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What is 'substantial extent' for non-trading activities?

Gains that qualify for business asset disposal relief (BADR) are taxed at a reduced rate of 10%, but relief for company shares is not available if the underlying company carries on substantial non-trading activities. HMRC has long applied a strict 20% test, but a recent Upper Tribunal case has forced HMRC to backpedal and further clarify the interpretation of 'substantial'.

In *Assem Allam vs. HMRC [2021] UKUT 0291*, the Upper Tribunal found that previous HMRC guidance using a simple 80/20 test of trading versus non-trading activity is not always going to produce the correct answer when deciding if the relief is available. HMRC guidance has not completely done away with the 20% test, but less emphasis is now placed on it.

In any dispute with HMRC, it is important to remember that a decision of the Upper Tribunal makes the law, but HMRC guidance does not have the force of law.

Upper Tribunal approach

The Upper Tribunal concluded that the legislation does not provide for a strict numeric test. The test of whether non-trading activities are substantial is a holistic one not confined to physical human activity, but requires an overall consideration of what it is that the company does.

Other factors than those listed in HMRC's guidance can also be relevant.

HMRC guidance

HMRC's revised guidance now states that the 20% test is only likely to be relevant when considering the level of non-trading income and the value of a company's non-trading assets. If neither exceed 20%, HMRC will generally accept that the relief is available without further enquiry.

- Also relevant is the proportion of expenses spent on non-trading activities, as well as the amount of time and resources incurred.
- The relevant factors should be considered over a company's history, not just at one point in time; particularly if trade is seasonal.

Having investment property may therefore preclude claiming BADR. However, there is a bit more leeway when it comes to a large cash balance because it may be argued out of the equation as being required for trading purposes.

HMRC's guidance on the meaning of 'substantial' can be found here within their capital gains manual.

Taxpayer Protection Taskforce to tackle Covid-19 fraud

A recent report by the public accounts committee estimates that the level of fraud and error across all Covid-19 support schemes could be as high as £20 billion. However, don't assume mistakes and errors will not be picked up – HMRC is running the Taxpayer Protection Taskforce (Taskforce) to scrutinise claims made.

The two main areas of concern are the furlough scheme with an expected loss through fraud of £5.3 billion, and the bounce back loan scheme with some £18 billion expected to be written off.

Scrutiny

The Taskforce was set up a year ago and will likely be in place until March 2023. The Covid-19 support schemes to be scrutinised by the Taskforce include:

- The furlough scheme;
- Self-employment income support schemes;
- Eat out to help out; and
- Bounce back and business Interruption loans.

Some of the enquiries made by the Taskforce will be completely random, but many will be in response to information received by HMRC. The Taskforce anticipates making some 30,000 enquiries in total.

For example, from December 2020, details of furlough claims made by employers were published online. Employees could therefore report suspicions of fraudulent claims, and HMRC intends to look at every report made.

One example of compliance action highlighted by HMRC was a business that had claimed to have furloughed all of their workforce for two months. However, an analysis of card sales data showed no drop-off in trade for these two months.

Errors and mistakes

HMRC is fully aware that errors and mistakes may have been made given the pressure that business owners were under during the pandemic. Fully furloughed staff may have ended up doing some work, or the conditions for a self-employment income support scheme grant weren't met.

Individuals and companies can use HMRC's online disclosure service to rectify any errors or mistakes made. Voluntary disclosure is preferable to HMRC finding out for themselves.

The starting point for HMRC's disclosure service can be found here.

Protecting the normal minimum pension age

The normal minimum pension age (NMPA) will increase from 55 to 57 on 6 April 2028, although a protected pension age regime will be introduced. This will allow those who meet the rules to take benefits based on their existing normal minimum pension age.

Protected pension age

Protection will apply to members of registered pension schemes who before 4 November 2021 had the right to take their pension entitlement earlier than 57.

- There will be no need to apply to HMRC for protected pension age.
- The regime will apply to all types of UK-registered pension scheme.
- A person with protected pension age will be able to take benefits in stages without losing protection.
- Moving jobs, a change of pension scheme, making a transfer to a new scheme or taking benefits could all have an impact on the NMPA that will apply.

The age was previously increased from 50 to 55 in 2010, and anyone who has protected pension age from that transition will see no change when the threshold increases to 57.

No protected pension age

The impact of the higher NMPA will depend on when a person was born:

Born before 7 April 1971	Will be 57 by 6 April 2028, so not affected by the change.
Born between 7 April 1971 and 5 April 1973	Will be 55 by 5 April 2028, so not affected if pension benefits fully taken by then. However, if a person still has benefits to take at 6 April 2028, they will have to wait until 57 before the remaining benefits can be taken.
Born on or after 6 April 1973	Will not be 55 by 5 April 2028, so will have an NMPA of 57.

The new protected pension age regime is wide-ranging and complex, providing both opportunities and risks. Professional advice is therefore essential.

HMRC's policy paper on increasing normal minimum pension age can be found here.

Taxpayer victory leads to room hire VAT exemption

A recent First-Tier Tribunal (FTT) decision in the taxpayer's favour has helped clarify that room rental is VAT exempt, but standard rating can apply if additional services are also supplied, such as a hairdresser renting chair spaces.

The FTT case involved hair and beauty business, Errol Willy Salons, hiring out two spare rooms to self-employed beauticians. Exempt VAT treatment suited the beauticians who were not VAT-registered.

HMRC argument

HMRC contended that a standard rated package of services was being provided rather than just the two rooms. Along with the use of rooms, the self-employed beauticians had access to the staff toilets and rest area, occasional use of the services of a receptionist, and were provided with light and heat. They also benefited from advertising.

HMRC argued the facts were similar to the *Byrom* case – which had gone in their favour – where rooms hired to self-employed masseuses came with a bundle of other services including access to a kitchen, showers, a washing machine, linen and towels, security and a reception.

A victory for HMRC could have impacted on any business letting out a spare room. However, although HMRC's ambition to narrow the VAT room rental exemption has been checked, they may now resort to legislative change.

The decision

The FTT disagreed that the *Byrom* case was comparable because the beauticians in the *Errol Willy Salons* case were only provided with what were essentially bare rooms. The masseuses in the *Byrom* case, in contrast, had the use of a package of services, one of which was the provision of a room.

- Although the additional services provided to the beauticians made it easier for them to provide their services, crucially none of the services were considered to be essential.
- The additional services were therefore incidental to the supply of the room.
- The predominant supply made by the taxpayer was room rental, and this was correctly treated as VAT exempt.

More detail on the *Byrom* case, along with a number of examples showing HMRC's view on the VAT treatment of supplies containing a number of elements (including the right to occupy property), can be found here.

Whatever happened to the wealth tax?

A new wealth tax to counter the cost of the Covid-19 pandemic was the talk of the financial pages not so long ago. Now it has disappeared… or has it?

By the end of 2020, as the huge cost of the Covid-19 pandemic became clear, there was much discussion about the introduction of a wealth tax. It was given added impetus by the publication of a 126-page report from the Wealth Tax Commission, an independent think tank launched in 2020.

Although the Commission did not recommend a specific level of tax, it focused heavily on a one-off tax that:

- Applied on an individual basis;
- Was at a flat rate of 5% on wealth above £500,000;
- Would normally be payable as five annual instalments of 1% (plus interest); and, crucially;
- Would cover *all* wealth including the value of your home and your pension.

The Commission thought that this format would lead to about 8.25 million people paying the new tax, raising a net £260 billion for the Exchequer – at the time broadly in line with the estimated cost of the pandemic.

A wealth tax generally polls well with the public, but that is often thought to be because those in favour think it will not affect them. As soon as the home, savings and/or pension are included in the definition of wealth, enthusiasm starts to fade. The 8.25 million people within the Commission's proposals is close to double the current number of higher and additional rate taxpayers. To make matters worse, the National Audit Office's latest estimate (to July 2021) for the total cost of the pandemic is £370 billion.

The Chancellor has said he is against a wealth tax. However, his two 2021 Budgets will eventually raise tax revenue by nearly £50 billion *a year*, so in the long term the Treasury will be collecting more than the Commission's one-off proposal would have delivered. Other than on the fringes, the Labour Party has not backed the Commission's proposals. Instead, it has spoken about increasing taxes *on* wealth – for example, by bringing capital gains tax rates in line with income tax.

The spectre of a wealth tax seems to have evaporated for now, but tax increases (by stealth or otherwise) – and the consequent need for tax planning – have not.

More detail on the wealth tax can be found here.

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