# Tax update

November 2018

**In this month's update we report on (1) proposals under consideration by the Treasury to extend capital gains tax relief to private landlords; (2) HMRC's factsheet on new higher penalties that it can impose where taxpayers have failed to declare and pay tax in relation to offshore matters; and (3) the annual report of Tax Inspectors Without Borders (TIWB). We also comment on three recent decisions relating to (1) the partial writing-off of loans; (2) Schedule 36 information notices; and (3) late filing penalties.**

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### Treasury considering capital gains tax relief for private landlords selling to long-term tenants

The Treasury is reported to be considering a proposal drawn up by the think-tank, Onward, to offer capital gains tax relief to private landlords who sell properties to their long-term tenants. more›

### Higher penalties for offshore matters

HMRC has published a factsheet on new higher penalties that it may charge in relation to offshore matters or offshore transfers that involve individuals and unincorporated businesses. more›

### TIWB's compliance initiative leads to an increase in tax revenues

Tax Inspectors Without Borders (TIWB) claims in its annual report that it is helping to increase domestic revenues by improving tax auditing and compliance in Europe, Africa, Latin America, the Caribbean and Asia. more›

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In *Douglas Atherley v HMRC*, the First-tier Tribunal (FTT) has held that the partial writing-off of a loan made by the taxpayer to a company of which he was the sole shareholder, created an allowable loss under section 253(3), Taxation of Chargeable Gains Act 1992 (TCGA). more›

### *Newton* – Tribunal confirms that "statutory records" should be narrowly construed

In *Newton v HMRC*, the FTT has held that the phrase "statutory records", for the purpose of an information notice issued pursuant to Schedule 36, Finance Act 2008 (FA 2008), must be construed narrowly. more›

### *Armstrong* – Tribunal cancels late filing penalties

In *Armstrong v HMRC*, the FTT cancelled late filing penalties because the taxpayer had not consented to receive penalty notices electronically. more›


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### About this update

Our Tax update is published on the first Thursday of every month, and is written by members of RPC's Tax team.

We also publish a VAT update on the final Thursday of every month, and a weekly blog, RPC's Tax Take.

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# News items

## Treasury considering capital gains tax relief for private landlords selling to long-term tenants

The Treasury is reported to be considering a proposal drawn up by the think-tank, Onward, to offer capital gains tax relief to private landlords who sell properties to their long-term tenants.

Under the proposals:

- existing buy-to-let properties would be eligible for 100% capital gains tax relief if the property is sold to a sitting tenant who has lived there for 3 years or more, and
- the gain from this tax relief would be split evenly between the landlord and the tenant, giving the landlord a windfall when they sell and the tenant a cash sum towards their mortgage deposit.

This policy could be paid for by restricting other tax reliefs for buy-to-let investors, such as reducing the private residence relief period from 18 months to 6 months.

The think-tank estimates that 88,000 households would take up the relief each year, with an average gain per property of £15,000.

A copy of the research paper can be viewed here.

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## Higher penalties for offshore matters

HMRC has published a factsheet on new higher penalties that it may charge in relation to offshore matters or offshore transfers that involve individuals and unincorporated businesses.

These higher penalties may apply when there is either:

- an inaccuracy
- a failure to notify, or
- deliberate withholding of information

that involves income tax, capital gains tax or inheritance tax.

From 1 October 2018, new penalties have been introduced for issues involving offshore matters or offshore transfers for all tax years up to and including 2015 to 2016. These penalties were introduced under the Requirement to Correct (RTC) legislation.

Taxpayers will be liable to a minimum penalty of 100% of the tax they owe in relation to any offshore issues for the tax years 2015 to 2016 and earlier, unless they have satisfied one of the limited criteria for supplying information after 30 September 2018.

A copy of the factsheet can be viewed here.

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## TIWB's compliance initiative leads to an increase in tax revenues

Tax Inspectors Without Borders (TIWB) claims in its annual report that it is helping to increase domestic revenues by improving tax auditing and compliance in Europe, Africa, Latin America, the Caribbean and Asia. TIWB estimates that an additional US$414m has been raised as a result of its initiative.

TIWB is run jointly by the Organisation for Economic Cooperation and Development and the United Nations Development Programme. Its programmes deal mainly with different issues of transfer pricing and international taxation. Ten programmes have been completed so far and a further 34 are under way.

A copy of the TIWB's annual report can be viewed here.

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# Case reports

## *Atherley* – qualifying loan write off created an allowable loss

In *Douglas Atherley v HMRC*[1], the First-tier Tribunal (FTT) has held that the partial writing-off of a loan made by the taxpayer to a company of which he was the sole shareholder, created an allowable loss under section 253(3), Taxation of Chargeable Gains Act 1992 (TCGA).

**Background**

Douglas Atherley (the taxpayer) was a stock broker who had an interest in interior design. He decided to become a professional interior designer and in 2002 established Kinari Ltd (Kinari), through which he conducted his interior design business.

The taxpayer became established in the residential market but decided to move into the more lucrative commercial property market.

Kinari was funded through a loan account. After several years of loss making, the company owed the taxpayer £616,959. In January 2013, the taxpayer decided to write off £350,000 of the loan. The business was then to be wound down in such a way that all creditors would be paid.

Kinari ceased trading in 2016.

The taxpayer attempted to claim loss relief for the loan write-off under section 253(3), TCGA. This section stipulates that if a qualifying loan has been made, as defined in section 253(1) (it was accepted that there had been a qualifying loan) and any amount of that loan has become irrecoverable, it can be claimed as an allowable loss.

HMRC did not accept that the loan was irrecoverable and relied upon section 253(12), which provides:

"(12) References in this section to an amount having become irrecoverable do not include references to cases where the amount has become irrecoverable in consequence of the terms of the loan, of any arrangements of which the loan forms part, or of any act or omission by the lender …".

HMRC's position was that the loan was not "irrecoverable" at the time it was written-off as Kinari continued to trade and the taxpayer lent a further £65,000 to the company. In HMRC's view, this suggested that the taxpayer did not believe that the loan was truly irrecoverable. In support of this assertion, HMRC pointed to the fact that the loan write-off was only partial and claimed that Kinari could have obtained a bank loan to satisfy the debt. As the write-off was an "act" by the lender the amount written-off was not irrecoverable and HMRC rejected the taxpayer's claim.

The taxpayer appealed.

**FTT decision**

The appeal was allowed.

In the FTT's view, there was sufficient evidence that the £350,000 was irrecoverable in January 2013. The fact that the write-off was "partial" did not create a difficulty for the taxpayer as partial write-offs of loans are common in other areas of commercial life.

1. [2018] UKFTT 0408 (TC).

The fact that there was a remote possibility that the loan might be repaid was therefore irrelevant. Given its loss making record, the FTT rejected as "fanciful" the suggestion by HMRC that a bank loan could have been obtained by Kinari and used to repay the loan.

**Comment**

Interestingly, the FTT pointed to the subsequent demise of the company as evidence to support its assessment that the loan had become irrecoverable. Although not relevant in this case, if Kinari had been more successful in subsequent periods the implication is that HMRC's position would have been stronger.

Although cases of this type will turn on their own particular facts, the FTT did suggest that, for the purposes of section 253(12), an "act" must be the sort of act which would prevent the company repaying the loan. There was no such arrangement or act in the present case. A decision to cease to carry on an unprofitable business was not an act, for the purposes of section 253(12).

A copy of the decision can be viewed here.

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## *Newton* – Tribunal confirms that "statutory records" should be narrowly construed

In *Newton v HMRC*[2], the FTT has held that the phrase "statutory records", for the purpose of an information notice issued pursuant to Schedule 36, Finance Act 2008 (FA 2008), must be construed narrowly.

**Background**

HMRC issued to Mr Maurice Newton (the taxpayer) a taxpayer notice under paragraph 1, Schedule 36, FA 2008 (the notice). The notice was issued in respect of tax years 2012/13, 2013/14 and 2014/15 and requested that the taxpayer provide the following:

(i) detailed lists of shareholders
(ii) detailed lists of dividends
(iii) list of all bank accounts
(iv) bank statements
(v) breakdown of a directors loan account, and
(vi) documentary evidence of any capital introduced.

The taxpayer appealed the notice to HMRC on the basis that the documentation requested was not reasonably required to check his tax position. HMRC contended that it had evidence that income received by the taxpayer had been omitted from his tax returns. No evidence of this claim was produced by HMRC.

The taxpayer requested that HMRC review the matter pursuant to section 49A, Taxes Management Act 1970 (TMA). Following the review, the notice was varied and items (iv) to (vi) were removed, as those requests were considered to be too vague and in any event were not reasonably required. Items (i) and (ii) were considered to be statutory records and item (iii) was considered to be reasonably required.

The taxpayer appealed on the basis the documentation was not reasonably required by HMRC for the purposes of checking his tax position and paragraph 21, Schedule 36, FA 2008, prohibited the issue of the notice. He also argued that none of the material constituted "statutory records".

2. [2018] UKFTT 513 (TC).

**FTT decision**

The appeal was allowed.

The FTT considered the following three questions:

(i) was the notice invalid because Condition B in paragraph 21(6), Schedule 36, FA 2008 (reason to suspect that an amount that ought to have been assessed to tax may not have been assessed), was not satisfied
(ii) was any of the information required by the notice "statutory records" (if it was, the FTT would not have jurisdiction to hear an appeal against that requirement – paragraph 29(2), Schedule 36, FA 2008), and
(iii) if the information was not a "statutory record", was it reasonably required to check the taxpayer's tax position?

*Reason to suspect*

In his submissions, the taxpayer highlighted that when issuing a third party notice under paragraph 2, Schedule 36, FA 2008, HMRC is required to seek the permission of the FTT. When issuing a taxpayer notice under paragraph 1, Schedule 36, FA 2008, HMRC has the option of seeking permission from the FTT and if it does and permission is granted the recipient of any such notice subsequently issued has no right of appeal.

Where HMRC does not seek the permission of the FTT to issue a taxpayer notice, as in the present case, although there is a right of appeal to the FTT there will have been no oversight by the FTT in the giving of the notice. In such circumstances, HMRC bears the burden of proof and must therefore demonstrate that the notice was justified (*Cliftonville Consultancy Ltd v HMRC*[3]).

As HMRC had failed to provide any evidence which the FTT could rely on to justify the notice, the FTT held that Condition B was not met and quashed the notice.

*Statutory records*

Although, given the conclusion reached by the FTT in relation to Condition B, it was not necessary for the FTT to determine what constitutes a "statutory record", it did nevertheless consider whether HMRC was correct in its assertion that the information requested constituted statutory records, against which there was no right of appeal (paragraph 39, Schedule 36, FA 2008).

The FTT considered that a restrictive approach needed to be taken to what amounted to a "statutory record". This was for two reasons. First, the recipient of a Schedule 36 notice is denied any right of appeal where the notice requires the production of statutory records. The recipient of such a notice is not able to contest HMRC's assertion that the document or information is reasonably required by HMRC to check the tax position of the taxpayer. Second, the provisions of the Taxes Acts which require the keeping and retention of records, contain substantial penalties for failure to keep such records.

The FTT noted that paragraph 62(3), Schedule 36, FA 2008, provides:

"Information and documents cease to form part of a person's statutory records when the period for which they are required to be preserved by the enactments mentioned in sub-paragraph (1) has expired."

3. [2018] UKFTT 231 (TC).

Section 12B, TMA, sets two time limits for the keeping of records in cases where, as in the present case, there was no enquiry into a tax return when the notice was issued. Where the recipient of the notice carries on a trade, profession or business, the limit is the fifth anniversary of 31 January after the tax year concerned. Where there is no trade, profession or business carried on by the recipient in any tax year, the limit is the first anniversary of 31 January after the tax year concerned.

HMRC gave no evidence that the taxpayer carried on any trade, profession or business. The limit therefore in relation to tax year 2014/15, was 31 January 2017 and 31 January 2015 and 31 January 2016 for tax years 2012/13 and 2013/14, respectively. As the notice was issued on 20 July 2017, none of what HMRC had asked for constituted statutory records.

The FTT also expressed the view that as section 12B(4) allows records to be preserved by any means, or allows the preservation of the information in them by any means eg by copying or digitisation, in section 12B cases "information" is only a statutory record if it is information which is in, or taken from, a document. A list of items which does not exist and which has not been kept and preserved is not a statutory record.

*Reasonably required*
The FTT said that had it been necessary to decide the question, it would have held that item (ii) was reasonably required but items (i) and (iii) were not reasonably required.

**Comment**
The FTT has expressed the view that, due to the lack of appeal rights, the term "statutory records" must be construed narrowly and that given, under paragraph 62(3), Schedule 36, FA 2008, statutory records cease to be such on the expiry of any time limit for their preservation, to constitute such records, information must be contained in a written document.

A copy of the decision can be viewed here.

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## *Armstrong* – Tribunal cancels late filing penalties

In *Armstrong v HMRC*[4], the FTT cancelled late filing penalties because the taxpayer had not consented to receive penalty notices electronically.

**Background**
On 6 April 2016, Ms Hannah Armstrong (the taxpayer) was issued with a notice, pursuant to section 8, TMA, to deliver a tax return for the tax year 2015/16 (the notice). HMRC's records indicated that the notice was issued by electronic communication to a secure mailbox on the self-assessment online account of the taxpayer. The notice required the taxpayer to deliver her return by 31 October 2016 (if filed in paper form) or 31 January 2017 (if filed electronically).

The taxpayer had ceased to be self-employed in January 2016 and was of the view, wrongly, that she was not required to file a "nil" return. She did eventually file her return late on 13 December 2017.

When the taxpayer failed to file on time, HMRC issued a penalty notice electronically to the taxpayer on 7 February 2017 for £100, pursuant to paragraph 3, Schedule 55, Finance Act 2009 (FA 2009). Further penalties were issued by HMRC electronically after three and six months (an additional £1,200 in total).

4. [2018] UKFTT 0404 (TC).

The taxpayer appealed the last two penalty notices, outside the 30 day statutory time period, on 21 December 2017. HMRC refused to agree that the appeals could be made out of time under section 49, TMA, and informed the taxpayer that her only recourse would be to seek permission from the FTT to submit her appeals out of time.

The taxpayer appealed to the FTT.

**FTT decision**
The appeal was allowed.

The first issue for the FTT to determine was whether the appeal should be permitted out of time. Applying the test set out in *Denton and others v T H White Ltd & others*[5], the FTT was of the view that the delay was "serious", being three months later than the statutory 30 day time limit. The explanation given for the delay was that the taxpayer had been unaware of the penalty notice. The FTT found that explanation to be plausible and something which weighed against the seriousness of the delay. The FTT concluded that the balance of prejudice weighed in favour of the taxpayer and gave permission for the appeals to be made late.

As HMRC may not use electric communications with a taxpayer unless the taxpayer has consented (this is the effect of regulation 3(1) of the Income and Corporation Taxes (Electronic Communications) Regulations 2003 (SI 2003/282) (the Regulations)), the second issue to be determined by the FTT was whether the taxpayer had agreed to receive penalty notices electronically.

The burden in showing the extent of the taxpayer's consent rested with HMRC and any such consent had to be "informed consent". On the material before the FTT, HMRC was unable to demonstrate that the taxpayer had done anything more than consent to receiving notices to file tax returns electronically. Accordingly, the FTT was of the view that although the taxpayer had consented to use the electronic system for the delivery of notices to file a tax return, that consent did not extend to communications relating to penalties. The penalties were therefore cancelled.

**Comment**
In previous cases where taxpayers have argued that they did not receive a notice that HMRC claims to have issued, the provisions of section 115(2), TMA, and section 7, Interpretation Act 1978, have been raised by HMRC. But those provisions relate to postal service. In this case, it was not postal service, but electronic communication, which was relevant. As the FTT commented, that raises different issues entirely.

The FTT expects any consent from a taxpayer to be informed consent, in other words, taxpayers must understand what it is they are consenting to and how precisely they will be informed of important matters that affect their tax liability, or their liability to sanctions, such as interest and penalties. Without such informed consent, notices given to taxpayers electronically, whether to a secure mailbox or an email address, may not be validly made.

A copy of the decision can be viewed here.

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5. [2014] EWCA Civ 906.

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