TECHNICAL BULLETIN

ISSUE NO. 157
MARCH 2021

SEISS PHASES FOUR & FIVE – WHAT TO WATCH OUT FOR

The Budget on 3 March announced a fourth and fifth stages of SEISS. What does this mean for your clients?

Known and unknown

Final HMRC guidance and the Treasury Direction to cover SEISS phase four are expected by the end of March, and details on phase five are still sketchy. So, a degree of caution is still needed if advising on SEISS – phases four and five are not yet set in stone.

Clients may well be confused as to the rules and their entitlement given the changes at each stage. In this context, there is a useful House of Commons Briefing Paper (no 8879) issued on 9 March, which summarises the current position and provides details of how the scheme has evolved. This brings some clarity as to where we are now, and how we got here.

Outline of SEISS 4 and 5

The recently published factsheet on SEISS (policy paper 3 March 2021) sets out what we know so far. This is that the fourth grant will provide a taxable grant calculated at 80% of 3 months' average trading profits. The fourth grant will be paid out in a single instalment and capped at £7,500 in total. It will be available from late April 2021 until 31 May 2021.

There will be a fifth grant covering May to September, with the claims portal expected to be open from late July. The amount of the fifth grant will be determined by how much business turnover has been reduced in the year April 2020 to April 2021.

The fifth grant will be worth:

- 80% of 3 months' average trading profits, capped at £7,500, for those with a turnover reduction of 30% or more; or
- 30% of 3 months' average trading profits, capped at £2,850, for those with a turnover reduction of less than 30%.

CONTENTS

SEISS PHASES FOUR & FIVE – WHAT TO WATCH OUT FOR 1
PUTTING 'PENP' TO PAPER 3
BREXIT AND VAT – 3 KEY ISSUES 5
EMPLOYEE OWNERSHIP TRUSTS 7
DIRECTORS' LOAN ACCOUNTS IN A PANDEMIC 8
TECHNOLOGY TRAINING TIPS 10
NORTHERN IRELAND PROTOCOL 12
MONEY LAUNDERING – INDICATORS OF CRIME IN YOUR CLIENT BASE 12
FALLING INTO THE WRONG TRAP – VEHICLES & BENEFIT IN KIND 14
TAX FOR ACCOUNTANTS & AUDITORS – LBTT & LEASES 15
HMRC CLEARANCE APPLICATIONS 17
COMPATABILITY OF UK LAW WITH THE EU PRINCIPAL VAT DIRECTIVE REGARDING AFRS 19
TAX & HMRC UPDATES 21
EMPLOYMENT CORNER 24

What to watch out for now

There are some significant changes which could wrong-foot clients:

1. Individuals who were eligible for earlier SEISS grants are not automatically eligible for SEISS 4 and 5:
   - Watch out! The goal posts have moved. SEISS has moved on a year in terms of eligibility and income calculations.
   - 2019-20 is now the year which HMRC will initially use to test for qualifying conditions and eligibility.
   - Continuing to trade conditions apply to 2019-20 and expecting to trade in 2020-21.
   - This all means that the qualifying tests (no more than £50,000 self-employed income / self-employed income at least equal to other income) are applied to different tax years. Someone might have qualified for SEISS 3, but, with different years in view, fail for SEISS 4.
2. Eligibility is now based on filing a 2019-20 income tax self-assessment return by 23:59 on 2 March 2021:
   - This applies to existing and new claimants.
   - If someone who claimed SEISS 3 successfully, did not file their 2019-20 return before midnight on 2 March, they will now be ineligible.
   - There is an 'exceptional circumstances' right of appeal.
3. More amendments to tax returns are likely to be taken into account:
   - As the filing cut-off date has moved to 2 March, amendments to previously submitted returns may now be brought into account.
   - This potentially means claimants who failed to get SEISS 1 to 3 may be eligible for SEISS 4 and 5.
   - Conversely, some claimants who qualified on the old cut-off date, may now be ineligible for future grants.
   - Detailed guidance is awaited, but clients who failed to qualify previously might be encouraged to try again this time round.
4. For those who have successfully claimed before, the amount of the grant may be different:
   - There is no eligibility checker for SEISS 4, and no calculator. Claimants just have to apply.
   - But watch out! As regards the amount of the grant, HMRC will average up to four years' income – for any years of trading from 2016-17 to 2019-20
   - So, it is 80% of trading profits, but perhaps not the same trading profits…
5. Not all new traders will qualify:
   - Much has been made in the move to phase 4 that more people will qualify - especially 2019-20 start ups. But not everyone!
   - Remember that the 50% of income from self-employment still applies. For start-ups later in the tax year, it is very easy for this condition to fail. For example, an employee moving into self-employment in, say, October 2020 might have six and a half months of employment income, against only five and a half for self-employment.
6. The 'turnover test' is for SEISS 5 alone, not for phase 4:
   - There has been a lot of talk about the proposed 'fall in turnover' test but note that this only applies for SEISS 5 – and details of exactly how it will work are still to be confirmed.

Anomalies

SEISS was brought in as an emergency measure and has almost become 'business as usual'. But it still retains some of its emergency flavour in quirks and anomalies.

One, which many clients will notice, is that SEISS 5 apparently covers the period May to September – five months – but the grant is based on three months' worth of profits. This seems to be a deliberate policy decision, though something of a mind bender to explain.

There will still be businesses which fall through the cracks and others that seem to get super-charged profits – more than 100% of what they would make in a normal year.

One issue to remind new claimants about is that SEISS calculations take no account of start and end dates. A business which trades for 5 months in a tax year will find that its profits are averaged as if applying to a full 12 months. This can mean disappointingly low grants for new starters.

For those who are both employed and self-employed the results can be disappointing too. If self-employed income falls below 50% of total income, the claim fails entirely.

Compliance

Caution clients against any blasé attitude to claims. Compliance activity is increasing and for phase 4 we are likely to see some pre-claim checks to confirm that a new business is actually trading.

In a new move, HMRC is due to get increased recovery powers for those 'no longer entitled'. This

brings in a potentially challenging 'second guessing' game and reconfirms the need to have adequate evidence to support decisions at the time of claiming. What if trade picks up, so that overall results for the year are better than normal? Can the claimant produce evidence that it was reasonable to claim at the time?

Going one step further, suppose a clamant amends a previously submitted tax return and the amendment reduces their self-employment income, the logic would be that they might need to self-assess and repay part of any SEISS claimed based on the previous figures.

Conclusion

We do not yet have all the details for SEISS 4 and 5, but already client expectations will need to be managed. Broad statements about who will be eligible must be translated via the lens of detailed calculations and cliff-edged rules into actual claims – and there may be many a slip between cup and lip.

PUTTING 'PENP' TO PAPER

A Brief History

The taxation of termination payments has remained much the same over the last three decades, with one major change during that time concerning the way in which Pay in Lieu of Notice (PILON) should be charged to tax if it was deemed to be an "autopilon" (i.e. the employer had established a custom or a practice of making PILON payments upon terminating an employee's employment, and this had created the "expectation to receive" a PILON payment in the event that an employee's employment was to be terminated).

The main aim of any employer paying a termination payment up until April 2018, when the legislation was reconfigured, was to try to exempt as much of the payment as possible by structuring it so it could be included in the first £30,000 tax free exemption as set out at sections 401 - 416 ITEPA 2003.

The order of approach

The order in which the legislation must be examined so that it can be classified as a termination payment has not changed. It must first be incapable of being classified as:

1. Earnings under s.62 ITEPA 2003;
2. A restrictive covenant payment under s.225 ITEPA 2003;
3. An employer-financed retirement benefit scheme (EFRBS) under s.394 ITEPA 2003;

If the payment falls outside of the classifications above, then it can be examined to see if it falls within ss.401-416. If a PILON was received under the terms of the contract of employment, then it is to be treated as earnings. If it was a non-contractual PILON, then assuming it did not fall into one of the other classifications above, it could potentially be treated as falling within the £30,000 exemption.

Redundancy in General

Statutory and enhanced redundancy payments (SRPs) fall within ss.401-416 ITEPA 2003 where they are deemed to be genuine redundancy payments in accordance with s.139 ERA 1996. No NICs are payable on genuine SRPs.

Payments made specifically to recognise the employee's service count as earnings under s.62 ITEPA 2003 and are therefore also subject to NICs.

The employer can apply for advance clearance under SP 1/94 to confirm that redundancy payments under non-statutory schemes are genuinely made to compensate for loss of employment through redundancy and are not a reward for services. Such applications must be made in writing and be accompanied by copies of the scheme document and the text of any letter to employees that explains the terms of the scheme.

The 2018 changes

From 6 April 2018, a new regime applies - it taxes as earnings the basic pay an employee would have earned had the employee worked his or her notice in full (and to subject that amount to class 1 NICs). Accordingly, the tax treatment no longer depends on whether there is a contractual PILON in the contract.

Relationship to the Coronavirus Job Retention Scheme (CJRS)

Some difficulties have arisen since the CJRS payments came in because of the confusion between reference pay and furlough pay which employees have been entitled to receive during the pandemic.

The Government guidance in the early months of CJRS was to advise employers that they should pay termination payments based on the reference pay (contractual pay upon which the furlough pay was based). However, it was then apparent that several employers, who let staff go for whatever reason from

March to July, had been paying termination payments based on the 80% furlough value.

On 31 July 2020, a new law was introduced preventing employers from using furlough pay as "weekly pay" level instead of pre-furlough pay (reference pay). As such, notice pay, statutory notice pay, and redundancy pay post 31 July 2020 must use reference pay. Where an employee has no set working hours, the employer must average 12 weeks' pay to calculate notice pay and redundancy pay.

N.B. Employers cannot claim wages paid during the notice period under CJRS after 30 November 2020 and should never have claimed redundancy payments or payments in lieu of notice under CJRS.

A few words on Post Employment Notice Pay (PENP)

Employers must treat a slice of a 'relevant termination award' which reflects basic pay for any part of a notice period that is not served as earnings, and subject that slice to tax and NICs (employer and employee). For HMRC's guidance on this, see EIM13874 to EIM13898 and EIM14000.

What is a relevant termination award?

A relevant termination award is a termination award excluding specified payments.

A termination award is a payment or other benefit falling within section 401(1)(a), that is, a payment or benefit received directly or indirectly in consideration of, in consequence of, or otherwise in connection with, the termination of a person's employment under s.402A(1). Payments falling outside of these definitions, such as restrictive covenants and contractual PILONs, cannot qualify as termination awards - see EIM13874.

Statutory Redundancy Pay and approved contractual pay (to the extent that it does not exceed the statutory redundancy pay) automatically qualify for inclusion in the £30,000 exemption set out at s.402C ITEPA 2003 where they have the same meaning as in section 309(5) ITEPA 2003.)

Non-statutory redundancy pay is by contrast a 'relevant termination award' which no longer automatically falls within the £30,000 exemption.

Note then, that where no 'relevant termination award' is paid (e.g., where the termination package is characterised by a contractual PILON and statutory redundancy pay), the PENP provisions will not apply.

What must be taxed as earnings?

The slice of the relevant termination award (RTA) that must be treated as earnings under section 402B is:

- The entire RTA if "post-employment notice pay" (PENP) is equal to or more than the RTA.
- PENP, if it is less than the RTA but is not nil.

If PENP is a negative amount, it is treated as nil.

Foreign service relief

From 6 April 2018, changes were made to the availability of the foreign service relief for individuals who have carried out all or part of their employment overseas, introducing a requirement whereby the individual must be a non-UK resident in the year in which the termination takes place to benefit from this relief.

From 6 April 2021, under legislation to be introduced in the Finance Bill 2021, HMRC will amend s. 27 ITEPA 2003 to ensure that non-residents are charged to UK tax and National Insurance contributions on PENP subject to their period of notice, as well as the main duties of employment, having been physically performed in the UK. The new rules will apply regardless of the individual's residency status on termination of employment.

Calculating PENP

There are two formulas for calculating PENP, the simplified formula and the general formula.

Simplified formula

The simplified formula applies to an employee who is paid monthly, whose contractual notice period is expressed in months, and whose employment is terminated with immediate effect or whose unworked period of notice is a whole number of months.

The formula is: BP x D – T, where:

- BP is basic pay for the last pay period to end before the day notice is given (assuming notice is given).
- "Pay period" is not defined in the legislation and therefore should be given its ordinary meaning – see EIM13886 and EIM13888.
- D is the number of months in the post-employment notice period (broadly the unworked period of notice).
- Note that D is calculated by reference to the notice that the employer must give (by contract or law). This may be different from the period of notice that the employee must give.
- T is amounts (other than holiday pay and termination bonuses) that are paid on termination

but are taxable as earnings. Most commonly, T will cover contractual PILONs

Conclusion

The rules on termination payments have become much more complicated over the last three years and contain traps for the unwary. Employers and agents should ensure that an employment lawyer signs off any employment law related aspects, and that an employment taxes expert with relevant experience in termination payments handles any of the employment taxation aspects.

BREXIT AND VAT – 3 KEY ISSUES

There have certainly been a few new acronyms to get our heads around on the VAT front since 1 January 2021; PVA, MPIVS, IOSS, MOSS (now the Non-Union version). These all bring with them a variety of new issues ranging from increased paperwork and changes to practice to the need for VAT registrations and compliance in EU countries.

UK businesses supplying goods and services to customers in the EU cannot ignore these new rules, procedures, and EU compliance requirements, so the following sets out some of the key points, and the practical considerations, of a few of these new measures.

1. Postponed VAT Accounting (PVA)

Prior to Brexit the VAT treatment of goods arriving into the UK from the EU (known as acquisitions) or from outwith the EU (known as imports) differed.

Acquisitions of goods from the EU required minimal paperwork and they moved freely into the UK without the need for payment of any VAT. The VAT was dealt with by way of Boxes 2 and 4 of the UK business's VAT return.

Imports from outwith the EU, however, were subject to Customs procedures, more paperwork and the VAT would normally have been payable prior to the goods entering the UK, albeit duty deferment accounts could have been used to speed up Customs clearance procedures and to allow a little extra time for the importer to pay the VAT to HMRC.

As from 1 January 2021 all goods arriving into the UK from anywhere in the world are now classed as imports.

PVA has been introduced by the UK Government to both ease the pressure at the UK ports when goods enter the UK, and to ease the cashflow pressure for businesses by allowing for the import VAT to be accounted for via the VAT return instead of the importer having to make an actual payment of VAT to release the goods into the country.

There is no formal application required to use PVA, but you must tell your agent or freight forwarder that you wish to use it so that the Customs Declaration is properly completed. This, in turn, will then generate an online Monthly Postponement Import VAT Statement (MPIVS). This statement can be accessed and downloaded from your online VAT account, and then used to declare the import VAT payable in Box 1 of the VAT return covering the period in which the import occurred. If the business can fully recover VAT, then the same amount would go into Box 4 as input VAT. Please note that Box 2 (and Box 9) of the VAT return should no longer be used!

If PVA is not used, then import VAT will have to be paid before the goods are released into the UK, and the importer will get a C79 from HMRC (in the same way as it would have for non-EU imports prior to Brexit). There is also the option to deal with the import VAT using a duty deferment account, whereby payment is collected by direct debit on the 15th day of the month following the calendar month in which the import occurred.

In both cases, where the business can fully recover VAT, this VAT should also be reclaimed via Box 4 of the VAT return.

PVA is equally applicable to goods now imported from non-EU as well as EU countries and therefore, for some businesses, its use will present a real cash flow advantage.

2. Selling Goods from the UK to customers in the EU

From a UK perspective, there is no longer a requirement to differentiate between business and non-business customers and the location to which the goods are sent. All goods sold from a UK business to customers outside of the UK are now zero-rated exports. The usual forms of evidence are required to support the removal of the goods from the UK and export declarations must be completed.

While not relevant for determining the UK VAT position, the destination of the goods, the terms of delivery, and whether the customer is in business or not, becomes relevant in relation to establishing EU compliance requirements.

The terms of delivery of the goods will now drive whether a UK business has a VAT registration obligation in the EU.

Sale of goods to business customers in the EU will generally mean that the recipient business is the importer in their country, and that they will deal with the relevant VAT requirements as an importer in that country.

In terms of goods sold to consumers, there are a few scenarios.

In simple terms, goods sold duty paid (DDP) means that the UK supplier is responsible for the payment of the import VAT in the country of destination and will have likely built that into the price of the goods; the consumer will therefore not have any further VAT to pay on receipt of the goods.

The UK supplier is deemed to be the importer in the country of destination and an onward sale of these goods then takes place in that country to the end consumer. A VAT registration obligation therefore arises in that country for the UK business.

Goods sold duty unpaid (DDU) puts the burden of accounting for the VAT on to the end consumer; they are effectively the importer in the country of destination and so under current rules, subject to further comments below, there is no requirement for the UK business to register for VAT in that country.

While relieving the burden of an EU VAT registration for the UK supplier, DDU terms has its disadvantages in terms of marketability to EU customers, especially for e-commerce businesses where the price paid for UK goods at point of sale is then inflated by a VAT charge (plus a courier administration fee) on arrival at their destination. It can make the pricing of goods on websites tricky!

With effect from 1 July 2021, the EU will also be implementing new procedures to deal with the sale of goods to EU consumers where the consignment value is €150 or less. UK businesses will be required to register for the Import One Stop Shop (IOSS) which has been created to facilitate and simplify the declaration and payment of VAT for goods sold from a distance by sellers from either the EU or from a non-EU country or territory.

It will require UK businesses to pick an EU country in which to register for this scheme. All sales under €150 to all EU countries will then be reported through this one IOSS return.

In relation to the period between now and 1 July, and then post July for consignments of over €150, businesses using DDP terms for sales to EU consumers will need to register for VAT in each EU country they sell to, which will in many cases prove to be a large administrative and costly burden.

In addition to using IOSS for the lower value consignments, businesses selling goods valued at more than €150 per consignment to EU consumers therefore have the following options:

- Sell under DDU terms only and deal with any adverse marketing issues;
- Cease selling to EU consumers altogether;
- Be selective and sell to only those EU countries where the revenue stream is high enough to warrant the additional administrative costs;
- Route all goods physically through one EU country – this would require VAT registration in that country and clearly there are considerations as regards operational matters and having an establishment or representative in that country also. However, this would then allow goods to move freely from that country into other parts of the EU under EU rules.

Businesses should now review their revenue streams and non-UK sales lines to determine how they intend to operate and comply with the relevant EU obligations accordingly.

3. Supply of digital services to consumers in the EU

The place of supply rules for services has not changed from the UK perspective as a result of Brexit. The general rule still applies, and the exceptions to the general must still be taken account of. In many situations, subject to checking the exceptions, UK VAT will not be applicable to services provided to customers outside of the UK, whether in business or not.

There is, however, a requirement to consider the EU position regarding supplies of digital services to EU consumers. Digital services are defined by HMRC here.

The place of supply of such services is where the customer belongs, and there is a requirement to be registered for VAT in that EU country. It follows, given the nature of digital services, that a UK business could have sales to consumers in all EU countries, and therefore there would be a need for VAT registration in all those countries.

An alternative, and certainly a preferable option, is for UK businesses to use the non-union MOSS (Mini One Stop Shop) which simplifies this compliance burden by allowing the UK business to report and pay VAT due

on sales in multiple EU countries (at the VAT rate applicable for each country) in just one country.

Businesses wanting to use the non-union MOSS need to choose an EU country in which to register for the scheme, and this will be the country where VAT returns are submitted, and the VAT paid. They must register by the 10th day of the month after relevant sales are first made in an EU country.

Registering for non-union Moss is English speaking countries is proving popular and accordingly many, including the Republic of Ireland, are experiencing capacity issues due to the volume of applications and the current pandemic. Businesses therefore need to consider their EU registration requirements as soon as possible and not wait for the deadline.

EMPLOYEE OWNERSHIP TRUSTS

Historically, where an entrepreneur wished to retire and dispose of the shares in his company, and there was no family succession, he would either seek a trade buyer or alternatively, the existing management of the company may have undertaken a management buyout.

In a trade sale or management buyout, typically the vendor would pay Capital Gains Tax (CGT) at the 10% Business Assets Disposal Relief ("BADR") rate and/or the normal 20% CGT rate.

With effect from 6 April 2014, and to encourage employee-owned companies, a new relief was introduced under the umbrella of an "employee ownership trust".

The three main tax benefits are:

1. No CGT at all is payable by the vendor. This is a holdover relief in that, if the shares are sold by the trustees in the future then the held over gain becomes taxable.
2. There is an Inheritance Tax exemption in respect of a transfer of value to the trustees.
3. Of interest to the company employees, is the possibility of the company being able to pay up to £3,600 to each employee per annum tax free in respect of qualifying bonus payments.

Qualifying Conditions

Several conditions must be met to obtain the benefits noted above.

The vendor:

1. Must not be a company.
2. Must not exceed a "limited participation requirement".
3. The holdover relief is not available where the vendor, or a connected person, has made a related disposal in a previous tax year, of the ordinary share capital in the same company.
4. A claim must be made under section 236H(1)(c) TCGA 1992.

The company:

1. The relief is available in respect of ordinary share capital, which is all share capital other than share capital which gives the holders a right to a dividend at a fixed rate but no other right to share in profits. This is similar to the position with BADR and the 5% requirement.
2. For the period from the date of disposal until the following 5 April, the company must either be a trading company or the holding company of a trading group. Again, there are parallels with BADR in that a trading company is one which carries on trading activities and whose activities do not include, to a substantial extent, activities other than trading activities. HMRC's view on this is contained in their manuals at CG64090. The company could therefore have some non-trading activities but the 80:20 "test" will have to be met.

The trust:

1. Must not allow trustees to apply the trust property for the benefit of anyone other than eligible employees. The trust property will include the company shares and perhaps accumulated dividend income from the company. It must not be possible for the trust to make loans to employees.
2. Must have a controlling interest in the company immediately after the transfer. It is not possible for a controlling interest to be added to in a later tax year by the same vendor. It is possible for several separate individuals to make disposals to the trust in the same tax year, in the creation of a controlling interest.
3. All employees of the company are eligible employees and must benefit on equal terms. Certain participators are excluded if they have or are entitled to acquire more than 5% of any class of

share capital of the company, or its assets on a winding up.

4. The trust deed can allow the surviving spouse of a deceased employee to benefit for a period of up to twelve months from the date of death. It can also require that an eligible employee does not benefit until they have completed a continuous period of employment of up to twelve months. Two other interesting points are that an individual can be excluded from benefit if he requests this in writing and secondly, trust property can be applied for charitable purposes.
5. The requirement for trust property to be applied on an equal basis among eligible employees can be met based on:
   a. the relative remuneration of each;
   b. length of service;
   c. hours worked.

   In short, not everyone is required to receive an equal amount and so seniority, or long service can be rewarded in terms of the tax free £3,600.
6. When the trust is being set up, the vendor can appoint the initial trustees who, in turn, control appointments to the company board.

Vendor options

As noted above, it is necessary for the employee ownership trust to acquire a controlling interest in the company. This could, for example, be 51% of the company's ordinary share capital with the other 49% remaining in the hands of the vendor or his family. It is possible therefore for:

- The vendor to retain a significant control or influence, and he can remain on the board.
- Within the eligible employees, there may be a "natural leader" who can continue to drive the business. However, if not, the vendor could dispose of part of his remaining shareholding to a new recruit who has the necessary abilities, and to give that individual a direct interest in the company.
- Ultimately however the 49% shareholder may sell some, or all, of his remaining holding subject to the prevailing CGT rates and entrepreneurs' relief.

Funding of the trust is generally provided by the company by way of non-tax deductible "contributions". If the company has surplus cash, it can make an initial contribution to the trust which in turn, utilises this to pay the vendor. There will generally also be deferred consideration due by the trust to the vendor. This deferred consideration can be repaid by the company making further contributions to the trust which, in turn, utilises these to repay the deferred consideration.

Two of the major tax advantages of an employee ownership trust are that the vendor can sell without any CGT liability, and employees can receive tax free bonuses from the company of up to £3,600 per annum. Beyond that, the trust ensures that the ownership of the company is for the benefit of all employees of the company for the time being. In a way this is very similar to a workers' co-operative, with jobs being kept in the local community, rather than being exported abroad.

DIRECTORS' LOAN ACCOUNTS IN A PANDEMIC

Many SME company directors draw on their director's loan account during the year and aim to clear any overdrawn balance with salary, dividends, or other repayment methods infrequently, or even annually.

SME directors could easily use a company credit card to pay a private debt or incur expenses on company business which are partly personal. All such transactions could result in an overdrawn loan account without the director being especially aware of it, as it might just be something which the accountant sorts out at the end of the year!

However, the pandemic has had a major impact on trading, with a knock-on impact on distributable profits, cash flow, salaries, and dividends. This reduces the options for dealing with overdrawn directors' loans.

What is the position now, and what are the consequences?

A two-sided equation

For SME companies, it is a double-sided equation. There are potential consequences for both the company and for the director, and although both sides of the equation are related, they are also distinct.

From the company's perspective a key issue is the possibility of a tax charge on the company due to there being an outstanding director's loan account. The charge is under s455 Corporation Tax Act 2010 (CTA

2010). This arises due to the director's status as a participator in a close company.

Quite separately, the director is potentially exposed to a benefit in kind charge to income tax. This charge is based on the director's status as an office holder or employee of the company. The charge results from provisions in the Income Tax Earnings and Pensions Act 2003 (ITEPA 2003) to tax the benefit of 'cheap loans' to employees.

Beneficial loans - the benefit in kind charge

The legislation here starts with s175 ITEPA 2003, which seeks to impose an income tax charge on company employees and office holders.

The rules apply to all companies but are particularly likely to impact owner managed companies where, arguably, it is easier for directors to arrange interest-free loans, and where it is more likely that the day-to-day dealings between director and company result in a debt to the company.

Not all loans attract a benefit in kind charge. There is a detailed list of the exemptions in HMRC Employment Manual EIM26132. These include loans for necessary business expenses, up to £1,000 (s178 and 179 ITEPA 2003). Also excluded are loans where the company charges interest of at least the official rate.

Employee loans are subject to a general £10,000 exemption threshold. Loans below this level can be ignored for benefit in kind purposes.

The relevant period for the benefit in kind charge is the tax year, not the company's accounting period. Where a loan from a company to a director or employee exceeds £10,000 in the year to 5 April, subject to certain exceptions as noted above, there is a taxable benefit in kind charge for the employee/director. This benefit needs to be reported on form P11D.

Exceeding the limit at any time during the tax year means that there is a benefit in kind charge on any 'cheap loans' for the whole tax year (or from date loan first made available, if this is after the start of the tax year, to date loan repaid, if this is before the end of the tax year). This applies even if the loan balance is under £10,000 for most of the year.

The benefit in kind charge is based on the difference between the official rate of interest and the actual rate charged by the company. There is no charge where the company charges at least the official rate of interest.

The normal method of calculating beneficial interest (per s182 ITEPA 2003) is a simple average of the loan amounts outstanding at the start and end of the tax year (or date made available/repayment date). The strict daily basis calculation (s183 ITEPA 2003) may be used instead, by election by the taxpayer or by notice from HMRC. The normal method is always used for the P11D calculation.

Loans to directors – the company perspective

SME companies will normally be 'close companies'. Broadly, a close company is one which is controlled by five or fewer individuals, who are called 'participators'.

While shareholder directors who hold over 5% of the equity will normally be participators, there are exclusions, extensions, and tests, so it is worth checking the details. There is a useful summary of conditions and exceptions in the HMRC Company Taxation Manual at CTM60100.

All this means that there may be company directors who are not participators, and participators who are not company directors. And it is loans to participators to which the legislation applies. The legislation starts at s439 Corporation Tax Act 2010 with a definition of a close company. The tax charge on the company is outlined in s455.

S455 CTA 2010 imposes a 32.5% tax charge on the company, as a percentage of the loan outstanding, for loans to participators in a close company where the loan is outstanding nine months after the company year end. So, unlike the benefit in kind charge, which is based on a tax year, the s455 charge is based on the company's accounts. Balances repaid within nine months of the company year-end do not attract a s455 charge.

There is a £15,000 exemption threshold for full-time working directors, who have no material interest in the company (broadly, this equates to having no more than a 5% shareholding). In such cases, loans up to £15,000 do not result in a s455 charge. Details can be found in s456 CTA 2010 and there is a useful summary in the HMRC Company Taxation Manual at CTM61540.

Special 'bed and breakfasting' rules apply to repayment of all, or part, of the loan followed by a further loan from the company within 30 days. This rule applies to repayments/advances of £5,000 or more (s464C CTA 2010). Similarly, repayment of loans over £15,000 when arrangements are in place for a replacement loan are caught by the s455 charge. For an overview of the provisions see CTM61500.

Options

The pandemic has affected businesses differently. Some will be able to continue with their usual remuneration strategy for directors, which often includes declaring dividends to clear any outstanding director's loan balances. In other cases, both the company and the directors may face liquidity issues which restrict the options.

New approaches may be needed here. Paying bonuses is one way to clear an overdrawn loan account, but it is expensive. The amounts needed to be grossed up, so that the net employment income, after tax and National Insurance is sufficient to clear the overdrawn loan account.

An alternative, and possibly a half-way house, is a loan waiver. There are special rules for participators in close companies which mean that the write off is taxed as dividend income rather than employment income for income tax purposes (see s189 ITEPA 2003 read alongside s19 Income Tax Act 2007). However, the income could still be viewed by HMRC as earnings for National Insurance purposes where the loan was to a working director.

The approach of paying the s455 CTA 2010 is not all bad news. It is essentially a timing issue as the s455 tax is repayable as the overdrawn loan is repaid to the company. But there may be a significant delay before s455 is repaid – see the note on reclaiming s455 tax on the Director's loans page of Gov.uk.

AML and PCRT

Before leaving the subject, a reminder on Professional Conduct in Relation to Tax (PCRT) and Anti-Money Laundering (AML) rules. Errors do happen, and there can be disagreements with directors, or issues arising on taking on a new client. For example, loan accounts may have been 'cleared' with dividend payments when the company had insufficient distributable profits.

PCRT includes a helpsheet on errors and appropriate actions where you disagree with the directors. AML may kick in where you discover errors which mean under payment of tax and the directors have not provided reassurance that outstanding amounts will be paid in a timely manner.

Conclusion

Changed times mean challenging assumptions. Old ways of dealing with overdrawn director's loans may need a rethink in the pandemic. Businesses may need bespoke solutions which balance their specific priorities. What was done in the past may now require a rethink.

TECHNOLOGY TRAINING TIPS

Written by Lugo Limited, ICAS IT Partner

This month we provide advice on technology training and share insights from recent Lugo and ICAS studies.

During a recent cyber security webinar, ICAS and Lugo hosted in February 2021, attendees were asked, '*Do you feel you are trained well enough on cyber security?'*. Shockingly, 83% said no. However, lack of knowledge and understanding when it comes to technology, is limited not only to cyber issues.

In a recent Lugo study conducted on IT in accountancy, respondents were asked about their top three pain points with respect to IT. Training was mentioned by 70% of firms, with issues such as lack of employee knowledge, product training, and client education noted. Therefore, when respondents were then asked what they want from technology, 65% of firms revealed a variety of training related wishes, including educational resources and technology specialists.

Equipping Leaders

Education should be from the top down to keep teams up to date on fast paced technological developments. We found a lack of understanding was a common concern across most interviewees, with 25% not feeling fully equipped to make informed choices on technology.

Firms are looking for more ideas and innovation from their IT team. In-house IT experience within a single business can often become stale, whilst external experts, such as Lugo's IT Director service, tend to have a broader perspective due to their exposure to a wide range of clients. However, it was noted by one of the technology advisers that many of their larger clients have their own in-house staff as well as engaging external advisers. Internal IT functions are useful in helping staff use existing software, whilst external experts are often best to advise on new technologies. This is known as co-managed IT.

Employee Knowledge

Looking at training across all those surveyed, Lugo's research found 87% of people attend training. This reduced to 71% in firms in the 1,501 - 2,500 client bracket, with only firms with over 5,000 clients training 100% of their staff.

One firm suggested that Continuing Professional Development (CPD) or training on technology-related matters should be prioritised, despite the existence of other immediate client priorities. The culture and ethos within the firm should encourage staff education for their own self-development as well as to enhance wider service delivery quality. Employees are representatives of the firm, so it is important to invest in educating staff on advances in technology.

Product Training

Due to the speed of change, it can seem impossible to keep up with the latest developments and the wide array of products accountants now use. This is exacerbated, for many, by the sheer number of apps and software solutions being introduced into the market. The key challenge is remaining aware and informed so you can effectively serve your clients.

There are implications of new technology for an established workforce, especially around the ability for them to retrain. We all wish for intuitive systems that require little training, and some people are naturally inquisitive as to how to make the most of the tools available, yet if our knowledge is outdated, so are our working practices and advice to clients.

Creating videos to answer frequently asked questions, or to demonstrate processes users might not perform very often, can be a great resource and will be specific to your firm and its systems. With a Microsoft 365 licence you can use Microsoft Stream to record videos up to 15 minutes long – however, we say the shorter the better! This should help reduce the '*massive knowledge gaps'* mentioned by another respondent.

Educational resources

There is a plethora of online product training available free of charge. If there's a need for training on Microsoft's products then a great place to start is the Microsoft Support site where you can access Microsoft's Learning and Training area, including the Microsoft 365 Training Centre and their Security Centre.

Compliance software vendors provide online resources to guide users, normally accessed through the help area of the programme. For example, to enhance users' knowledge and understanding, Wolters Kluwer offer a CCH Learning Portal, and there is also an Iris Training Centre, to build staff proficiency in key areas.

Cloud bookkeeping solutions tend to certify users who have become proficient in their applications to a specified level including Xero, QuickBooks and Sage University. Awards can incentivise employees to increase their product knowledge and supporting staff through the training shows a commitment to investing in your people.

There are hundreds more add-on apps which can provide extra functionality such as automated data entry, budgeting, forecasting, and debt chasing. Having a sound knowledge of what is available in the marketplace can enhance client conversations. If you use Xero, the digital magazine Xu is a great resource highlighting new developments in the industry.

Additionally, since many SMEs are unaware of the vital impact of cyber training or know where to start educating their staff about this, the National Cyber Security Centre (NCSC) offers free online training. The interactive training ends with an assessment consisting of 8 questions about the topics covered, to provide a quick knowledge check.

It was found that 66% of firms interviewed by Lugo are part of at least one peer learning group. Organisations such as Accelerate or the Innovation 2020 group give like-minded firms the chance to discuss hot topics and keep informed of innovations in the sector.

Conclusion

The huge rise of new technologies is having an impact on staff training within firms as they struggle to keep up. Whilst we will never know everything there is to know about technology, firms should ensure they are not being left behind. Supporting and encouraging employees and clients to embrace the benefits of this digital age will stand you in good stead for the future, whatever it holds.

Look out for more insight into the key themes from Lugo's research in future ICAS Technical Bulletins.

If you would like to discuss any element of this research or enhance your own cyber resilience, please email Liz.Smith@LugoIT.co.uk

NORTHERN IRELAND PROTOCOL

Under the Northern Ireland Protocol, Northern Ireland (NI) is still part of the UK VAT system with NI businesses continuing to submit one UK VAT return and having one UK VAT registration number. However, several things have changed as follows:

Since 1 January 2021:

- NI remains aligned to the EU VAT rules for goods, but not for services.
- In relation to transactions involving the movement of goods with NI, the UK is now being referred to as 'GB'.
- The way VAT applies to supplies of goods between NI and GB will broadly continue as it has done. VAT will be charged as if they are domestic UK supplies, even though it is recognised that supplies of goods between GB and NI (and vice versa) are exports and imports for VAT purposes.
- It should be noted that when a UK VAT registered business moves its own goods from GB into NI, it will have to account for output tax on its VAT return, as if it had sold the goods to a third party. If it intends to use the goods solely to make taxable supplies, then it can claim the VAT as input tax on the same VAT return, subject to the normal recovery rules.
- A VAT registered business moving its own goods the other way, from NI to GB, does not have the same requirement to account for output tax.
- While VAT grouping will still be available to businesses in NI, VAT needs to be accounted for (and reclaimed, subject to the normal recovery rules) where goods are supplied by one group member to another and the goods move from GB to NI, or where supplies are made of goods located in NI at the time of supply, unless the supply is between group members that both have establishments in NI.
- The second-hand margin scheme will no longer apply to supplies of goods in NI where those goods have been brought into NI from GB. VAT will be chargeable on the full selling price. Many business sectors that use the second-hand margin scheme will see the impact on their profit margins, and consequently the end consumer could end up with price increases.

MONEY LAUNDERING – INDICATORS OF CRIME IN YOUR CLIENT BASE

After a recent presentation from the Metropolitan Police, Alasdair Millar, Senior Reviewer within Practice Monitoring reflects on what might be considered some red flag indicators of money laundering activity in a typical accountancy practice.

"I know my clients really well".
"I would know if any of my clients were up to mischief".
"I don't deal with that kind of client".

That's often what practitioners tell me when our discussions turn to money laundering compliance and reporting during Practice Monitoring reviews. As comedian Kevin Bridges said sceptically, "Do ye? Aye".

At a recent meeting held with the accountancy bodies and a forensic accountant in the Metropolitan Police, I was struck by her observation that in only one case she had dealt with did she think the people convicted looked like archetypal gangsters.

Money launderers, and people engaged in organised crime, look just like you and me. So, what can we look out for to help us identify when clients are involved in activities they ought not to be?

1. Lack of sales records

If your client asks you to prepare their accounts purely from bank statements without the back up of sales records or any other supporting documentation, then keep in mind that this is a recurrent feature in money laundering investigations for a variety of different crimes.

Indeed, failure to keep accounting records is a criminal offence under S386 of the Companies Act 2006. In 2016 (R v Skinner and Ferron) two directors, whose only company records were bank statements, a collection of invoices, and insurance documents, were convicted of this offence.

2. Income received at unusual times of the day

Do statements from the card processor indicate significant income being received at unusual times of day? For example, receipts being processed in the wee small hours when your client is not part of the nocturnal economy?

Clients have been known to “lend” their card payment processing machine to others allowing funds to be remitted from unknown customers. Funds are then withdrawn in cash or transferred over to the person borrowing the machine.

Income received at odd times of day can be an indicator of the laundering of monies from prostitution. In 2017 a man was convicted when he allowed a card machine, connected to a music studio he ran, to be used to collect payments from customers of a brothel. The case was supported by an analysis of the timing of the receipts being processed by the machine.

3. Lack of assets or supplies

Put simply, there are insufficient assets in the business to carry out what the core activity purports to be, or the business does not appear to have purchased sufficient goods to generate the extent of sales being reported.

The police would tell you that a lack of assets or supplies is indicative of false accounting and a front for criminality. One example given at the recent meeting with the Met Police was a case where a car hire firm had no cars in the company accounts. Cars, and much of the company’s income, went through directors’ personal bank accounts – the detail of which was not provided to the accountant.

4. Lack of staff costs

Where a business is engaged in providing some sort of service but has little or no staff/contractor costs and derives a level of income more than what could reasonably be expected by the owners, this can be an indicator that the client may be involved in modern slavery or human trafficking.

5. Loans and Bridging loans

There are several indicators associated with extortion that police have identified in investigations into organised crime families in London. Clients may present themselves as businesspeople yet are involved in serious and organised crime, with the extortion being accompanied by threats of violence making victims fear for their lives.

Indicators might include clients who are not widely recognised as being financial institutions granting loans secured on the residential properties of their customers. Loans may be recorded as owed to a client, but no evidence exists that the loans were paid out. Loans may be secured on residential properties with excessive interest rates. Perhaps properties were acquired by clients for substantially less than market price when the customer defaulted on the loan.

Impact on practising accountants

Criticism is levelled at the practitioner when they perhaps notice these things in their day-to-day work, yet do not report their suspicions further. They may even go so far as to enquire why the level of assets or purchases are lower than expected for the level of activity, or how the business operates so successfully without any staff.

However, once they get an answer sometimes practitioners can then not apply the same level of scepticism as they applied when they raised the query in the first place. It is true you are not expected to investigate in the manner of a police officer, but you are expected to apply your professional scepticism and report your suspicions.

As a profession, we can be used to add a veneer of legitimacy to illegitimate criminal business enterprises. Occasionally accountants enter this world with their eyes wide open, but more often criminals exploit legitimate accountants who unwittingly act for them.

Accountants can become complacent or insufficiently sceptical because we are all busy trying to make a living in what are currently very difficult circumstances. Money laundering is far from being a victimless crime, so in a world where slogans seem to proliferate, let us remind ourselves to stay alert, be sceptical and make reports when needed.

FALLING INTO THE WRONG TRAP – VEHICLES & BENEFIT IN KIND

The 2020/21 P11D cycle is coming up and the following two tax cases show how easy it is to fall into the wrong trap with vehicles for benefit in kind purposes and rack up a hefty tax bill for the employee at the same time.

Case 1

Determinations, discovery assessments, and closure notices

In the case of Tim Norton Motor Services v HMRC [2020] TC7973 which was heard at the First Tier Tax Tribunal in October 2020 and decided in December 2020, the NICs determinations, discovery assessments, and a closure notice raised by HMRC spanning seven tax years from 2010-11 concerned the availability of two different cars in a car dealership to a shareholder-director. Benefits in kind (BIKs) were computed under Part 3 Ch.6 ITEPA 2003, and corresponding employer's NICs on the provision of said BIK were also assessed on the employer company.

When is a car not "available"?

Due to the value of the vehicles concerned, which were a rare model of Maserati and a Ford GT40 which the company had purchased in 2001 and 2005 respectively, the benefit charges were high. HMRC raised the assessments following an employer compliance review in 2016, after which the officer concluded that the cars had been "made available" to Mr Norton for periods longer than those in relation to which a BIK had been declared.

Good faith

The company had made what it considered to be sufficient effort to demonstrate that the cars were not 'made available' to the director under s.114 ITEPA 2003 by carrying out the following actions:

- The cars were kept on the company premises which was ten miles away from the director's own home;
- The keys to the car were held in a locked box within a locked safe on the business premises;
- The staff handbook contained an instruction to deny the use of any vehicle without express permission of management;
- The cars were not used for commuting by the director or his wife;
- The Maserati was kept at the back of a large showroom garage behind several other vehicles; the Ford was kept in the showroom;
- The Ford was occasionally taken to car shows for advertising purposes. If either of the cars was to be used, Vehicle Excise Duty was paid in advance and a SORN declaration completed when the car was returned to the company premises. MOTs were in place when the cars were driven;
- Only Mr Norton was insured to drive the vehicles, and for the first few years, only one of the vehicles was to be driven at any one time;
- Mr Norton declared that he only used both cars for business purposes and the Ford had the company logo affixed to it by way of livery;
- P11D declarations had been made for certain periods in the years during which the assessments had been made to cover off the periods when it was considered there had been some (unspecified) private use of the cars by Mr Norton.

Decision

Despite the arguments put forward by Mr Norton that he would not have driven the car on occasions when it was technically illegal to do so, and the car would not have been covered by the insurance had it been involved in an accident, the judge decided that a BIK and corresponding NICs liability nevertheless applied while the car was off the road.

He considered the staff handbook was not prohibitive enough to place sufficient restraint on Mr Norton, and that it was simple enough to restore availability at any time by paying Vehicle Excise Duty and ensuring the roadworthiness of the car.

Case 2

When is a van a car?

In the long-running case of Payne, Garbett and Coca-Cola European Partners Great Britain Limited v HMRC, the Court of Appeal decided in August 2020 that the three panel vans (a Vauxhall Vivaro and two VW Transporter T5 Kombis) were to be treated as cars for BIK purposes, which of course conferred a much higher BIK on to the employees and a higher employer NICs liability on to the employer. This is an important decision for employers who supply these types of

vehicles to employees and serves as a note to the unwary that care should be taken when considering what declaration to make on P11D.

Previous decisions at the First and Upper Tier Tax Tribunals had allowed one of the vehicles (the Vivaro) to remain classified as a van while the other had to be reclassified as a car.

Tech spec

Each of the vehicles were fitted with a second row of seats behind the first row – known as a "crew cab" fit out. The Vivaro was fitted out slightly differently to the other two Kombis and survived the Tribunals as a van because the second set of seats did not extend across the full width of the vehicle, whereas in the Kombis, they did, which reduced the load space at the back of the Kombis by a small margin. The Kombi seats were removable - but this only appeared to demonstrate to the Tribunals that the vehicles served an equal dual purpose of transporting people as well as cargo, whereas the Vivaro was deemed to be primarily fitted out to carry cargo.

The Court of Appeal disagreed that the Vivaro technical specifications were so radically different from the Kombis as to draw a distinction and classified them all as cars.

Tax adviser's dilemma

Due to the binding, but still appealable, nature of the decision, essentially this outcome leaves those advising clients on the matter of car and van fleets with some crucial discussion and review points for the agenda of the next meeting:

- Are fleets of what the client might think are vans, now to be treated as cars where they have been modified to accommodate mixed cargo of people and goods?
- What evidence does the client have to back this rationale up?
- Are previously submitted returns of expenses and benefits (P11Ds) in need of amendment?
- What choices is the company making in terms of fleet renewal going forward?
- What levels of tax and NICs are potentially at risk if nothing is done?
- What are the relevant VAT and capital allowances points? (see below)

VAT and Capital Allowances implications

Whilst the Coca-Cola case did not consider the capital allowances aspects, clearly if capital allowances have been overclaimed by the business, there may be more tax to pay. The definition of a van for capital allowances purposes is similar to that within s.115 ITEPA 2003. Vans are generally also eligible for the Annual Investment Allowance, and cars are not.

Similarly, the VAT treatment of the purchase of cars is different to that of vans and is, generally speaking, not recoverable. To add to the complication, the definition of a van for VAT purposes is not the same as it is for BIK purposes, and an exemption can be applied if the payload is one tonne or above, regardless of whether there is a second row of seats.

So, it may be the case that, due to this ruling, some vehicles in a fleet are treated as cars for BIK purposes, whilst treated as a van for VAT.

Finally - a note on Double Cab Pick-Ups

It is not entirely clear whether "double cab pick-up" vehicles, which are treated as vans for both VAT and BIK purposes where the VAT payload definition is fulfilled, are now to be treated differently – only time will tell.

TAX FOR ACCOUNTANTS & AUDITORS – LBTT & LEASES

Those involved in accounts preparation and audit have unparalleled insights into what is going on within a business. Many of these transactions have tax consequences which will be routinely dealt with following preparation of the accounts.

But some events and transactions have tax consequences which may not be immediately obvious, as the consequences may not be apparent simply from the figures. One such group is changes to leases for Land and Buildings Transactions Tax (LBTT).

Several events can trigger a recalculation of LBTT, and/or the need to submit a return to Revenue Scotland. If accounts and audit staff can highlight these occasions to the client, it will help avoid penalties. In the present economic climate of the pandemic, it might even produce a welcome tax refund.

What is LBTT?

To quote Revenue Scotland:

LBTT is a tax applied to residential and commercial land and buildings transactions (including commercial purchases and commercial leases) where a chargeable interest is acquired.

Revenue Scotland administers LBTT with support from Registers of Scotland (RoS).

LBTT replaced Stamp Duty Land Tax (SDLT) in Scotland from 1 April 2015. The particular focus here is on commercial leases.

What is the issue with leases?

LBTT on commercial leases has purpose-built flexibility. Unlike SDLT, it is subject to reappraisal during the course of the lease. The aim is to tie the costs of the tax more closely to the economic value of the lease, and to recognise that this economic value may change over time.

The way this happens is by creating review points during the life of the lease. Key review points are: every three years from the effective date of the lease; on assignation of a lease; and on termination. But there are other, more subtle occasions of charge.

Many business owners are unaware of the nature and importance of this cyclical review process. Fear of additional tax to pay, unfamiliarity with the rules, or simply the challenge of making returns, can mean that tax points are missed. This can lead to penalties, and tax bills, or even missed opportunities to recover some tax already paid.

Why now?

LBTT on leases is topical now for two main reasons:

1) 1 April 2021 marks six years since the introduction of LBTT in April 2015. This means that the season of second round three-yearly lease reviews is just starting.
2) Due to the pandemic, there have been significant changes to many leases, and these changes may trigger the need to make a return to Revenue Scotland. In addition, if the value of a lease has fallen, the business may be due a welcome refund of part of the LBTT initially paid on the lease.

Conspicuous and hidden tax triggers

The tenant often has little to do with the initial submissions around LBTT on a lease. Although these are legally the tenant's responsibility, they are often made by the landlord's solicitor. By the three-year review stage, contact with the landlord's legal team is likely to have lapsed and recognition of the need to make a return can be lost.

While the three-year review point may be obvious, and Revenue Scotland would normally issue a reminder, tenants may still be unaware of their responsibilities and fail to take appropriate action. Other occasions of potential charge are more hidden.

For example, one more subtle occasion of charge is the 'tacit relocation'. This happens where a lease has expired, but the tenant continued to stay on in the premises – often under the original terms. How many businesses would spot this as a trigger-point for submitting an LBTT return?

Other occasions, which may become apparent from preparation or audit of the accounts, include: variations in the lease; increases or decreases in rent; assignment or termination of a lease; or a lease taken out under SDLT becoming reportable under LBTT for the first time. This can happen due to a change in lease terms.

Note that outgoing tenants must submit an assignation return to Revenue Scotland within 30 days from the effective date. All this means that alerting clients to the need for immediate, timely action is a priority.

Cycles within cycles

A further complication, and worthy of a file note, is that any increases to the rent due, or to the length of the lease, or even a change in the area occupied, may be liable to LBTT, but not necessarily immediately!

Such variations would normally be reportable at the next three-yearly review date (three years, six years, nine years etc from the effective date the lease started).

So, there may be two separate interlocking cycles. Landlords will often want to review a lease for possible increases in rent every five years, but LBTT returns have a three-years cycle. Therefore, a rent increase at year five, would be reportable under LBTT in year six.

Good news, bad news

There is a real opportunity here for accounting and audit staff to turn potential bad news into good news. Missing an LBTT deadline can mean £1,000 in penalties, even if no tax is due. But the position might not be as bad as clients think.

The good news is that some leases should not really be in the system at all. They were put into the system as a 'fail-safe' by the landlord's solicitors. Many leases need 'nil returns', on which there is no additional tax to pay. Therefore, do not assume there will be a tax bill, and advise clients to get the position checked out first.

If their lease should not have been there initially, there would be nothing to pay now and, if they contact Revenue Scotland, the need for a return in future could be extinguished. This could apply, for example, with leases for less than seven years, and under £150,000 Net Present Value. For a full list of leases which are notifiable/not notifiable, see [LBTT4003 - Notifiable transactions](#).

Revenue Scotland is being particularly understanding during the pandemic. It has said that where a three yearly review return was due in Covid-19 period and was sent in late, then no penalties will be charged. But do not delay, it only applied to returns due during the current pandemic.

Example – 3-year reviews (additional tax payable) – relevant date

A flower shop was let to a Tenant for 15 years from 2015. The annual rent payable was £45,000. The Tenant submitted a LBTT lease return and their payment of £3,682. Paid to Revenue Scotland within 30 days (of the effective date).

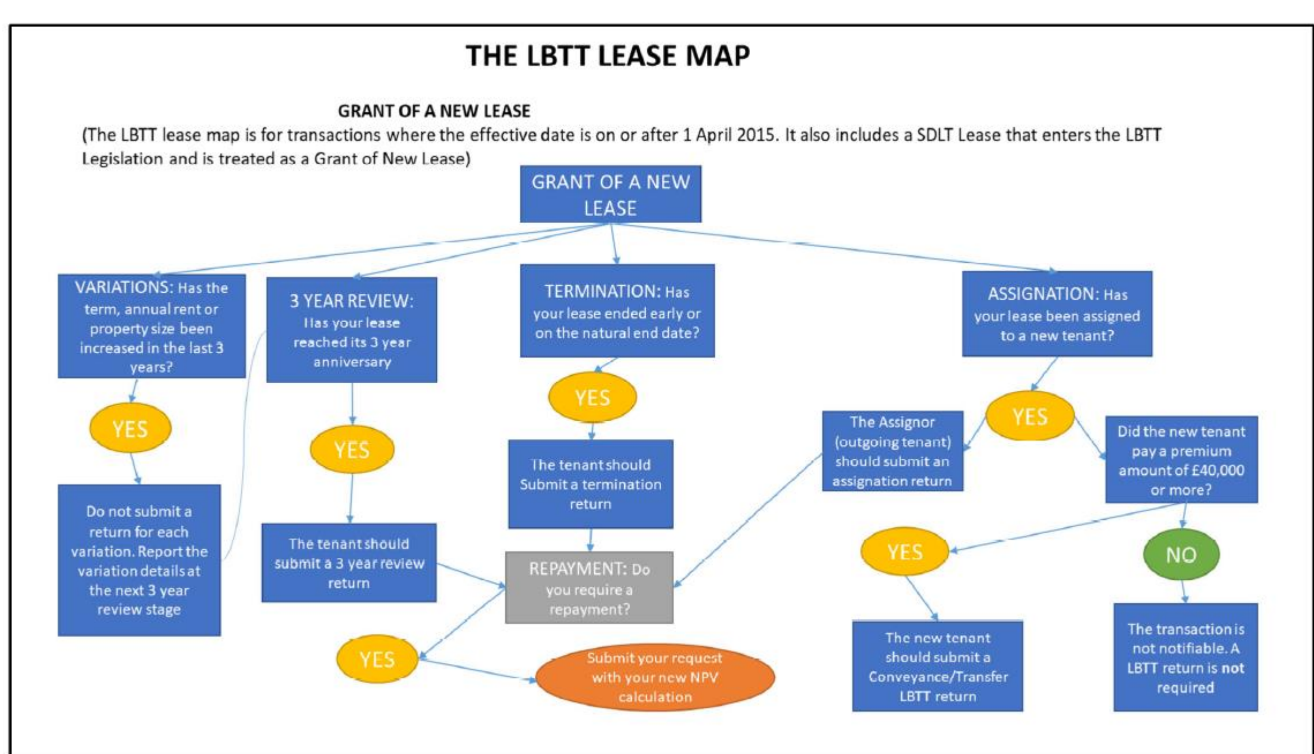
The first 3-year review was due in 2018. Tenant submitted their 3-year review returns in 2018 and 2021 and so on.

But in 2022 (i.e., between 3-year cycles), the landlord increased the rent to £70,000 pa. Tenant submitted their next 3-year review return in 2024 and included details of variation to the annual rent to £70,000.

Tenant submits their 3-year review return, and the net present value (NPV) needs to be re-calculated to see if there is any additional tax due. As the annual rent was increased in 2022, the calculation shows that additional LBTT of £1,548 is due on the transaction.

Tenant must submit a 3-year review return and an LBTT payment within 30 days of the return date.

How LBTT works – the LBTT map



Further information and contact details

LBTT and leases https://www.revenue.scot/land-buildings-transaction-tax/leases

Mailbox: lbtt@revenue.scot

[Opinions Service](#)

[Secure messaging service](#)

Support desk tel: 0300 020 0310

HMRC CLEARANCE APPLICATIONS

Statute provides that taxpayers can seek advance clearance from HMRC in several areas ranging from whether an issue of shares by a company will enable the subscriber to qualify for relief under the Enterprise Investment Scheme, to the purchase of its owns shares by a company, to name a few.

The most common situations where statutory clearances are sought in practice relate to company reconstructions, such as:

1. Share for Share Exchanges

Where a predator company seeks to acquire the target company for a consideration, which may involve cash paid up front, but also the exchange, by the existing shareholders, of their shares in the target for shares or loan notes issued to them by the predator.

In these circumstances, clearances are normally sought under:

- Section 701 ITA 2007 that HMRC is satisfied that no counteraction notice will be served under Section 698 ITA 2007, as the main purpose, or one of the main purposes of the transaction is not to obtain a tax advantage.
- Section 138 TCGA 1992 that HMRC is satisfied that the reconstruction will be effected for bona fide commercial reasons and does not form part of a scheme or arrangement of which the main purpose, or one of the main purposes, is the avoidance of liability to Capital Gains Tax (CGT).

Sometimes, the owners of a trading company will wish to interpose a new holding company, which they own, whereby the holding company issues shares to them in exchange for their shares in the trading company. The reason for this is often that the trading company has built up cash reserves, or has created a property business, and the owners wish to protect these assets from the commercial risks associated with trading. Having formed the holding company, the investment properties and surplus cash will be hived up to the holding company.

For clearances to be given, there needs to be a commercial reason for the transaction. Over several months, it has been reported that members have experienced a change in the attitude of HMRC, with detailed questions now being asked concerning, for example, the type of properties which will be bought by the proposed new holding company and what they will use them for. In the extreme, some clearances have been refused.

It is therefore advisable to provide HMRC with as much information as possible in the initial clearance application regarding the commercial rationale for share for share exchanges, so that they can provide the clearance sought without having to enter into further correspondence.

2. Purchase by a Company of its own shares

Where a company purchases its own shares, the default position is that the excess of the proceeds received over the amount paid by the original subscriber for the shares is subject to Income Tax as a distribution. If certain conditions are met, then the gain on disposal is subject to CGT. Clearances are normally sought under:

- Section 1044 CTA 2010 that the conditions for capital gains treatment are met.
- A Section 701 ITA 2007 clearance is normally sought at the same time, that a counteraction will not be issued.

3. Statutory Demerger

These are rare in practice, as clearance is not given where the demerger is in contemplation of the sale of one or more of the companies, post demerger. It is necessary for there to be a demerger of two trades for a statutory demerger to be possible. It is not possible where a company is seeking to demerge a property business, for example, from a trading business.

Where the conditions for a statutory demerger are met, then clearance can be sought under Section 1091 CTA 2010.

4. Non-Statutory Demerger – Capital Reduction

Businesses within a single company, or a group of companies, can be demerged to separate the businesses into different groups owned by the same shareholders or, alternatively, to allow one or more shareholders to receive a particular company with other shareholders receiving one or more other companies.

Frequently, however, such a demerger is utilised to separate a property investment business from an existing trading company, usually to remove investment assets from a risky trading company, but sometimes in contemplation of the sale of the trading company.

Clearances are sought under the following statutory provisions:

- Section 701 ITA 2007 (see above).
- Section 138(1) TCGA 1992 where a new holding company is created above the existing company, so that there is a sufficiently high share capital to reduce.
- Section 139 TCGA 1992 to ensure that HMRC is satisfied that the proposed transfer of the company being demerged will be effected for bona fide commercial reasons and does not form part of a scheme of arrangement of which their purpose, or one of the main purposes, is the avoidance of liability to tax.
- Section 748 CTA 2010 to ensure that HMRC is satisfied that under the proposed reconstruction, no counteraction notice will be served under Section 746 CTA 2010 as the transactions will be effected for genuine commercial reasons, and that enabling Corporation Tax advantages to be obtained is not the main object, or one of the main purposes, of any of the transactions.

It is not a requirement that clearance is obtained but when the facility is available, it is advisable to take advantage of it.

HMRC have thirty days in which to respond, and recently it appears that they are taking virtually the entire period allowed in which to respond. This period should be factored into the timetable for any proposed reconstruction.

Matters can be sped up by submitting the clearance application by email to reconstructions@hmrc.gov.uk, requesting that HMRC reply by email, if the requisite undertakings are provided to them that the client is willing to accept the risks of using email.

Non-statutory facility

As well as the statutory clearance facility, HMRC offer a non-statutory facility where there are areas of uncertainty. These can be quite diverse, but many have concerned the availability of Entrepreneurs' Relief, now Business Asset Disposal Relief, where the trading status of a company may be in doubt if, for example, it holds substantial cash deposits. HMRC have produced Annex A for most types of non-statutory clearance which sets out the information which they require, in a particular format.

This is a very useful facility where there are areas of uncertainty, but there are certain aspects which cannot be subject to a non-statutory clearance application. One of these is whether the anti-avoidance legislation which can, in certain circumstances, apply to treat proceeds of a member's voluntary liquidation as a distribution subject to Income Tax.

As noted above, Annex A is the checklist for clearance services which are most used. In addition, there are others for specific circumstances:

B. Business Investment Relief Advance Assurance checklist

C. Business Property Relief checklist

D. VAT clearance service

E. Only to be used in relation to closed years (where the enquiry window has closed) and where the taxpayer has registered to make an offshore disclosure via HMRC's digital disclosure service.

Useful information is contained in HMRC's manuals at ONSCG1000 onwards.

Details of the email address to which a non-statutory clearance application should be sent is provided in the relevant Annex.

HMRC try to deal with non-statutory clearance applications as quickly as possible, but the timescales will vary depending upon the complexity and pressure of work.

COMPATABILITY OF UK LAW WITH THE EU PRINCIPAL VAT DIRECTIVE REGARDING AFRS

The background to Messrs Harrison v HMRC

Messrs Harrison (Harrisons) is a farming partnership in Cumbria which buys, rears, and sells on cattle and sheep. Harrisons appeared before the First Tier Tribunal to challenge a decision by HMRC to refuse Harrisons the right to use the Agricultural Flat Rate Scheme (AFRS) which would allow the retention of a flat rate of 4% on sale of goods and services in lieu of filing returns and accounting for output and input VAT.

The dispute, and what is at stake

Harrisons had been registered for VAT since 1973, operating the standard system for preparing and filing VAT returns. Its application in December 2018 to join

AFRS was refused by HMRC because the flat rate addition of 4% on its annual turnover would total £114,000 which would be higher than its actual input VAT of £71,164 for the previous year.

HMRC considered that Harrisons faced no administrative difficulty in operating the normal VAT scheme and merely wanted AFRS certification to benefit financially. In HMRC's view it was entitled to deny Harrisons under the provisions of Regulation 204(d) of the VAT Regulations 1995. As stated in Notice 700/46 an applicant for AFRS should not stand to gain more than £3,000 in the year following application.

The appellant's arguments

Harrisons objected to HMRC's decision on several grounds. Firstly, they argued that Regulation 204(d) is ultra vires as regards the Principal VAT Directive. They pointed to Shields & Son Partnership v HMRC where the ECJ held it was for Member States to set flat rate compensation at a rate which prevents flat rate farmers as a whole benefiting from an amount greater than the input VAT charged, but also held that it is not contrary to EU law for an individual farmer to obtain greater compensation from the flat rate scheme than the input VAT recovery that he would have been able to deduct under the normal VAT arrangements. The VAT Directive cannot be interpreted as meaning farmers who recover substantially more under the flat rate scheme compared to normal VAT arrangements constitute a category of farmers who can be excluded from the scheme.

Harrison's second argument was that it was aware of competitor businesses allowed to operate AFRS despite achieving more than £3,000 annual benefit. Therefore, the principal of equal treatment was breached.

HMRC's response

HMRC counter argued that if Harrisons were correct in their analysis of the Shield case, then AFRS would no longer have the purpose of simplifying VAT arrangements for farmers. Instead, it would be open to all regardless of size, sophistication, and ability to operate the normal VAT arrangements.

In HMRC's view, the £3,000 test is an appropriate proxy for the Directive's requirement that "the flat-rate compensation percentages may not have the effect of obtaining for flat-rate farmers refunds greater than the input VAT charged." The Directive permitted the exclusion of certain categories of farmer including those for whom the normal VAT arrangements are not likely to give rise to administrative difficulties.

The decision

The Tribunal acknowledged it had difficulty in deciding whether the refusal of AFRS was ultra vires from the perspective of EU law, but on balance favoured HMRC's arguments. A key point in the Tribunal's reasoning was that the Shields case was not on all fours with Harrisons since Shields was already using AFRS. There was insufficient clarity for Shields to know in advance when AFRS would be withdrawn from it for protection of the revenue. However, Harrisons faced no uncertainty as it would have been foreseeable that the advantage created by use of AFRS would have exceeded £3,000.

The Tribunal also noted that the ECJ made clear that AFRS, as an exception to the normal rules of VAT, must be narrowly construed, and the exceptions (i.e., those who cannot fall within it) must be broadly construed. AFRS's purpose is to address the difficulties which the normal VAT rules cause small farming businesses, and EU law permits Member States to exclude farmers from the scheme where the normal rules are unlikely to create administrative difficulties.

The Tribunal had less difficulty in dismissing Harrison's alternative argument that it suffered unequal treatment compared to farmers using AFRS and benefiting more than £3,000 annually. Harrisons presented no evidence of other farmers being admitted to AFRS despite not satisfying the UK stipulation that the anticipated benefit should not exceed that limit. In addition, the mere reliance on the Shields case on that point was fatally damaged by the fact that Shields qualified for entry to AFRS at the outset, unlike Harrisons.

TAX & HMRC UPDATES

Self-Assessment Late Payment Penalties

HMRC has announced that Self-Assessment customers will not be charged the initial 5% late payment penalty if they pay their tax or make a Time to Pay arrangement by 1 April.

The payment deadline for Self-Assessment was 31 January and interest will be charged from 1 February on any amounts outstanding. The deadline itself has not changed, but this year, due to the impact of Covid-19, HMRC is giving taxpayers more time to pay or set up a payment plan.

Payment plans or payments in full must be in place by midnight on 1 April to avoid a late payment penalty.

Anyone worried about paying their tax should contact HMRC for help and support on 0300 200 3822.

HMRC to accept bulk appeals for late tax returns

Agents will be able to complete a bulk appeal form for late filing penalties, but only for individuals/ businesses who could not file their self-assessment tax return due to Covid-19. The new process is available from 24 March on gov.uk, for six months.

Online VAT Deferral New Payment Scheme

Over half a million businesses that deferred VAT payments between March and June 2020, under the VAT Payment Deferral Scheme, will now be given the option to pay their deferred VAT in equal consecutive monthly instalments from March 2021.

Businesses are required to opt-in to the VAT Deferral New Payment Scheme via the online service that opened 23 February and closes on 21 June 2021.

Payments can be spread into two to eleven equal monthly instalments, interest free. The earlier businesses opt-in, the more instalments that are available to help spread the cost.

SME Brexit Support Fund

The SME Brexit Support Fund is now open for applications. Provided certain eligibility criteria are met, HMRC may provide funding towards the costs of training and/or professional advice, to help with changes to trade rules with the EU.

Traders can apply for up to £2,000 in total. Find out more about each grant here.

NMW increases in April

The National Minimum Wage and National Living Wage rates will increase on 1 April.

In addition to the new rates, the age from which workers become eligible for the National Living Wage will be lowered. From 1 April all workers aged 23 and over must be paid the National Living Wage or above.

Review the new rates of pay at Gov.uk.

HMT publishes super-deduction factsheet

HM Treasury (HMT) has published a factsheet covering the new super-deduction announced in the 2021 budget, which will allow companies to cut their tax bill by up to 25p for every £1 they invest in qualifying assets.

Broadly, between April 2021 and 31 March 2023, companies investing in qualifying new plant and machinery assets will be able to claim:

- A 130% super-deduction capital allowance on qualifying plant and machinery investments; and
- A 50% first-year allowance for qualifying special rate assets.

Reduced VAT rate for hospitality extended

The temporary reduced VAT rate of 5% has been extended until 30 September 2021 for food and non-alcoholic drink sales.

Thereafter, a new rate of 12.5% will apply for 6 months from 1 October 2021 to 31 March 2022, before it returns to 20% from 1 April 2022.

VAT Return – Digital Links

Businesses will be required to have digital links between software programs on their first VAT return starting on or after 1st April 2021.

A digital link is an electronic or digital transfer, or exchanging of data, between software programs, products, or applications. HMRC accepts a range of digital links.

HMRC are hosting several webinars over the coming weeks where digital links and how to meet the appropriate requirements will be fully explained.

Bounce Back Loan repayment terms extended to 10 years

Businesses that took out government-backed Bounce Back Loans to get through Covid-19 will now have greater flexibility to repay their loans.

Borrowers now have the option to tailor payments according to their individual circumstances with the option to extend the length of the loan from six to 10 years, make interest-only payments for six months or pause repayments for up to six months.

This will mean that businesses can choose to make no payments on their loans until 18 months after they originally took them out.

The Pay as You Grow (PAYG) options will be available to more than 1.4m businesses which took out a loan.

HMRC identity verification letters – repayments

When a taxpayer submits a Self-Assessment tax return resulting in a repayment of tax being owed to them, HMRC undertakes routine checks to ensure the claim is genuine and to identify potential compliance risks.

Where risk indicators suggest that the taxpayer or the claim may not be legitimate, HMRC will contact the taxpayer to confirm their identity. This will include the requirement for the taxpayer to provide documentary evidence to prove who they are, and to answer some basic questions with regards to the repayment request they have submitted.

HMRC recognise that a small number of genuine claimants may receive their letters. HMRC try to keep this process as simple and as possible, but the taxpayer must still respond as requested to such a letter.

If the taxpayer is uncertain about any aspect of the correspondence or needs additional support, they should contact HMRC on the official Self-Assessment helpline number provided.

Delay in 5MLD registration deadline for non-tax paying trusts

ICAS attended an HMRC stakeholder meeting in March, at which HMRC confirmed that availability of the IT registration system for 5MLD non-tax paying trusts will be delayed. As a result, HMRC subsequently made the following announcement extending the registration deadline for affected trusts:

"As you are aware the Trust Registration Service will be extended to enable non-tax paying trusts to register in compliance with the Money Laundering Regulations. We are now able to provide more detail on the timescales and registration deadlines:

- *We now expect the IT to open for registrations in summer 2021 rather than the spring.*
- *We appreciate this will be a cause for concern in terms of the current registration deadline of March 2022.*
- *We therefore intend to extend that deadline within the legislation in order to provide trustees and agents of existing trusts with approximately 12 months in which to register from the date of IT delivery.*
- *We will provide further updates and clarification on this in due course."*

HMRC Protective Assessments – Requirement to correct

HMRC are making assessments over the next few weeks in respect of offshore tax disclosed to them, following the introduction of the Requirement to Correct (RTC) legislation (Schedule 18 Finance (No2) Act 2017). The RTC extends some assessing time limits, which run out on 5 April 2021. Where a settlement has not yet been agreed with HMRC, and it is necessary to assess the tax, a protective assessment will be made shortly. A taxpayer's right to appeal, and ask for a postponement of tax, are just the same as usual.

The Worldwide Disclosure Facility is available for taxpayers to make a voluntary disclosure to HMRC. Through this process, taxpayers can bring their tax affairs up to date and, usually, cases are settled by way of a contract settlement. When taxpayers choose to disclose this way, they can self-assess their penalty, and most disclosures made this way will not result in an in-depth enquiry.

However, there are some taxpayers with historic tax liability disclosures with whom HMRC have not yet been able to conclude a contract settlement. HMRC is restricted by assessing time limits set out in legislation, and for some of those taxpayers where tax may fall outside those limits, HMRC will need to protect the tax that would otherwise be lost. HMRC will do this by sending those taxpayers tax assessments. This does not mean that HMRC cannot continue to engage with agents or taxpayers to agree their tax position for those years. If that is your client's preference, you should contact HMRC to arrange this.

If you represent one of those taxpayers who has tax that will fall out of the assessing time limits on 6 April 2021, HMRC will raise an assessment based on the taxpayer's disclosure and will write to you to advise you of the tax liability that HMRC have calculated. If your client does not agree with the assessment raised by HMRC, it is important that you or they write to HMRC to appeal it. The letter and attachments that HMRC will send out, set out the years HMRC needs to protect, the tax that is due, how to make a payment and what taxpayers should do if they disagree. Where there is an agent acting, HMRC will send a copy to them. Letters will be tailored to individual circumstances, particularly where there is an ongoing compliance check.

EMPLOYMENT CORNER

How should the cost of salaries for furloughed workers ordinarily engaged in R&D activity be treated?

Where an employer has had to ask staff not to work due to the coronavirus and has claimed furlough payments for them, this will undoubtedly have impacted on the R&D tax relief claim. Usually, the cost of employing staff engaged in R&D activity represents a significant proportion of the allowable pool in R&D tax relief claims.

Two main issues must be considered here:

1. The CJRS does not count as State Aid but is instead classed as a “general subsidy”. This means that furlough payments do not qualify under the SME scheme; and
2. To qualify for R&D tax credits, the employees must have been actively engaged in qualifying R&D activity, which means that the periods when they were at home and not working does not qualify for tax relief.

There will be employers who have chosen to top up the payments to 100% of salary and claimed the relevant percentage of salary (readers will recall this fluctuated between 80% and 60% between August and October 2020) and they will also have had to bear the cost of some employer’s NICs and pension contributions as well. Any employer’s NICs and pension contributions made by the employer that can be linked to furlough payments do not qualify.

The only amounts that qualify for SME R&D relief are payments of actual salary and associated employer’s NICs and pension costs when an employee has been actively working in the business, as well as associated sickness and holiday pay, so long as CJRS has not been claimed in respect of these payments. Such costs should be apportioned between qualifying R&D work and other work.

Where CJRS has been claimed on holiday or sick pay periods, which would otherwise have been apportioned to qualifying R&D, SME’s may be eligible to claim under the R&D Expenditure Credit (RDEC) scheme instead for this element. This is because RDEC is available to SME in relation to subsidised or subcontracted out expenditure.

Sick pay covered by Coronavirus Statutory Sick Pay Rebate Scheme is not eligible for R&D claims.

Universal credit for the self-employed - nil returns during the pandemic

The DWP have asked ICAS to raise awareness of the continuing need for Universal Credit claimants to make monthly submissions of their self-employment income, even when they are temporarily not trading due to the pandemic.

Nil returns are a requirement of Universal Credit and any self-employed claimants should be directed to the guidance which says:

‘At the end of each monthly assessment period, you’ll need to report:

- *how much you earned from self-employment, even if it is nothing;*
- *any money you paid into a pension; and*
- *information about your business.*

This also applies to company directors, even those paying themselves by PAYE.’

Kickstart scheme drops minimum threshold of 30 jobs

The government has opened the kickstart scheme up to smaller employers after removing the limit that required organisations to create a minimum of 30 vacancies to apply directly.

The scheme provides funding towards the creation of new job placements for individuals aged between 16 - 24, who are in receipt of Universal Credit and potentially facing long term unemployment.

The government will pay 100% of the National Minimum Wage or National Living Wage for 25 hours a week, covering a period of six months. In addition, they will fund the associated employer National Insurance and minimum employer auto enrolment pension contributions.

View the updated guidance for a full summary.

TECHNICAL BULLETIN

ISSUE NO. 157
MARCH 2021

EDITORIAL BOARD

James E Barbour	Director, Policy Leadership, Accounting & Auditing ICAS
Anne Adrain	Head of Sustainability and Corporate & Financial Reporting
John C Cairns	Partner, French Duncan LLP
Jeremy E Clarke	Assistant Director, Practice Support, ICAS
Kate L Neilson	Practice Support Specialist, ICAS
Elaine M Dyer	Partner, Martin Aitken & Co Ltd
Philip McNeill	Head of Taxation (Tax Practice and Owner Managed Business Taxes), ICAS
Justine Riccomini	Head of Taxation (Scottish Taxes, Employment & ICAS Tax Community), ICAS
Guy Smith	Senior Tax Manager, inTAX Ltd
Ron Weatherup	Director, Lugo
Liz Smith	Business Development Director, Lugo
Lynn Gemmell	Director, Gemmell McGee VAT Solutions

SUBSCRIPTIONS & ENQUIRIES

Jeanette Rorison — Customer Champion, Practice Support

practicesupport@icas.com

Contact us

CA House, 21 Haymarket Yards, Edinburgh, UK, EH12 5BH

+44 (0) 131 347 0100

connect@icas.com | icas.com

@ICASaccounting ICAS – The Professional Body of CAs

Although care has been taken in the production of this Technical Bulletin, it is a summary only of the topics discussed. Any views expressed by contributors within this publication are their personal views and not necessarily the views of ICAS. Neither ICAS nor the members of the editorial board shall be liable for negligence in the preparation, presentation or publishing of the material contained herein, nor for the correctness or accuracy of that material, nor for actions, failures to act, or negligence on the part of those to whom the material is disseminated, which results in any liability, loss, claim or proceedings whatsoever and howsoever caused by, on behalf of, or against any person.

© Copyright 2020 ICAS. It is understood that reproduction of the contents of this Technical Bulletin as purchased by a firm shall not constitute an infringement of the Institute's copyright provided always that such reproduction shall be limited for the purpose of training and administration within the firm or the private study of partners or employees thereof and for no other purpose whatsoever.