# A few points of interest

This article sets out a few recent points which the author has found of interest.

## A recent case of "time travel"

The recent case of *Bainbridge v Bainbridge* [2016] EWHC 898 (22 April 2016), in which the author acted for the Claimant, shows that it is sometimes possible to travel backwards in time for general law and, in principle also for tax law, purposes. Partners in a farming partnership had transferred land into a discretionary trust giving rise, unexpectedly for the partners, to capital gains tax ("disposal 1"). Moreover the trustees had sold some of that land to acquire new land ("disposal 2", this disposal having been made by the trustees). The trustees leased all of the land they held back to the partners who used it in their trade. The Court agreed that disposal 1 could be set aside under the principles in *Pitt v Holt* [2013] UKSC 26. The Court accepted that disposal 1 could be set aside even where the transfer to be set aside related to land which had been sold by the trustees and which could not be returned to the partners. Instead what would be returned to the partners was the proceeds of sale and anything which those proceeds of sale had been used to acquire, i.e. the new land acquired.

How, after the setting aside (which had retrospective effect), were the various events to be analysed under the general law, taking into account the setting aside? The Chancery Court Master said this:

> "It seems to me, therefore, that the right way to analyse what must be considered in the present case as having occurred, once the transfers into trust are treated as never having happened, is that the original owners have retained [the land transferred into the trust], but that the sales (actually by the trustees) are to be imputed to those original owners, as also is the use of the proceeds (in part) to invest in the new land, and (in part) to pay stamp duty, costs and other liabilities of the business."

One consequence of this is that the farmers should be entitled to rollover relief on disposal 2 as they were deemed to have been using the land sold for the purposes of their trade and so to have used the new land acquired with the proceeds. This is an interesting illustration of travelling into the past to re-do things as they ought to have been done, which should be effective for tax purposes.

**Corporation tax repayments without a claim**

Where tax has been suffered at source a return showing the overpayment will cause a refund to be due without the need for a claim. The *Higgs* judicial review ([2015] UKUT 0092), in which the author acted for Mr Higgs, established that, in a case where tax had been suffered at source, no time limits applied to prevent the taxpayer filing a tax return triggering a refund of tax. This was a case where a notice to deliver a tax return had been served but had not been complied with for many years. In particular, the 4 year time limit in s34 TMA 1970 did not apply to *self*-assessments, as opposed to assessments *by* HMRC.

This is now being overridden by new s34A FA 2016, introduced by FA 2016 to deal with the *Higgs* decision. A 4 year time limit also applies to claims.

However, the TMA provisions are mirrored in the Schedule 18 FA 1998 rules for companies (see also *Bloomsbury Verlag v The Commissioners for HMRC* [2015] UKFTT 660). The equivalent of s34 TMA 1970 in the corporation tax context (paragraph 46 Schedule 18 FA 1998) also does not include self-assessments. This is unaffected by FA 2016. The equivalent of s59B(1) which triggered the right to a repayment in *Higgs* without a claim is mirrored, for corporation tax purposes, in s59D(2). The position obtained in *Higgs* (where the 4 year time limit was held inapplicable) would therefore appear to continue to apply for corporation tax purposes since there is no equivalent to s34A for corporation tax purposes.

**Continuing relevance of Timpson v Moyes under the new remittance rules**

HMRC say in their Remittance Manual (at para 33140): "T, a remittance basis user, donates an amount of money to a Battersea Dogs Home, a UK charity, by making a payment direct to the charity from his US bank account which contains his relevant foreign income. There has been a direct remittance of T's income into the UK; it does not matter that he or any other relevant person does not benefit personally from the money." This is based on the old case of *Timpson v Moyes*.

In the author's view this is not correct (as also pointed out by James Kessler QC in his "Taxation of Foreign Domiciliaries"). In order for there to be a

remittance, the property in the UK must be property "of" a relevant person when it is in the UK (unless it is actually the income or gains in question). A bank transfer does not involve the property of the transferor being in the UK. The correct analysis of a bank transfer is set out in the House of Lords case of *Reg v Preddy* [1996] AC 815 which concerned mortgage fraud. Lord Goff said this:

> "The question remains however whether the debiting of the lending institution's bank account, and the corresponding crediting of the bank account of the defendant or his solicitor, constitutes obtaining of that property. The difficulty in the way of that conclusion is simply that, when the bank account of the defendant (or his solicitor) is credited, he does not obtain the lending institution's chose in action. On the contrary that chose in action is extinguished or reduced pro tanto, and a chose in action is brought into existence representing a debt in an equivalent sum owed by a different bank to the defendant or his solicitor. In these circumstances, it is difficult to see how the defendant thereby obtained *property belonging to another,* i.e. to the lending institution…..
>
> In truth the property which the defendant has obtained is the new chose in action constituted by the debt now owed to him by his bank, and represented by the credit entry in his own bank account. This did not come into existence until the debt so created was owed to him by his bank, and so never belonged to anyone else."

So no property belonging to the transferor enters the UK and on the example there is no remittance. The same would apply to a gift by the non-dom to an adult child (not a relevant person) from outside the UK.

**Limit on income tax for discretionary trust**

As a general rule, under s811 ITA 2007 the liability of non-UK resident trustees is limited, in relation to UK savings income (such as dividends), to the income tax deducted at source or to any tax credit on the UK source income. This is however disapplied by s812 where there is a beneficiary who is a UK resident, so that the trustees are liable at the trustee rate on the UK source income in that case.

One situation where a liability for the trustees of such a trust could hitherto be avoided is if the income was allocated to a non-resident settlor under s624 ITTOIA 2005. That is only possible if the income would be chargeable to income tax by deduction or otherwise (648 ITTOIA 2005). It was the case that UK dividend income was chargeable to income tax albeit the tax was limited to the tax credit. So in that case, the settlements regime would apply and the trustees would not be assessable on the income tax since it would be the income of the non-resident settlor under s624 ITTOIA 2005 (albeit the settlor's income tax liability would be limited to the tax credit).

Following FA 2016, dividend tax credits are removed. It follows that any UK dividend income received by the trust is no longer deemed to be that of the settlor. Accordingly, subject to the granting of any interest in possession, the

trustees are liable for income tax on the UK dividend income if there is a beneficiary of the trust who is UK resident.

**Bayliss v HMRC**

The recent penalty case of *Bayliss v Commissioners for HMRC* [2016] UKFTT 500, in which the author acted for the taxpayer, highlights the need for a causative link between negligence and the loss of tax in order for a penalty to be chargeable, in that case under s95 TMA 1970. That point seems to have been lost on HMRC following the decision of the First-tier Tribunal in *Litman* [2014] UKFTT 089 where the Tribunal imposed a penalty on the taxpayers who had entered into a scheme on the basis that the taxpayers should have assessed whether the transactions stood up to commercial scrutiny. Un-commercial transactions are not always disregarded for tax purposes however (see e.g. *Mayes* [2011] STC 1269). A penalty is only due if the negligence caused the understatement of tax in the return. In *Bayliss* HMRC argued there was negligence because, for instance, the taxpayer had not kept a full suite of documentation, has signed a sophisticated investor certificate when he was not such an investor, that there were inconsistencies in some of the dates of the documents and on various other grounds. The Tribunal did not consider there to be a causative link between these matters even assuming they were negligent and the understated tax in the return (which was down to more fundamental problems with the scheme in question which the taxpayer had no way of identifying). The taxpayer had moreover taken reasonable in assessing whether the scheme worked and whether it had been effective prior to submission of his return and therefore no penalties were due. It is worth noting

however the changes to the penalties regime announced in the August 2016 Consultation Document, making it harder for the taxpayer to rely on the "reasonable care" defence to a penalty.

**"Making good" for NI purposes**

Where a "making good" payment by the employee has the effect of reimbursing the entire cash equivalent relating to the personal use of that asset, HMRC accept that the provisions of s.10(7A) SSCBA 1992 permit a deduction for the amount relievable for income tax purposes also for Class 1A purposes. The effect therefore is that the making good is wholly effective for eliminating both income tax and Class 1A NIC on any particular benefit.

However if the benefit is not entirely eliminated then HMRC claim Class 1A NI on the full benefit without taking into account any reduction achieved for income tax purposes. It is all or nothing. This is based on the statute which requires, in order for the benefit to be eliminated for NI purposes, that the deduction allowed in respect of "a matter" under the income tax code is "at least equal to the whole of any corresponding amount which would… fall by reference to that matter to be included in [general earnings for NI purposes]". So, HMRC would say that use of an asset if only partially eliminated as a benefit for income tax purposes by a making good of less than the full amount is still fully (and never partially) chargeable under the NI code for benefits.

That may be true as a general proposition but it is still necessary to identify what the benefit is and to distinguish between different "matters". To take an

example, the provision of free travel on a number of different occasions are different benefits. If one such trip is reimbursed, the benefit of that particular trip is eliminated for Class 1A purposes also. That benefit is eliminated even if others are not. The legislation looks at benefits on a “matter” by “matter” basis. Each trip is a different “matter” and it would be wrong, as HMRC have been known to seek to do, to conflate them.