Tax Matters

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Welcome to the latest edition of the TLT Tax Team's "Tax Matters". In this edition, we have covered recent developments across the taxes including employment income tax, off-payroll working and VAT. If you would like to discuss any item in further detail, please speak to a **key contact**.

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Tax Administration and Maintenance Day 2024

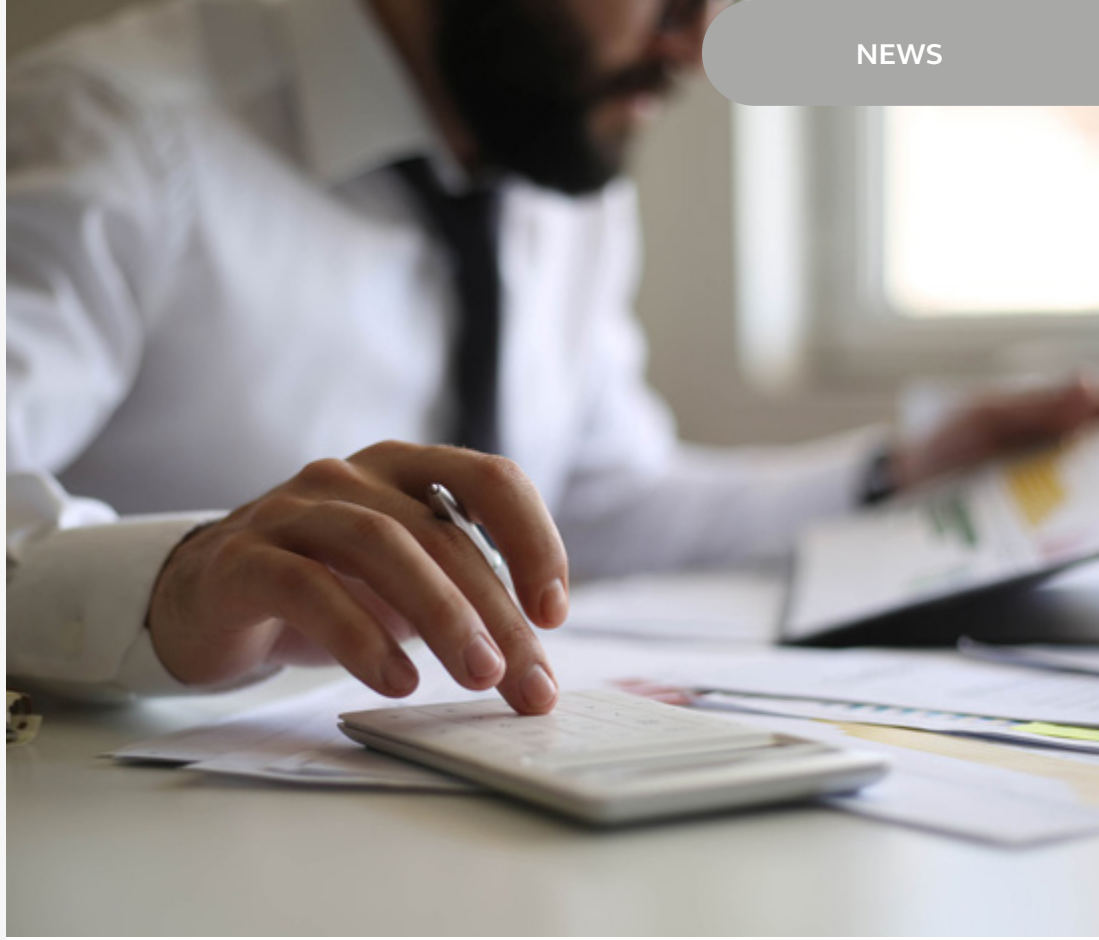
The Government's latest Tax Administration and Maintenance Day 2024 took place on 18th April 2024 and a small number of technical tax policy proposals were announced.

The following consultations were announced:

- consultation on the VAT treatment of Private Hire Vehicles – this consultation seeks to understand the potential impacts of two High Court judgments (in the Uber cases) on the private hire vehicle sector and its passengers and to explore ways to mitigate any undue adverse effects of those judgments on the private hire vehicle sector;
- consultation on draft regulations to mandate employers operating in a Freeport or Investment Zone special tax site to provide their employee's workplace postcode to HMRC if they are claiming the relevant secondary Class 1 National Insurance contributions (NICs) relief through their payroll; and
- consultation on the VAT treatment of charitable donations (to be launched later this year) – to encourage charitable giving, the Government is proposing to introduce a targeted VAT relief for low value goods which businesses donate to charities for the charities to give away free of charge to people in need.

The Government continues to be focused on tackling non-compliance in the umbrella company market and although no response to the closed consultation on that market was published, the Government announced that it is minded to introduce a due diligence requirement to exclude non-compliant umbrella companies from labour supply chains. The Government will continue to engage with the recruitment industry and other key stakeholders on the detail of a statutory due diligence regime for businesses that use umbrella companies, and ensure it has the best understanding of the impacts that this could have on reducing non-compliance.

Not unexpectedly, no further details were published in relation to the proposals, announced at the Spring Budget 2024, to abolish the existing tax rules for non-domiciled individuals and replace them with a residence-based regime. However, HMRC held a series of "listening events" last month to hear external views on the reforms and has announced that it will publish further information on how the Government plans to engage on the technical detail of the legislation in due course.



We continue to await responses to the closed consultation on the Taxation of Employee Ownership Trusts and Employee Benefit Trusts and the closed call for evidence in relation to the SIP and SAYE incentive schemes.

No draft legislation was published for consultation in relation to the proposal to extend full capital allowances expensing to assets for leasing. However, the HMRC Treasury led technical consultation on capital allowances launched earlier this year will continue throughout 2024.

WHY IT MATTERS?

Businesses impacted by the recently announced consultations will need to monitor the outcomes from those consultations.

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VAT on professional fees connected to sale of subsidiary irrecoverable: *Revenue and Customs Commissioners v Hotel La Tour Ltd*

LEGAL ISSUE

The legal issue for the Court of Appeal in this case was whether Hotel La Tour Ltd (**HLT**) could deduct VAT input tax incurred in connection with a sale of shares in a subsidiary company.

CASE DETAIL

HLT is a holding company and owned the share capital of Hotel La Tour Birmingham Ltd (HLTB). HLT and HLTB were a VAT group with HLT as the representative member.

HLTB owned and operated a luxury hotel in Birmingham and HLT provided HLTB with management services including the provision of key personnel for the hotel business.

In 2017, HLT sold the shares in HLTB for the net amount of £16,000,000, comprising consideration for the shares and repayment of a loan made by HLT to HLTB less the costs of sale including the fees for professional services (**Services**). The Services, costing HLT £382,899.51 plus VAT of £76,822.95, were provided by marketing agents, solicitors and chartered accountants.

HLT intended to, and did, use the proceeds of sale to part-fund the development of a new hotel.

Subsequently, HLT sought repayment of the input tax incurred on the Services but following enquiries (and an internal review), HMRC disallowed the repayment of the input tax on the basis that the Services were used to make a supply of shares on which VAT is not deductible because it is a VAT exempt supply.

The First Tier Tribunal (**FTT**), relying significantly on the Court of Justice of the European Union case of Skatteverket v AB SKF (**SKF**) found in favour of HLT, deciding that the VAT on the Services was recoverable because there was a direct and immediate link between the costs incurred and HLT's taxable business of building and developing and the eventual management of the new hotel.

The Upper Tribunal (**UT**) agreed with the FTT decision and HMRC appealed to the Court of Appeal.

CASE OUTCOME

The case of SKF was considered in detail by the Court of Appeal which determined that the SKF case established only that inputs incurred in connection with the sale of shares could, in theory at least, be attributed to overheads if (and only if) there was no direct and immediate link established by way of direct attribution to the share sale.

The Court held that SKF preserved the existing rules i.e. that input tax incurred on services having a direct and immediate link with an exempt supply of shares is irrecoverable, although such input tax may have a direct and immediate link either with the share sale or with the taxpayer's business as a whole (that being a matter for the domestic court to determine).

The Court of Appeal concluded that the inputs incurred by HLT in respect of the Services were used in, were cost components of, were directly and immediately linked with, the exempt share sale and therefore they were irrecoverable by HLT. The Court was not persuaded that the existence of a VAT group between HLT and HLTB at the time of the share sale altered their conclusion and therefore HMRC's appeal was allowed.

WHY IT MATTERS

The Court of Appeal decision has narrowed the circumstances in which a company will be able to recover input tax incurred in connection with the sale of a subsidiary for fundraising purposes. Taxpayers who had been hoping to make additional claims for input tax following the FTT and UT decisions will be disappointed by this decision.

- Read the judgment here.

Discretionary transaction bonuses taxable as employment-related benefits: *OOCL UK Branch v The Commissioners for His Majesty's Revenue and Customs*

LEGAL ISSUE

In this case payments were made to a number of employees by a shareholder of the employer company. The First Tier Tribunal (**FTT)** had to determine if those payments were earnings from the employees' employment. If they were, then the payments would be chargeable to income tax under s62 of the Income Tax (Earnings and Pensions) Act 2003 (**ITEPA**) and employee and employer National Insurance Contributions (**NICs**).

CASE DETAIL

Mr Tung was the chairman and majority shareholder of Orient Overseas Container Line Limited (**OOCL**). In July 2017, OOCL was the subject of a takeover bid resulting in the sale of Mr Tung's interest in OOCL. In August 2018, Mr Tung resigned as a director of OOCL but shortly before doing so he informed the employees of OOCL that he wished to make a special discretionary payment to each of them, funded by the Tung family. The payments were described as a "bonus" and were each a multiple of monthly salary. 99 UK employees received a payment via OOCL's payroll from which income tax (under PAYE) and NICs were deducted.

OOCL subsequently sought repayment from HMRC of the PAYE income tax and NICs deducted from the payments on the basis that the payments were neither emoluments from the employment nor paid by reason of the employment.

HMRC refused the repayment claim and OOCL therefore appealed to the FTT.

CASE OUTCOME

The FTT held that the payments were not income "from" employment and therefore were not taxable under section 62 of ITEPA. The FTT were not satisfied that the payments were made for either past or future services rendered by the employees. Further, (i) the payments were non-contractual, voluntary and not expected by the employees, (ii) the payments were not part of a regular pattern of payment and would not be repeated, (iii) each employee was paid a market rate of salary and performance related bonus without reference to the payments, and (iv) the full cost of the payments was borne by Mr Tung funded from the sums he received from the share sale (and therefore could not have been made on that same basis by OOCL).

However, this did not mean that the payments were free of income tax and NICs as they were found to be taxable as employment-related benefits under section 201 of ITEPA. It was not contested that in order to receive a payment each recipient had to be an employee and the FTT determined that the only relationship of substance between Mr Tung and the recipients was that he was the chairman and majority shareholder of their employer. Employment was therefore a cause of the payments which were made by reason of employment.

WHY IT MATTERS

This case confirms that cash transaction bonuses paid to employees in connection with the successful sale of their employer (or a parent company) will almost always be subject to income tax and NICs even when the payments are discretionary and irrespective of whether the payments are funded by the employer, a parent company or a shareholder.

- Read the judgment **here**.

Material errors in First Tier Tribunal IR35 decision: *The Commissioners for His Majesty's Revenue and Customs v RALC Consulting Limited*

LEGAL ISSUE

In this case HMRC appealed to the Upper Tribunal (**UT**) against a decision of the First Tier Tribunal (**FTT**) in relation to the application of the intermediaries legislation in section 49 of the Income Tax (Earnings and Pensions) Act 2003 (**ITEPA**) to three sets of contractual arrangements involving Mr Alcock, RALC Consulting Limited (**RALC**), an agency and two end clients.

CASE DETAIL

RALC provided the services of Mr Alcock, an IT consultant, via an agency to two end clients - Accenture (UK) Limited and the Department for Work and Pensions. At all material times, Mr Alcock was the sole director of, and the sole shareholder in, RALC.

HMRC assessed RALC to income tax under PAYE and National Insurance Contributions (**NICs**) on the payments received by RALC in respect of the arrangements on the basis that the intermediaries legislation applied and RALC appealed to the FTT.

The FTT had to decide whether income tax and NICs were payable pursuant to the intermediaries legislation which involved deciding whether the hypothetical contracts between Mr Alcock and the end clients would have been contracts for services (meaning that Mr Alcock would have been self-employed) or contracts of service (meaning that Mr Alcock would have been employed).

The FTT determined that the intermediaries legislation could not apply to the engagements on the basis that there was insufficient mutuality of obligation between Mr Alcock and the end clients in the hypothetical contracts to establish an employment relationship. RALC's appeal against HMRC's income tax and NICs assessments was therefore allowed. HMRC appealed to the UT.

CASE OUTCOME

The parties agreed that a helpful approach to addressing appeals under the intermediaries legislation is the three-stage process adopted by the Court of Appeal in the case of Atholl House being: (i) find the terms of the actual contractual arrangements and relevant circumstances within which the individual worked; (ii) ascertain the terms of the hypothetical contract between the worker and the end client; and (iii) consider whether the hypothetical contract would be a contract of employment.

However, the UT found that although the FTT had directed itself that it should adopt the above approach, it made material errors in law in not properly constructing a hypothetical contract for each of the engagements and in failing to properly consider whether the resulting hypothetical contracts would be employment contracts.

The UT also determined that the FTT had made further errors in law in its application of the concept of mutuality of obligation. In particular, the UT stated that:

- the fact that the deemed employer is not under any obligation to provide further work and the deemed employee is not under any obligation to accept any further work that is offered does not prevent mutuality of obligation existing within an engagement under which work is offered, the worker does the work offered, and the worker is paid; and
- the lack of any guarantee of a minimum number of hours' work and the right of the deemed employer to terminate the arrangement at will are not inconsistent with mutuality of obligation in relation to an individual engagement, if there is mutuality of obligation whilst the contract subsists.

The UT set aside the decision of the FTT and remitted the appeal back to the FTT.

WHY IT MATTERS

This case is a reminder for all businesses involved in engaging workers via personal service companies (and particularly for those end clients responsible for preparing status determination statements) of the approach that a tribunal will take in determining if an employment relationship exists between the worker and the end client.

- Read the judgment **here.**

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Evidence of supplies in VAT invoices: *Fount Construction Limited v HMRC*

LEGAL ISSUE

In this case, a number of VAT invoices were issued to Fount Construction Limited (**FCL**) which made a claim to HMRC to recover the input tax set out in those invoices. The issue for the First Tier Tribunal (**FTT**) was whether those invoices contained sufficient information to constitute valid VAT invoices for the purposes of regulation 14(1) of the Value Added Tax Regulations 1995 (**Regulation 14**), and therefore whether the input tax was recoverable by FCL.

CASE DETAIL

FCL had received three invoices from Landcore Limited totalling £15,218.58. The invoices contained the address of a building site and a single description "Building Works at the above". The invoices also specified that VAT was calculated at the standard rate and included a VAT-exclusive subtotal, the VAT amount and the overall total.

HMRC disallowed FCL's claims for recovery of the input tax on the basis that the invoices did not meet the relevant legislative requirements of Regulation 14 which requires that a VAT invoice should include:

- a description sufficient to identify the services supplied; and
- for each description, the extent of the services and the rate of VAT and the amount payable, excluding VAT.

FCL appealed against HMRC's decision.

CASE OUTCOME

The FTT did not agree with HMRC's suggestion that the invoice description needs to be in such detail as to enable HMRC to draw definitive views on the VAT treatment of the supply from the invoice alone. The FTT went on to state that "the invoice is the gateway into any enquiries by HMRC, rather than a repository for the answers to any questions that might be asked".

The FTT concluded that a general short description of the nature of the services (such as "Building Services"), along with some further identifying information such as the name of the site, the contract or the date of works, will be sufficient to meet the requirements of Regulation 14.

Accordingly, FCL's appeal was allowed.

WHY IT MATTERS

This is a common sense decision from the FTT which will come as a relief to both issuers and recipients of VAT invoices given the impact that failure to comply with the requirements of Regulation 14 can have on the recipient's input VAT recovery.

However, since HMRC has wide ranging powers to seek further information in relation to a supply (as referenced by the FTT in the decision), businesses may wish to check that sufficient identifying details are provided in their VAT invoices to avoid delays in their input tax recovery.

- Read the judgment **here.**

Updated HMRC guidance on the VAT treatement of voluntary carbon credits

What are voluntary carbon credits?

Carbon credits are transferable instruments which are created by an independently verified carbon-crediting project and which remove carbon dioxide from the atmosphere, reduce emissions below a projected amount or avoid emissions which would otherwise occur.

Each carbon credit represents a reduction or removal of one metric tonne of carbon dioxide or an equivalent amount of greenhouse gases, from the atmosphere measured by reference to a baseline scenario.

Voluntary carbon credits are typically purchased by businesses as part of their Environmental, Social and Governance strategy to enable them to offset their own emissions and reduce their carbon footprint.

How are voluntary carbon credits treated for VAT purposes?

Voluntary carbon credits are currently treated as outside the scope of UK VAT.

The rationale for this VAT treatment was that when voluntary carbon credits were first introduced, HMRC's view was that they could not be incorporated into an onward supply and there was no evidence of a secondary market.

What is changing and why?

HMRC's "Revenue and Customs Brief - VAT treatment of voluntary carbon credits" confirms a significant change in HMRC's policy in relation to the VAT treatment of voluntary carbon credits. This change in policy means that VAT at the standard rate will need to be accounted for on the sale of voluntary carbon credits where the place of supply is in the UK.

The change in policy is the result of significant developments in the voluntary carbon credit market, including secondary market trading and businesses incorporating voluntary carbon credits into their onward supplies.

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Will the new VAT treatment apply to all activities involving voluntary carbon credits?

No. The Revenue and Customs Brief provides that the following activities in relation to voluntary carbon credits will remain outside the scope of VAT:

- the first issue of a voluntary carbon credit by a public authority;
- the holding of voluntary carbon credits as an investment, where there is no economic activity;
- donations made to voluntary carbon credit projects; and
- sales of voluntary carbon credits from self-assessed projects with no independent or third-party verification.

HMRC has also confirmed that VAT relief will be granted under the Terminal Markets Order to contracts in taxable voluntary carbon credits traded on terminal markets. This means that the zero rate of VAT will apply when voluntary carbon credits are traded under that order.

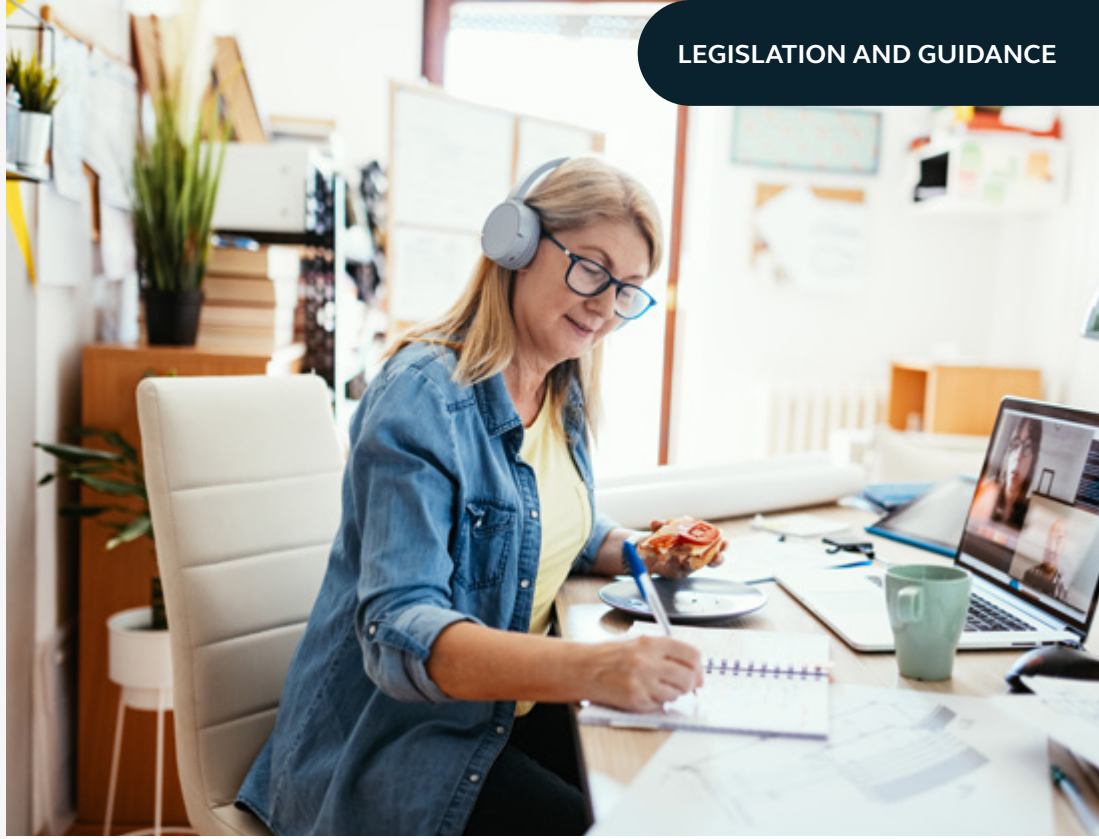
When does the change take effect?

The new VAT treatment will apply to voluntary carbon credits from 1 September 2024.

WHY IT MATTERS

Businesses who create, sell or buy voluntary carbon credits need to be aware of the forthcoming change to the VAT treatment of voluntary carbon credits to ensure that the correct rate of VAT is applied from September 2024.

Travel expenses for remote and hybrid workers - updated HMRC guidance



For some time HMRC has been grappling with the tax implications of remote and hybrid working, including the availability of travel expense deductions.

In fact, this was one of the key areas of focus of the policy paper (Hybrid and distance working report: exploring the tax implications of changing working practices) issued by the Office of Tax Simplification in December 2022 in which it was noted that a number of tensions and misunderstandings are created by applying the established travel expenses tax rules to new working patterns.

The reimbursement by an employer of an employee's travel expenses will be exempt from tax if the expense is tax deductible for the employee. The general principle that applies to travel expense deductions is relatively straightforward – being that an employee is not permitted tax relief for the cost to the employee of any journey which constitutes "ordinary commuting" or "private travel" – however the practical application gives rise to a number of complexities.

"Ordinary commuting" means any travel between a permanent workplace and the employee's home or any other place which is not a workplace. What does that mean for an employee who works remotely? Does there home become a permanent workplace so that travelling between home and another office is not "ordinary commuting"? Based on HMRC's guidance, this is only likely to be the case where the employee performs substantive duties of their employment at home as an objective requirement of their job. However, HMRC will only usually accept that working at home is an objective requirement of the job if the employee needs certain facilities to perform those duties and those facilities are only practically available to the employee at their home.

Even if HMRC will accept that the employee works at home as an objective requirement of the employment, HMRC's guidance is clear that tax relief for the cost of travel between their home and their permanent workplace will only be due for travel made on days where the employee's home is a workplace. So, for example, if the employee works in their employer's office on Monday to Thursday but the job requires the employee to work from home every Friday, the employee will get tax relief for the expense of traveling between the office and their home on Friday but not on any other days.

The latest update to HMRC's guidance specifically addresses the common scenario where an employee is given the opportunity (but is not required) to work from home on a flexible basis and makes it clear that where the employee has a base office from which they can work (although they may choose not to do so) journeys from home to that base office will be treated as "ordinary commuting" meaning that the employee cannot claim tax relief on those journeys.

WHY IT MATTERS

It is important for employers reimbursing the cost of employee travel expenses to understand the tax implications of that reimbursement, particularly where employees work remotely or on a hybrid basis. Each employee's personal circumstances will need to be reviewed to ensure that the employer is complying with its tax obligations and employers will need to monitor changes to working patterns on an ongoing basis.

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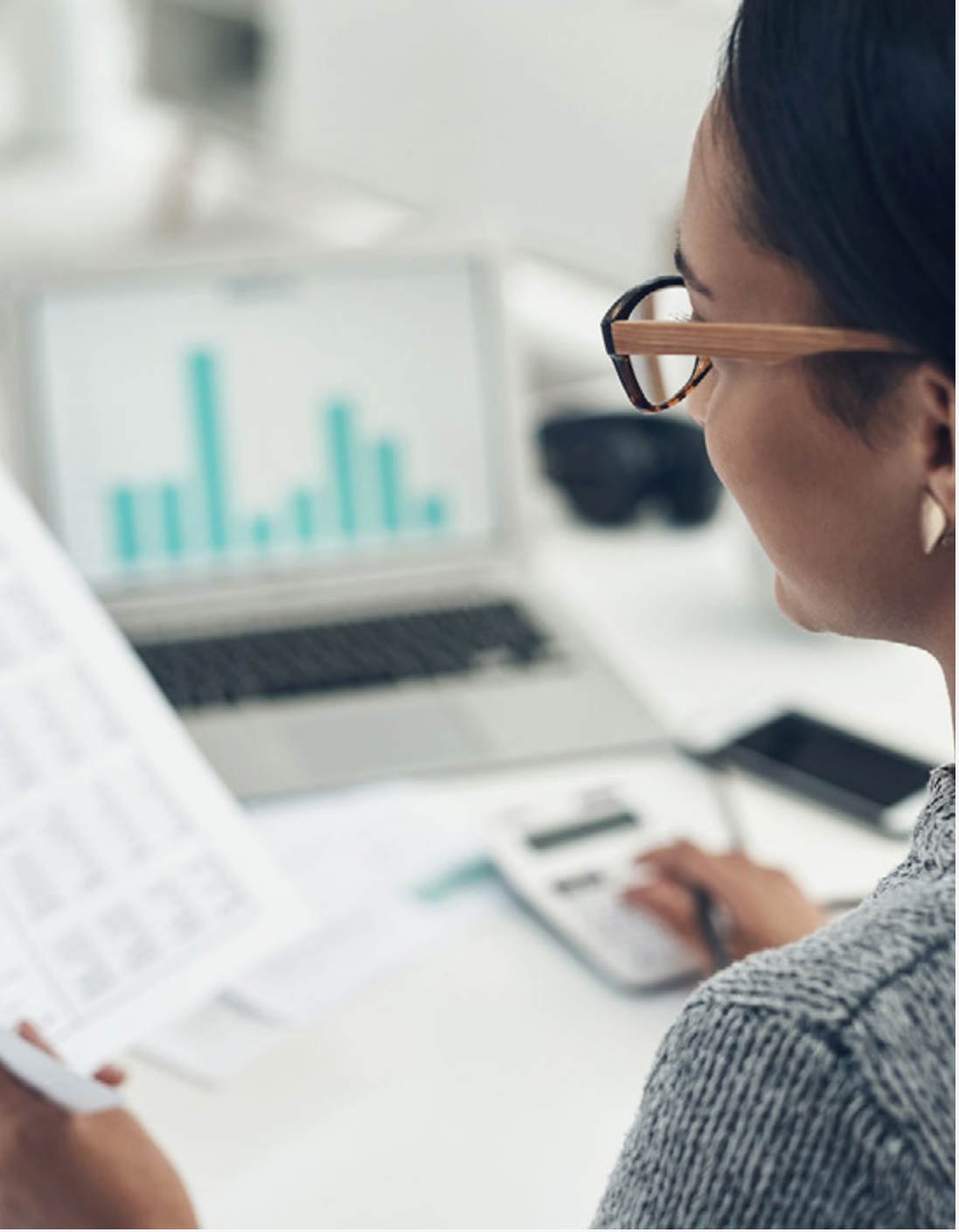

Looking ahead

Key tax developments to look out for over the next quarter:

30 June 2024

- Expiry of the 6-month extension period to the agreement for the repeal of digital services tax between UK, Austria, France, Italy, Spain and the US.

3 July 2024

- Court of Appeal scheduled to hear the appeal in G E Financial Investments v HMRC relating to residence and permanent establishment under the UK/US double tax treaty.

6 July 2024

- Deadline for online filing of annual Employment Related Securities returns with HMRC.

8 August 2024

- Final date for responses to HMRC's consultation on the draft regulations to mandate employers operating in a Freeport or Investment Zone special tax site to provide their employee's workplace postcode to HMRC if they are claiming the relevant secondary Class 1 National Insurance contributions (NICs) relief through their payroll.

Key contacts

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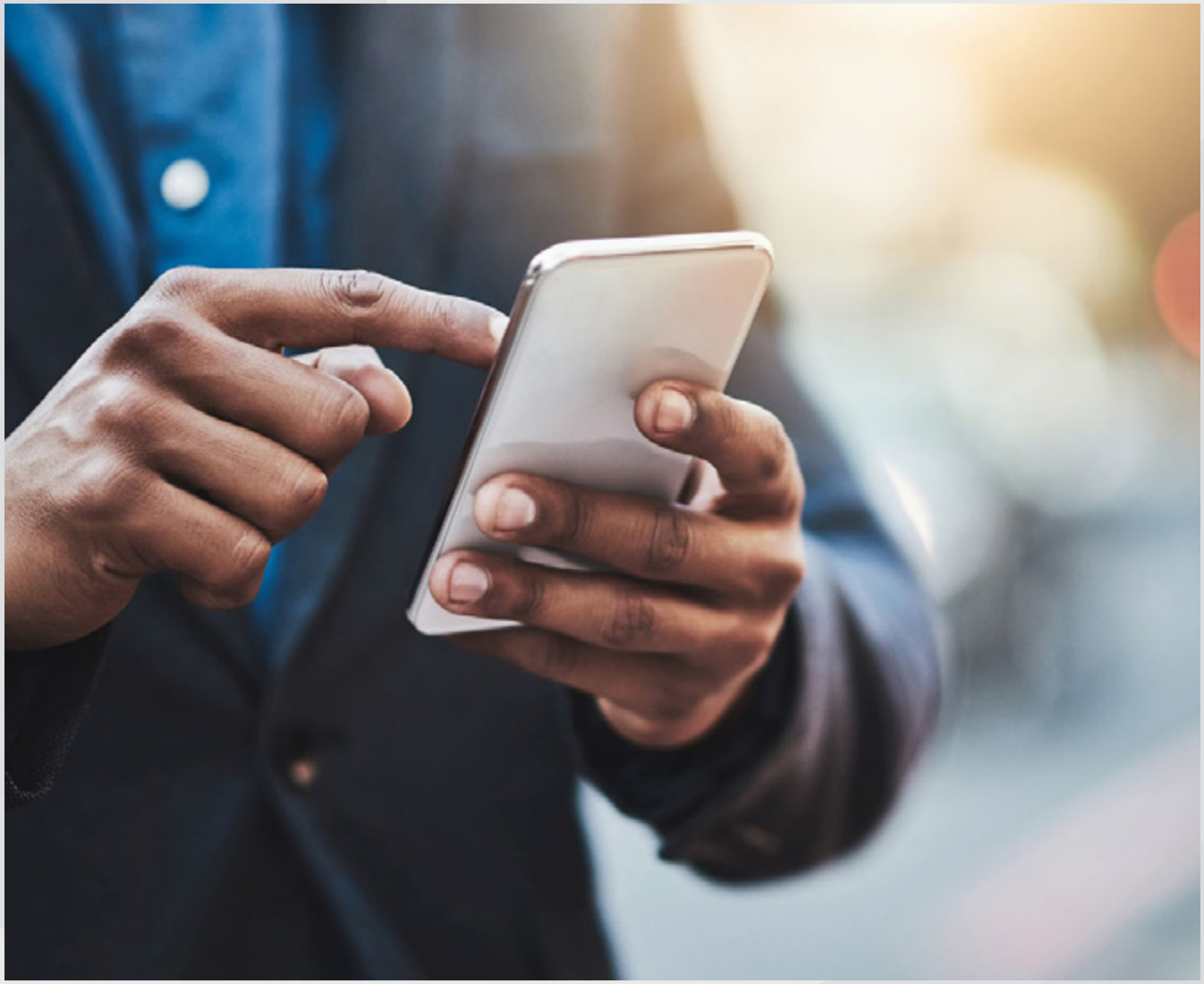

For what comes next
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