view, this is wrong in principle especially when HMRC make so many mistakes and their review process fails to work properly. Far too many appeals get to the tribunal which should have been settled by negotiation and sensible discussion with HMRC.

In the case summarised above (Mr. Akhtur Ali) HMRC assessed a penalty and in my view that was maladministration. Mr. Ali should be entitled to damages from HMRC. In the future, someone in similar circumstances to Mr Ali will have to pay a fee to go to an appeal tribunal to correct HMRC's mistakes.

Tax Chamber	**Current**	**New**
First-tier Tax Chamber		
Appeals against Fixed Tax Penalties of £100 or less	No Fee	£20
Paper – Issue	No fee	£50
Paper – Hearing	No fee	No fee
Basic – Issue	No fee	£50
Basic – Hearing	No fee	£200
Standard – Issue	No fee	£200
Standard – Hearing	No fee	£500
Complex – Issue	No fee	£200
Complex – Hearing	No fee	£1,000
Upper Tribunal Tax and Chancery		
Permission to appeal – Issue	No fee	£100
Permission to appeal – Hearing	No fee	£200
Appeal – Issue	No fee	£100
Appeal – Hearing	No fee	£0

The new fee rates can be found at page 22 onwards but note that an appeal against the fixed penalty of £100 will cost a fee of £20, as well as the stress and management time.

Derek Allen
31 January 2016
Set your diaries for the next edition of the general tax update which will be published on 28 February 2016