



UK Tax Law Update

August 2007
Issue 1

Welcome to the first issue of the UK Tax Law Update produced by the London Office of Steptoe & Johnson. We will be distributing this bulletin every 2-3 months. This Update is written with a broad spectrum of our clients in mind, therefore if you would like to discuss any particular issue in more detail please contact Kassim Meghjee (kmeghjee@steptoe.com) or your usual Steptoe & Johnson contact. We hope you enjoy reading this and welcome any feedback that you may have.

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International/European Tax Developments

1. EC law freedoms and Non-Member States

Winfried L. Holböck v. Finanzamt Salzburg-Land (ECJ Case No. C-157/05)

This case dealt with EC law freedom of movement of capital and freedom of establishment and interactions with Non-Member States like Switzerland. The Austrian claimant held shares in a Swiss company that wholly owned an Austrian company. The European Court of Justice (“the ECJ”) held that Austrian rules permitting the taxing of dividends at a higher rate when received from a Swiss company than from an Austrian company (in both cases, when made to an Austrian tax resident individual) is compatible with EC law. The Court held that freedom of establishment within the EC law did not extend to situations involving establishment in third countries even where a resident of the EC had control over the subsidiary within the EC. As far as the movement of capital was concerned, the Court held that, although there was a restriction on the movement of capital, the exception in Article 57(1) of the EC Treaty applied (restrictions that were in existence at 31 December 1993) and therefore the rules were consistent with EC law. This is an important judgement in that, if such restrictions did not exist at the relevant date, the freedom of movement of capital would apply even where Non-Member State companies are interposed.

2. EC law freedoms and deductibility of taxable intra-group financial transfers

Oy AA (ECJ Case No. C-231/05)

This case dealt with the freedom of establishment within the EC and deductibility of intra-group financial transfers. The claimant was a Finnish subsidiary whose parent was tax resident in the UK. The UK parent made a loss in a year in which the Finnish subsidiary made a profit and it was envisaged that the Finnish subsidiary would make a taxable intra-group financial transfer. This is permissible under Finnish legislation, and the transferring company is permitted a deduction upon satisfying certain conditions, including the condition that the recipient is also established in Finland. All required conditions, except for the same state establishment, were satisfied. The ECJ held that although the requirement of same state establishment was, prima facie, in breach of the freedom of establishment, it was justified on overriding public interest grounds, in particular, the balancing of the allocation of power to tax between member states and the prevention of avoidance of tax.

3. EC non-discrimination law and losses incurred by Community nationals

Luxembourg v Lakebrink (ECJ Case No. C-182/06)

This case dealt with EC non-discrimination laws and losses incurred by Community nationals in other Member States. The taxpayers, who for tax purposes were resident in Germany, were employed and earned their income exclusively in Luxembourg. In determining the tax rate applicable for payment of tax in Luxembourg they declared rental income losses from their properties in Germany. The tax authorities refused to accept those losses in determining the tax rate for non-residents. The taxpayers’ appeal was stayed and the national Court referred the matter to the ECJ. The ECJ held that, although the situations of residents and non-residents were as a rule not comparable, where a resident of one Member State



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earned the majority of his income in the other Member State, rental income losses could be considered and that national laws prohibiting that were discriminatory.

4. UK's Investment Manager Exemption

Revised Statement of Practice 1/01

HM Revenue & Customs (the "Revenue") published revised Statement of Practice 1/01 setting out the terms on which non-resident funds can appoint UK-based investment managers without the risk of the funds being regarded as tax resident in the UK. The publication follows a period of consultation with the investment management industry. The general effective date of the revised Statement of Practice is 20 July 2007. However, the effective date is delayed where changes to the current circumstances or contractual arrangements are required; in which case the original text can be relied upon until 31 December 2009.

5. Insurance intermediaries established outside the EC

Commission's formal request to the UK to amend its rules relating to recoverability of VAT

The European Commission made a formal request to the UK to amend its rules, which restricted the rights of insurance intermediaries that are established outside the UK to reclaim UK VAT. The UK legislation was amended in December 2004 by adding to the list of those which are irrecoverable, a new category of UK VAT incurred by such intermediaries. Insurance brokers and agents who are established outside the EC and who provide services to customers also based outside the EC were, as a result, denied the right to recover any UK VAT incurred by them. This change however did not apply to insurance agents or brokers established within the Community. The Commission is of the view that this rule is inconsistent with the EC's Thirteenth Directive (86/560/EEC). EC Law requires the UK to amend its legislation within two months of the formal request (which was made on 3 July 2007). If the UK fails to make the necessary amendment, the European Commission may refer the matter to the ECJ. Those who have been denied the recovery of such VAT in the last 3 years may lodge a claim with the Revenue on the basis that throughout that period relevant UK laws were, and still remain, inconsistent with EC law.

6. EC VAT and the meaning of "special investment funds"

JP Morgan, Flemming Claverhouse Investment Trust Plc (ECJ Case No. C-363/05)

The ECJ held that, for VAT purposes, "special investment funds" may include closed-ended investment funds and that Member States have discretion in determining which types of funds are covered by the notion of "special investment funds". The Court also held that Member States must ensure fiscal neutrality among "special investment funds" which are in competition with each other. The Court confirmed that the relevant VAT Directive has direct effect and can be relied on before a national court in order to challenge any national legislation which is alleged to be incompatible with it. The practical impact of this decision is that management services for investment funds will, in virtually all cases, now be exempt and thus, no VAT will be chargeable by the manager providing such services.



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7. EC VAT and the refund of VAT under the Eighth and the Thirteenth VAT Directives

Planzer Luxembourg SARL (ECJ Case No. C-73/06)

The ECJ held that the certificate issued as prescribed by the Eighth Directive does, in principle, allow the presumption that the person making the claim for refund in one Member State is established in another Member State and is subject to tax there. However, nothing prohibits the tax authority of the Member State in which the claim for refund is made from verifying the certificate if it has doubts as to the existence of the establishment in the other Member State. The decision also encompassed claims for refund from a claimant who is not based in the community which are made under the Thirteenth VAT Directive. The Court held that, whether the claimant is established outside the community is determined by ascertaining where the essential decisions concerning its general management are taken and where the functions of its central administration are exercised.

8. EC law and indirect taxation on the raising of capital

Albert Reiss Beteiligungsgesellschaft mbH (ECJ Case No. C-466/03)

The ECJ has held that the Member may not charge notarial fees for the authentication of a transfer of shares in a company made as an increase in the share capital of another company in a system where the notaries are employed as civil servants and the fees subsidise public expenditure. Such fees are an indirect tax on the raising of capital in breach of EC Council Directive 69/335/EEC (as amended).

9. EC VAT and the allocation of 3G mobile telecommunication licences

T-Mobile Austria GmbH (ECJ Case No. C-284/04) and Hutchinson 3G UK Limited (ECJ Case No. C-369/04)

The ECJ held that allocation by the state of licences did not constitute an economic activity for VAT purposes. Thus, the amounts paid by telecommunication operators for those licences could not be regarded as inclusive of VAT which could then be recovered from the relevant tax authority.

10. EC law and tax on raising capital

Optimus Telecomunicações SA (ECJ Case No. C-366/05)

This case dealt with tax payable on raising capital by a company. The company was an undertaking with its principal place of business in Portugal. It increased its share capital through a cash payment. When that increase in capital was recorded, the taxpayer was required to pay stamp duty of 0.4% in accordance with national laws enacted in December 2001. The taxpayer challenged that liability to stamp duty before the national courts, arguing that the tax infringed art 7(1) of Council Directive 69/335/EEC (prohibition concerning certain indirect taxes on the raising of capital). The Portuguese courts stayed the proceedings and referred the case to the ECJ which held, inter alia, that as the Portuguese Act of Accession did not prevent the application of the relevant article (as it was not expressly excluded by it), neither was such tax nor its introduction permissible under EC law.



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11. Joint International Tax Shelter Information Centre (“JITSIC”) expansion

The Commissioners of the Australian, Canadian, United Kingdom and United States tax administrations have decided to open a second office of JITSIC in London in the Autumn of 2007. Additionally, Japan has accepted an invitation to join JITSIC, and a representative of its National Tax Agency will be present at the London centre.

12. Double Taxation Conventions, Protocols and Forms

- **UK – Switzerland: Protocol to the Double Taxation Convention**

A Protocol amending the Double Taxation Convention between England and Switzerland has been signed in London. It will enter into force once both states have completed their legislation procedures.

- **UK – the Faro Islands: Double Taxation Convention**

A Double Taxation Convention between the United Kingdom and the Faro Islands has been signed in London. It will enter into force once both parties have completed their legislative procedures.

- **UK – Japan: New forms to be used for claims under the Double Taxation Convention**

The Revenue has issued forms which are to be used for any claims for relief from UK source income paid on or after 1 January 2007 under the UK-Japan Double Taxation Convention. This includes forms to be used for income from a UK Real Estate Investment Trust.

Corporate and Business Tax Developments

13. Quoted Eurobonds

The Professional Securities Market, Euro MTF and the Irish Alternative Securities Market

The Revenue has issued guidance on the application of the Quoted Eurobond Exemption, which allows for interest to be paid without withholding when certain conditions are met. The Quoted Eurobond Exemption applies where the securities (i) are issued by a company; (ii) are “listed on a recognised stock exchange”; and (iii) carry a right to interest. The guidance issued by the Revenue states that as far as the condition (ii) is concerned, securities that are officially listed on the Professional Securities Market in London, the Euro MTF in Luxembourg and the Alternative Securities Market in Ireland, will be regarded as “listed on the recognised stock exchange” and therefore interest payable on securities listed on the exchanges can be paid without withholding.

14. Restitution claims and compound interest

Sempra Metals Ltd (formerly Metallgesellschaft Ltd) v Inland Revenue Commissioners [2007] All ER (D) 294

The House of Lords has given its decision in a test claim under a group litigation order to manage numerous claims as a result of the ECJ's decision which held that the UK's advance corporation tax regime, as it was in force in 1999, was inconsistent with EC law. It held that the UK Courts had jurisdiction at



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common law to award compound interest where the claimant sought a restitutionary remedy for the time value of the money paid to the Revenue. A remedy of restitution differs from that of damages in that it is the gain to the Revenue that is measured rather than the loss to the claimant.

15. Sharia Compliant Bonds – Recognised Stock Exchanges

The Revenue has designated the following stock exchanges as ‘recognised stock exchanges’ for the purposes of section 48A Finance Act 2005 (Sharia Compliant Investment Bonds):

- Abu Dhabi Securities Market
- Bahrain Stock Exchange
- Dubai Financial Market
- Dubai International Financial Exchange
- Labuan International Financial Exchange
- Saudi Stock Exchange (Tadawul)
- Surabaya Stock Exchange

16. PLUS-listed market designated as a ‘recognised stock exchange’

With effect from 19 July 2007, the Revenue has designated the PLUS-listed market as a ‘recognised stock exchange’ under section 1005 Income Tax Act 2007. PLUS Markets PLC gained recognised investment exchange status on 19 July 2007 and this enabled it to apply for recognised stock exchange status for its PLUS-listed market segment. It is only the PLUS-listed market segment of PLUS that is now a recognised stock exchange. This market will be able to admit to trading shares and securities that are included in the official UK list as maintained by the Financial Services Authority in its role as the UK Listing Authority. The PLUS-quoted and PLUS traded markets will continue to provide trading services in shares which, for tax purposes, are unlisted. These two markets have not been designated as recognised stock exchanges and the current tax treatment of their constituent companies remains unchanged.

17. The right to use Leisure Facilities

The Highland Council ((2007) ScotCS CSIH 36)

The Scottish Court of Session held that unlimited access to all leisure facilities in a leisure centre, typically for a monthly or an annual payment, is liable to VAT at the standard rate on the basis that it constitutes a single supply of the right to use the leisure facilities. It held that the fee cannot be apportioned between different facilities even though some facilities, such as swimming tuition are exempt while use of the sauna is standard-rated.

18. Purchase and re-sale of gilts

DCC Holdings (UK) Limited v Revenue and Customs Commissioners ((2007) SpC 611)

This is a Special Commissioners case on purchase and resale of gilts. The taxpayer entered into a number of net paying repurchase transactions (“repo transactions”) in gilts with a bank. A representative



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transaction was a purchase of gilts from the bank for £812 million, which were to be returned to the bank 11 days later for £785 million – the taxpayer was entitled to receive interest of £28.8 million in the interim that it did not have to pay the bank. As a result of the transaction, the taxpayer made an economic and an accounting profit of £1.8 million. However, it made adjustments for corporation tax return purposes and showed a loss of £27 million (i.e. £812 million minus the £785 million). The Revenue rejected the loss claim and issued an adjustment. The taxpayer appealed to the Special Commissioners. The Special Commissioner held, after detailed analysis, that the profit made by the taxpayer for accounting purposes did not require any adjustment under either the loan relationship rules or the transaction in securities legislation and therefore the economic and accounting profit of £1.8 million had to be brought into account for tax purposes.

19. Employee Share Schemes – Returns can now be filed online

The Revenue has announced that companies can now file employee share scheme returns online – this applies to Share Incentive Plans, Save As You Earn, Company Share Option Plans, as well as other non-tax advantaged shares and securities.

20. Assignment of a claim for repayment of VAT

Midland Co-Operative Society v Revenue and Customs ([2007] EWHC 1437)

The High Court held that a right to a repayment of VAT under Section 80 of the Value Added Tax Act 1994 is assignable and an assignee will have standing to make a repayment claim from the Revenue.

21. Reverse charge for the supply of mobile phones and computer chips

Reverse charge rules apply with effect from 1 June 2007 for the sale of mobile phones and computer chips. Traders who buy those goods have to account the VAT in respect of them directly to the Revenue. This applies to, in summary, transactions involving mobile phones and computer chips where the ex-VAT invoice value is £5,000 or over. There are changes to the invoice requirements, which must now state that it is the obligation of the trader who buys the goods to pay the VAT to the Revenue and the seller has to produce a Reverse Charge Sales List.

22. Theatres: VAT and Partial Exemption

The Revenue has revised its policy on input tax recovery on costs of staging shows (production costs) for which theatre admissions are VAT exempt. It follows the Court of Appeal decision in the case of Mayflower Theatre Trust Ltd [2006] which went against the Revenue. The Revenue has decided not to appeal the decision. Theatres which receive single supply of production services from touring companies that include material essential for the production of programmes, e.g. logos, photographs and costing information, may treat the VAT as residual, which is recoverable in accordance with its partial exemption method. This is the case even if programme material forms a minor part of the contract. All claims for recoverability of VAT in such circumstances which were either denied or not made, can now be made subject to the normal three-year limit.



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23. Reduced rate of VAT

The supply and installation of mobility aids for the elderly and smoking cessation products

Beginning 1 July 2007, the supply and installation of certain mobility aids will be eligible for the reduced rate of VAT (5%) when installed in domestic accommodation occupied by a person aged 60 or over. For a period of one year only the supply of smoking cessation products will be eligible for the reduced rate of VAT as well.

Real Estate Tax Developments

24. Compliance and the New Construction Industry Scheme

The new Construction Industry Scheme rules which came into effect on 6 April 2007 have provisions requiring continuous reviews by the Revenue. The Revenue is likely to carry out reviews annually, at which time they will review the sub-contractor's compliance over the previous 12-month period. The Revenue has also published a fact sheet (CIS 343) which lists minor breaches which it will, in certain circumstances, regard as acceptable. Though it needs to be seen how it bears out in practice, the annual review process could mean that a sub-contractor may be faced with net payments (and hence cash-flow problems) some time after actual multiple minor breaches of the compliance obligations.

25. Land belonging to Schools and relief from SDLT

The Treasury issued an Order (SI 2007/1385) effective 25 May 2007 that exempts land transactions from the charge to stamp duty land tax where the transfers are of land to a local education authority within prescribed sections of the School Standards and Framework Act 1998 or in connection with removal of or reduction in foundation governors within prescribed sections of the Education and Inspections Act 2006 if either the purchaser or the vendor is a public body.

26. Industrial buildings allowances and storage facilities

Revenue and Customs Commissioners v Maco Door and Window Hardware (UK) Ltd

A UK subsidiary of an Austrian company claimed industrial buildings allowance on a warehouse used to house goods such as door locks and door handles manufactured by the Austrian company. The Revenue rejected the company's claim on the basis that the company was not carrying on a qualifying trade within what is now section 271 of the Capital Allowances Act 2001. The company appealed, arguing that it was carrying on a trade of "storage", which qualified for allowances. The Special Commissioner accepted this argument, observing that the products were held for sale in circumstances where sale was not expected to be immediate. The warehouse was in use for the purposes of that part of the company's trade that consisted of the storage of goods or materials to be used in the manufacture of other goods or materials. The Court of Appeal (reversing the High Court's decision in the Revenue's favour) held that whether the company is carrying on a trade of "storage" is a question of fact and that the Special Commissioner had not erred in law. Although industrial building allowances are being phased out over the next four years, businesses which have a separate warehouse function may want to consider lodging protective claims for historic industrial building allowances claims, as well as making claims in the current and prospective accounting periods.



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27. UK REITs

Statutory Instruments issued

The Revenue has issued a number of draft regulations in relation to real estate investment trusts. These are:

- Real Estate Investment Trust (Joint Venture Groups) Regulations 2007 covering the requirements for joint venture groups;
- Real Estate Investment Trust (Breach of Condition) (Amendment) Regulation 2007, which will amend the Real Estate Investment Trusts (Breach of Conditions) Regulations SI 2006/2864; and
- Real Estate Investment Trusts (Financial Statements of Group Real Estate Investment Trusts) (Amendment) Regulations 2007, which will amend regulations SI 2006/2865

These are expected to have effect for accounting periods beginning on or after 1 January 2007.

28. Capital Gains Tax on the sale of Property

Underwood v Revenue and Customs ([2007] – SpC 614)

This case dealt with a claim for capital loss which could be used against capital gains made on disposal of other assets. The claimant had acquired a property for £1.4 million in 1990. He then entered into a contract to sell the property for £400,000 to another person in 1993 with an option to purchase it back for £400,000 + 10% of the increase of value in the property during the option period (which ended on 31 December 1995). In 1994 the claimant entered into a contract to sell the property to a connected company for £600,000. The same solicitor acted for all the parties to the various contracts and options. He concluded that as a legal transfer of the property had not occurred, and he would transfer the property directly to the connected company. The claimant argued that the beneficial interest in the property had passed when the contract was entered into in 1993 and that the capital loss should be available for him to offset against other capital gains. The Special Commissioner disagreed and held that there was never a disposal in 1993. Therefore, the claimant always held a beneficial interest in the property. The appeal was therefore dismissed. The transfer of the property to the connected company would, for capital gains tax purposes, be at the market value and therefore that transaction would not have generated a loss which could be offset against any other capital gains the claimant may have had.

29. Property and VAT

- Transfer of a going concern and sale and leaseback

Morton Hotels Limited (VAT Tribunal Decision – V20039)

One hotel group sold three hotels to another group. The buying group entered into a sale and leaseback arrangement for financial reasons immediately on the acquisition. The Revenue argued that the sale and leaseback transaction was an intervening transaction, so that the acquisition by the buying group did not constitute a transfer of a going concern and hence VAT was payable on the transfer of the three hotels. The VAT tribunal disagreed, holding that there was nothing in the legislation for an intervening



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transaction of this nature to prevent the transaction from being regarded as a transfer of a going concern – the asset was used by the transferee in the same way as the transferor prior to the transfer and, in reality, the business continued without any gap or interruption.

- Place of supply of legal services and services relating to land

Kenneth Richard Daunter (VAT Tribunal Decision – V20120)

This case dealt with the place of supply for VAT purposes. An individual who lived in Jersey, not within the European Community, helped a woman purchase a leasehold flat in Bristol under an agreement whereby she would occupy the flat for her lifetime. Thereafter, he would be entitled to possession and ownership of the flat. The woman died in 2003, and he took court proceedings against her personal representative to gain possession of the flat. The solicitors who acted for him charged VAT on their services. He lodged an appeal to the VAT tribunal, contending that the services should be treated as having been supplied in Jersey, where he lived and should therefore be zero rated. The tribunal rejected this contention and dismissed the appeal, holding that the supplies were of 'services relating to land', so that the place of supply was in the UK. The tribunal observed that although solicitors were not specifically referred to in para 5 of the VAT (Place of Supply of Services) Order 1992, their services were included in the Order as 'others involved in matters relating to land'.

- Non-pecuniary obligations and supply of land

Velvet & Steel (ECJ Case 455/05)

This case was referred from the German Courts and dealt with whether the assumption of the obligation to renovate a building was an exempt supply. In two contracts for the sale of land, the vendors undertook to carry out renovation work on the buildings concerned. Following the sales, the vendors concluded contracts with the applicant, assigning a fraction of the purchase price in return for the assumption of, inter alia, the obligations to renovate. The purchasers of the buildings subsequently agreed to release the applicant from its obligations in return for the payment to them of part of the purchase price. The profit resulting from that transaction remained with the applicant. The domestic tax authorities deemed the assumption by the applicant of the obligations to renovate to be a transaction subject to VAT. The applicant challenged that decision, relying on Art 13B(d)(2) of the Sixth Directive (77/388/EEC), now embodied in Art 135 (1)(c) of the new VAT Directive. Arguing that the provision granted an exemption not only for the assumption of pecuniary obligations but also for the assumption of non-pecuniary obligations, the German Court referred the question to the ECJ for preliminary ruling. The ECJ ruled that Art 13B(d)(2) permitted the assumption of non-pecuniary obligations to be subject to VAT.

- Licence of sports pitches

Polo Farm Sports Club (VAT Tribunal Decision – V20105)

A sports club granted a hockey association a licence to use some artificial hockey pitches between 8.00am and 9.30pm each day. It reclaimed input tax relating to the supply. The Commissioners issued a ruling that the supply was exempt. The club appealed, arguing that such a supply was a taxable supply which fell within Item 1(m) of Group 1 of Schedule 9 of the Value Added Tax Act 1994. The tribunal



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accepted this argument and allowed the appeal, observing that the exclusion set out in Note 16 to Group 1 of Schedule 9 did not apply as the grant was not for ‘a continuous period of use exceeding 24 hours’ (and therefore not within Note 16(a)) and the interval between each period was ten and a half hours (i.e. ‘less than one day’ and therefore not within Note 16(b)).

- Forfeiture of deposit not subject to VAT

Société thermale d'Eugénie-les-Bains (ECJ Case C-277/05)

This case was referred to the ECJ from the French Courts and relates to the supply of hotel services. It dealt with whether a sum paid as a deposit is also subject to VAT where the client exercises the cancellation option available to him. The ECJ held that the sum retained by the hotelier as a fixed cancellation charge has no direct connection with the supply of any service for consideration and, as a compensation payment, it is not subject to VAT. This case has wider implications in the context of real estate transactions where deposits are forfeited if a transaction does not proceed to completion. Subject to contractual terms, if the deposit is deemed to include a proportional sum of VAT, that proportion may be recoverable from the seller even if the proportion representing the deposit is not.

Personal Tax Developments

30. Allowable deductions from income tax – examination fee

Revenue and Customs Commissioners v Decadt ([2007] All ER (D) 139)

Under the terms of the taxpayer’s contract of employment, the taxpayer was required to attend specific training courses for the purposes of obtaining a professional certificate. The taxpayer sought to deduct examination fees and associated accommodation and travelling expenses from his earnings pursuant to section 336(1) of the Income Tax (Earnings and Pensions) Act 2003. The General Commissioners had allowed the taxpayer’s appeal on grounds that the training was an obligation under the contract of employment. The High Court, however, held that it was not the employment contract which was key, but whether or not the expenses were incurred “necessarily” in the performance of the duties of that employment, which was not the case and therefore the Revenue’s appeal was allowed.

31. Capital gains tax and Qualifying Corporate Bonds

Harding v Revenue and Customs Commissioners ([2007] SpC 608)

This case involved the exchange of shares for loan notes which incorporated a right to redeem the loan notes in currency other than sterling. The appellant received loan notes in exchange for shares. The appellant argued that although the loan notes were not qualifying corporate bonds at the point of exchange, they were qualifying corporate bonds at the point of redemption on the basis that the right to redeem in a currency other than sterling had lapsed at the time of redemption, so that no capital gains tax would have been payable at redemption. The Special Commissioner dismissed the appeal, holding, inter alia, that the lapsing of the right in the loan note was not a “transaction”, as a transaction was something that was done by two or more people and therefore the loan notes were not qualifying corporate bonds at all times.



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32. EC law and the freedom of movement of workers

Georgios Alevizos (ECJ Case C-392/05)

The ECJ held that an employee in the public service, the armed forces, the public security forces or the harbour police corps of a Member State who stayed for at least 185 days a year in another Member State with the members of his family in order to carry out an official task of a definite duration in that latter state, had, for the duration of that task, his normal residence in the other Member State for the purpose of the special supplementary single payment tax on vehicle registration levied on the permanent import into Greece of a private motor vehicle from Italy. Although the case applies to special supplementary single payment tax on vehicle registration, the principle is applicable to all taxes payable on the importation of personal property into one Member State from another Member State in similar circumstances.

33. IR 35 and whether a contractor would be an employee if engaged directly by the client.

Islands Consultants Ltd v Revenue & Customs Commissioners ((2007) SpC 618)

The Special Commissioner held that the provision of services by a company of its controlling director, through an employment agency, on a series of three-month contracts for a five-year computer project satisfied the requirements of ‘hypothetical employment contract’ for the purposes of what is commonly known as IR35 (the relevant rules are now at para 6 of the Social Security Contributions (Intermediaries) Regulations 2000 as well as section 49 of the Income Tax (Earnings and Pensions) Act 2003). This meant that the company was under an obligation to account for the income tax and national insurance contributions on the payments due to it because such payments were deemed to be ‘employment income’.

34. Statutory Sick Pay

Revenue and Customs Commissioners v Thorn Baker Ltd ([2007] EWCA Civ 626)

The Court of Appeal held that statutory sick pay is not payable to agency workers whose contract with the agency is for a period of three months or less. The Revenue subsequently issued guidance stating that agency workers can nonetheless be entitled to such payments if, amongst other scenarios, the following apply. Two or more such contracts with the same agency are separated by eight weeks or less and (i) the total length of the contracts is more than 13 weeks; (ii) the total period actually worked is more than 13 weeks; or (iii) the contracts are extended so that together they run for more than 13 weeks.

35. Right to recover income tax and employee’s NIC

McCarthy v McCarthy & Stone Plc ([2007] EWCA Civ 664)

The Court of Appeal held that a company has a remedy in restitution to recover income tax and employee’s national insurance contribution from a former employee where the company accounted the same to the Revenue. The case involved the exercise of rights under a share option scheme which did not contain the contractual right to recover income tax and employee’s national insurance contribution from the former employee. Though employees may find it difficult to resist recovery claims it is still important for share option scheme rules to provide a contractual right for the employer to recover income tax and employee’s



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national insurance contribution from all employees, whether still in employment or not.

36. Businesses run by husband and wife entitled to take income as dividends

Jones v. Garnett ([2007] UKHL 35)

The House of Lords held that the anti-avoidance legislation relating to settlements does not apply to arrangements allowing couples to take income as dividends rather than salary (the former being taxed at a lower rate than the latter). The Court held that under the legislation, the income from the company in which the couple held equal shares could not be chargeable to income tax and national insurance contribution as if it is employment income of one of them. This was because consent of the taxpayer to allow the transfer of the shares to his spouse was an outright gift meaning that the transaction fell within an exclusion from the operation of the relevant anti-avoidance provisions. The Government is considering amending the legislation in the light of this judgement.

37. Sharia Compliant Bonds and meaning of securities

Legislation has been laid before the House of Commons which extends the meaning of 'securities' to include Sharia Compliant Bonds. This means that such Bonds may now also be caught by the income tax charges imposed under Part 7 of the Income Tax (Earnings and Pensions) Act 2003. The relevant legislation is expected to come into effect on 14 August 2007.

If you would like further information please contact Kassim Meghjee (kmeghjee@steptoe.com) in London or your usual Steptoe & Johnson contact.

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