Tax Updates – January 2023

Highlights

- The government has launched a consultation on proposed changes to R&D relief, including proposals to merge the SME and RDEC schemes.
- HMRC resourcing issues continue, with staff being transferred to work on Brexit and Covid-19 while billions of pounds of tax go uncollected.
- At the same time, IHT investigations are on the rise and HMRC has launched two new campaigns targeting earnings from online marketplaces and non-resident companies that own UK residential property.
- The Tribunal has been busy, with a few interesting decisions issued on EIS, interest for official error and the VAT zero-rating of healthy snack bars.

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1. Upcoming hearings

CA: *Volkerrail Plant Ltd v HMRC* (Case ID: CA-2022-001053/54) – Hearing date: 8 February 2023 – Group relief appeal regarding whether s. 403D(1)(c) ICTA constitutes an unlawful restriction on EU freedom of establishment.

UT: *Invicta Motors Ltd v HMRC* (Case ID: UT-2022-000028) – Hearing date: 27 and 28 February 2023 – Whether a s. 85 agreement prevents new claims being brought – *res judicata* and abuse.

UT: *GE Financial Investments v HMRC* (Case ID: UT-2021-000165) – Hearing date: 27 or 28 February, or 1 March 2023 – Residence and US DTA relief.

CA: *London Luton Hotel BPRA Property Fund LLP v HMRC* (Case ID: CA-2021-000087 and 000738) – Hearing date: 13 March 2023 – Business Premises Renovation Allowance.

CA: *British Telecommunications plc v HMRC* (Case ID: CA-2021-000700) – Hearing date: 21-23 March 2023 – Restitution claim relating to bad debt relief.

UT: *Laing O'Rourke Services Ltd v HMRC; HMRC v Willmott Dixon Holding Ltd* (Case IDs: UT-2021-000196 and UT-2022-00035) – Hearing date: 20-22 March 2023 – Payments made to employees under a car allowances were earnings for NICs but not 'relevant motoring expenditure' and the para 7A disregard not available.

UT: *George Mantides Limited v HMRC* (Case ID: UT-2020-0122) – Hearing date: 4, 5 or 6 April 2022 – IR35 hypothetical contract interpretation.

UT: *United Grand Lodge of England v HMRC* (Case ID: UT-2022-00009) – Hearing date: 24-25 April 2023 – VAT exempt supplies relating to membership fees charged to Freemasons.

UT: *Lancashire John v HMRC* (Case ID: UT/2021/00049) – Hearing date: 8, 9 or 10 May 2023 – Transfer of Assets Abroad appeal.

CA: *Royal Bank of Canada v HMRC* (Case ID: CA-2022-000812) – Hearing date: 17 May 2023 – Taxation of oil royalties received by overseas bank and applied to outstanding debt of insolvent borrower.

2. Legislation and consultations

Legislation – Autumn Finance Bill: The Finance Act 2023 (originally entitled "Finance (No. 2) Bill 2022") received Royal Assent on 10 January 2023. As a reminder, the bill covers the tax rate, threshold and allowance changes announced at the Autumn Statement.

Draft legislation - SDLT: All remaining stages in the House of Lords for the Stamp Duty Land Tax (Temporary Relief) Bill took place on 18 January. The date for Royal Assent has not yet been set. This is a bill to temporarily reduce the amount of SDLT chargeable on the acquisition of residential property. It has already been given provisional statutory effect under the Provisional Collection of Taxes Act 1968.

Draft legislation – EU law: The Retained EU Law (Revocation and Reform) Bill had its first reading in the House of Lords on 19 January, but no date has yet been set for its second reading.

Regulations – Mandatory Disclosure Rules: On 16 January 2023, the International Tax Enforcement (Disclosable Arrangements) Regulations 2023 were made. Arrangements entered into on or after 28 March 2023 must be reported to HMRC under these rules. DAC6 regulations will be repealed at the same time and therefore any arrangements entered into on or after that date will not be reportable under DAC6. However, the DAC6 reporting portal will remain open for one month to allow arrangements entered into before 28 March to be reported under DAC6. The current DAC6 guidance (which is relevant to MDR for hallmarks D1 and D2, i.e. arrangements designed to undermine tax reporting under the CRS and transparency rules) will be updated where necessary to reflect these new regulations.

Order – Second-hand vehicles: The Value Added Tax (Margin Schemes and Removal or Export of Goods: VAT-related Payments) Order 2023 has been made, introducing a VAT-related payment scheme which will apply to second-hand motor vehicles from 1 May 2023. The scheme allows businesses removing or exporting used motor vehicles to Northern Ireland or the EU for resale to claim a VAT-related payment from HMRC. HMRC has also published guidance on the scheme.

Explanatory notes – ViDA: The Treasury has published explanatory notes (here, here and here) on the potential impact of the VAT in the Digital Age (ViDA) EU proposals on Northern Ireland. The notes explain that the UK may need to develop new reporting structures in light of the ViDA proposals, given that Northern Ireland VAT rules for supplies of goods are aligned with the EU.

Consultation – R&D: On 13 January 2023, the government launched a consultation to simplify the UK's R&D tax relief system. It will be open until 13 March 2023 and sets out proposals on how a single scheme could be designed and implemented. This would replace the two R&D tax relief schemes currently in place, the Research and Development Expenditure Credit (RDEC) and the small or medium enterprise relief (SME). It is currently the Government's intention that, if implemented, the new scheme will take effect from 1 April 2024.

Consultation outcome – Agents: A summary of responses has been published by HMRC following a consultation on raising standards in tax advice. As a result of the feedback received, the government will take steps to improve transparency in the repayment agent market and protect customers, including requiring repayment agents to register with HMRC and strengthening checks on agents. HMRC is also planning to introduce legislation to change the way repayment agents are paid in order to better protect customers. This has also been covered by the FT.

EU – Administrative cooperation: The EC has published a proposal to amend existing EU rules on administrative cooperation and combatting fraud in the field of taxation, in order to strengthen the tools tax administrations have at their disposal. It is estimated that in 2020 the EU lost €93 billion in VAT revenue due to tax fraud, tax evasion and tax avoidance. A public consultation is planned for the first quarter of 2023.

International Tax Reform — Pillar Two: On 9 January 2023, the International Accounting Standards Board (IASB) formally proposed amendments to IAS 12 Income Taxes. The proposed amendments aim to provide temporary relief from accounting for deferred taxes arising from the implementation of the OECD Pillar Two model rules. The Exposure Draft International Tax Reform – Pillar Two Model Rules is open for comment until 10 March 2023. The IASB aims to finalise any amendments in the second quarter of 2023, subject to comments on the Exposure Draft.

Announcement - HMRC performance in 2021/22: The Public Accounts Committee (PAC) has reported that HMRC is still not deploying the resources required to maximise the tax revenues it collects or provide an acceptable level of customer service. £42 billion is owed in unpaid tax, and HMRC is failing to collect around 5% of the tax it is owed each year. HMRC has two months to respond to the report, including setting out its plans to raise customer service levels and the level of investment in compliance needed to reduce the tax gap. The FT has also reported on this.

3. HMRC guidance

VAT penalties: HMRC has published guidance on the new VAT penalty and interest regime, which applies to VAT accounting periods starting on or after 1 January 2023:

- Late payment interest – Late payment interest will be payable (at base rate plus 2.5%) on the amount outstanding from the first day the payment is overdue. If more than 15 days late, a late payment penalty will also apply.

- Penalty points and penalties for late VAT returns – Late submission penalties apply on late VAT returns based on a penalty points-based system.

- Repayment interest on VAT credits or overpayments – Repayment interest replaces the repayment supplement and is paid at the base rate minus 1%, with a minimum rate of 0.5%. Taxpayers are only eligible for repayment interest on overpayments that relate to an amount due to HMRC.

- How late payment penalties work – The taxpayer will get a first late payment penalty if the payment is 16 or more days overdue. Between 16 and 30 days late, this is calculated at 2% of the VAT owed at day 15. After it has been overdue for 31 days or more, it is calculated on 2% of what is outstanding on day 15 plus 2% of what is outstanding on day 30. There is a second late payment penalty at 31 days or more overdue, calculated at a daily rate of 4% per year.

- Removing penalty points received – Penalty points expire 24-25 months post-issue. However, points can be removed by having a complete period of compliance and submitting all returns on time, or by submitting all outstanding returns for the previous 24 months.

Option to tax: HMRC has announced that from 1 February 2023, it will stop issuing option to tax notification receipt letters. Instead, taxpayers will receive an automated response to their email. Notifications sent other than by email will not get an acknowledgement.

Agents: HMRC has published a policy paper on its approach to working with agents. The paper outlines how HMRC supports and assists agents, including by sending introductory emails, providing webinars and running a dedicated helpline.

4. HMRC spotlights and nudge letters

Online marketplaces: HMRC has launched a One to Many letter campaign targeting earnings from sales on online marketplaces and from creating content on digital platforms. These letters are driven by third party information showing taxpayers' trading activity. Recipients are asked to complete a 'Certificate of Tax Position' within 30 days.

ATED: HMRC has launched a letter campaign targeting non-resident companies that own UK residential property and that HMRC considers may have incorrectly stated the bands in their returns. The letters are accompanied by a Certificate of Tax Position and a Notice of Intention to Disclose. This is linked to HMRC's campaign to tackle non-compliance connected with offshore corporates owning UK property.

Avoidance schemes: As part of its crackdown on tax avoidance promoters, HMRC has published the details of five more tax avoidance schemes which seek to disguise remuneration.

CCO: HMRC has published an FOI release on the number of live Corporate Criminal Offences (CCO) investigations. HMRC currently has 9 live CCO investigations underway and a further 26 live opportunities under review spanning 11 different business sectors. HMRC states the legislation is succeeding in driving behavioural change.

5. Recent decisions – Direct tax

EIS: Hoopla Animation Ltd v HMRC [2023] UKFTT 24 (TC) (For the taxpayer: Andrew Chambers and Adrian Wilkins. For HMRC: Ruth Hughes and Tomos Rees.) – The FTT dismissed an appeal against HMRC's decision not to allow the taxpayer to issue compliance certificates under the enterprise investment scheme (EIS) on the basis that there were "disqualifying arrangements" (i.e. the taxpayer had paid a substantial part of the money raised by the share issues to one of the parties to the arrangements).

Transfer of business: 2 Green Smile Ltd v HMRC [2023] UKFTT 15 (TC) (For the taxpayer: Michael Firth instructed by Silver Levene LLP.) – The FTT had to decide on the date of a de facto transfer of a dental business from a partnership to a company, as that impacted on a claim for deduction for amortisation in relation to goodwill. The FTT held that the transfer took place on the date the parties formed a settled intention to transfer the whole business, by reference to correspondence and the recording of goodwill in the company's accounts.

Gold bullion scheme: Wired Orthodontics Ltd v HMRC [2023] UKFTT 17 (TC) (For the taxpayer: Andrew Thornhill KC instructed by Levy and Levy Solicitors. For HMRC: Adam Tolley KC and Charles Bradley.) – This appeal concerned a tax avoidance scheme whereby gold bullion was paid to directors by a company via an EBT. The FTT held that the scheme failed, as the gold bullion constituted "money or money's worth" and was taxable as earnings.

Employee shares: Gain Capital Ltd v HMRC [2023] UKFTT 61 (TC) (For the taxpayer: Christopher Stone instructed by RSM. For HMRC: Georgina Hirsch.) – The FTT held that gifts of shares to ex-employees constituted earnings from their employment under ITEPA 2003.

Deductible expenses: Mainpay Ltd v HMRC [2023] UKFTT 16 (For the taxpayer: Michael Firth instructed by The Independent Tax and Forensic Services LLP. For HMRC: Sadiya Choudhury.) – The FTT held that travel and subsistence expenses paid by an umbrella company to contracted workers supplied to employed agencies were taxable, as the workplaces attended by the workers during their assignments were permanent workplaces.

IR35: S&L Barnes Limited v HMRC [2023] UKFTT 42 (TC) (For the taxpayer: Michael Collins instructed by Markel Tax. For HMRC: Bayo Randle.) – The FTT held that IR35 did not apply to a personal service company which supplied the services of a rugby commentator to Sky TV.

Penalties: Nicolas Burley v HMRC [2023] UKFTT 59 (TC) (For the taxpayer: David Yates KC instructed by PwC.) –The taxpayer argued that HMRC had failed to notify late payment penalties to him. The FTT found that the penalties had been properly notified and that the taxpayer was aware of this, particularly as he had only raised non-receipt at a late stage in the dispute.

Reasonable excuse: Thomas Cruise v HMRC [2023] UKFTT 41 (TC) – This was an appeal against penalties for filing a self-assessment tax return late. The FTT found that the taxpayer had no reasonable excuse as he had failed to read the notice to file and notices of penalties issued electronically to him via his personal tax account.

6. Recent decisions – Indirect tax

Interest for official error: HBOS PLC & Lloyds Banking Group PLC v HMRC [2023] UKUT 13 (TC) (For the taxpayer: Amanda Brown KC of KPMG. For HMRC: Eleni Mitrophanous KC.) – The UT held that interest on repayment claims should run from the date the claims would have been made, had there not been a legislative error arising from non-compliance with EU law. The UT found that the incompatibility of a domestic statute with EU law constitutes an error on the part of HMRC.

Confectionery: WM Morrison Supermarkets PLC v HMRC [2023] UKUT 20 (TC) (For the taxpayer: Valentina Sloane KC instructed by Deloitte. For HMRC: Howard Watkinson.) – This case concerned whether Nakd and Organix bars should be zero-rated as cakes (the appellant's case) or standard-rated as confectionery (HMRC's case). The UT remitted the appeal to the FTT on the basis that, in reaching its decision, the FTT had failed to consider the healthiness of the product and the absence of ingredients associated with traditional confectionery.

Discounted payments: TalkTalk Telecom Ltd v HMRC [2023] UKFTT 12 (TC) (For the taxpayer: Andrew Hitchmough KC and Quinlan Windle instructed by PwC. For HMRC: Kieron Beal KC and Andrew Macnab.) – The FTT held that there is a reduction in consideration only where a prompt payment discount is actually taken up by a customer, not just offered. Victor Cramer of Stewarts has also commented on this decision for Tax Journal.

Attribution of VAT to business activity: Ince Gordon Dadds LLP v HMRC [2023] UKFTT 44 (TC) (For the taxpayer: Michael Firth.) – This case related to input tax claimed on a flotation on the Alternative Investment Market, which was effectively a reverse takeover. The acquirer sought to recover input tax via the VAT group representative member on services received in relation to the takeover. The FTT dismissed the appeal and held that there was no direct and immediate link with taxable supplies, and the costs were also not general overheads.

Appealable decision: Isle of Wight NHS Trust v HMRC [2023] UKFTT 23 (For the taxpayer: Zizhen Yang instructed by Berthold Bauer VAT Consultants Ltd. For HMRC: Jennifer Newstead Taylor.) – The taxpayer appealed against a reply from HMRC in relation to correspondence on the VAT liability of supplies of locum doctors to NHS hospitals. HMRC applied to have the appeal struck out as it had not issued an appealable decision. The FTT held that the letter was an appealable decision, as it clearly set out the issues faced by the taxpayer and HMRC's technical position, and expressed a "concluded view".

Late appeal: Golden Grove Trust v HMRC [2023] UKFTT 27 (TC) (For the taxpayer: Robert Warne of Crowe UK LLP.) – The FTT refused an application for permission to bring a late appeal. Although the appellant's adviser was primarily responsible for making the appeal and had failed to do so, the taxpayer had also failed to follow up with its advisers.

Late reinstatement application: Maqsood Hussain t/a Nisa Local v HMRC [2023] UKFTT 40 (TC) – The FTT refused the taxpayer's application for late reinstatement of a withdrawn appeal. The taxpayer had given notice of withdrawal to the Tribunal, who in turn notified HMRC, and tried to argue that s. 85 of VATA 1994 only took effect where the taxpayer directly notified HMRC. The FTT held that indirect notification was sufficient for the purposes of s. 85.

7. Media

HMRC resources: The FT has reported that 2,300 HMRC staff (around 10% of tax compliance officers) have been transferred to work on Brexit and Covid-19 schemes, meaning that billions of pounds of tax are being left uncollected. At the same time, Jim Harra has admitted that the Covid fraud task force is "not the best value" for money, as it only expects to recover £1.1bn of an estimated £4.5bn lost through pandemic support schemes.

IHT: According to the FT, the amount of inheritance tax (IHT) collected by HMRC following investigations has increased by one fifth year on year, up from £254m in 2020-21 to £326m in 2021-22. HMRC is allocating more resources to IHT investigations due to the rising value of assets and the sums at stake.

Windfall tax: Several energy groups have indicated that they expect be impacted by UK and EU windfall taxes on fossil fuel companies. Shell expects its 2022 earnings to be hit by almost $2.4bn and Total by $2.1bn. Harbour Energy is also planning to cut jobs in response to the increase in windfall taxes.

Net zero: The ICAEW Tax Faculty has commented on the government's recent net zero review and what more can be done from a tax policy perspective to achieve net zero. In particular, the Faculty has recommended that support for green technology should go beyond inclusion in the R&D scheme and that, while tax reliefs are one option, loans and grants might be a better idea given that many businesses are currently suffering cash flow issues.

VAT registration: Tax Policy Associates have reported that around 26,000 SMEs are holding back their growth to keep their revenues below £85,000 in order to avoid meeting the VAT registration threshold. Tax Policy Associates recommend either removing the cliff-edge and phasing in VAT above a certain threshold, or introducing a rebate system.

FINs: HMRC has published a report on the use of Financial Institution Notices (FINs) and their effectiveness in improving HMRC's international information request response times. This includes a number of updates, including a reversal of a previous proposal to collect customers' location by reference to the IP data collected when customers access their online or mobile accounts. CMS have commented on this development.

Tax relief statistics: HMRC has published a report on the costs of non-structural tax reliefs, i.e. reliefs designed to encourage certain types of individuals, activities or products to achieve economic or social objectives (e.g. CGT private residence relief, VAT zero rating of food). The total cost increased by £30bn (18%) year on year, although tax receipts also increased by over 20% in the same period. The ICAEW has summarised the main findings of the report.

VAT statistics: HMRC has published annual UK VAT statistics for 2021-22. Total VAT receipts increased by 55% year-on-year, having dropped significantly in previous years due to the VAT payment deferment policy, the impact of the Covid-19 pandemic and the temporary reduced hospitality rate.

Tax compliance: In a recent PAC session, Jim Harra answered questions on tax compliance which revealed that calls to the self-assessment helpline were a third higher in January than they would normally be at this time of year. There are also higher levels of tax non-payment by small businesses than pre-pandemic, and HMRC are aiming for a record compliance yield of £36bn.

Video Games Tax Relief: According to a recent report by TaxWatch, Video Games Tax Relief cost £197m in 2021-22, which is five times as much as forecast when the relief was introduced in 2014. Although the relief was set up to support independent British developers, HMRC's statistics show that large firms benefit from it the most.

Future of VAT: EY have published their "Future of VAT in the UK" report, which explores what might be next for VAT based on research and conversations with businesses. The key findings are that the government should review and modernise the VAT system and share a clear roadmap for real-time reporting by 2023.

Electronic invoicing: The OECD has published the "Tax Administration 3.0 and Electronic Invoicing" report, which looks at the current state of electronic invoicing based on a global survey by reference to case studies from countries that have implemented electronic invoicing.