Double whammy

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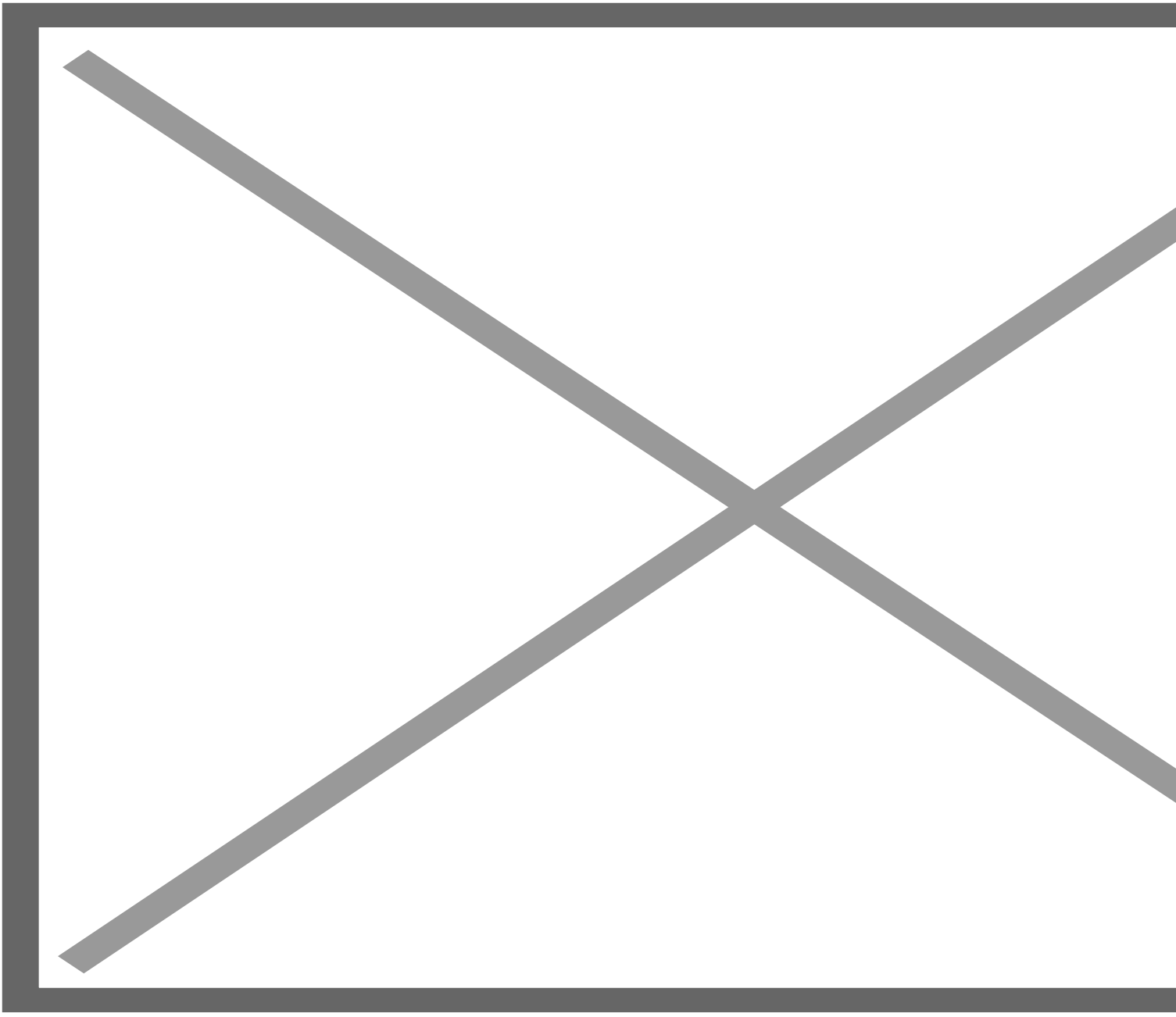

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Ian Walker and *Prathab Jagajeevanram* consider the practicalities arising from the judgment in the *Southern Aerial* case

Key Points

What is the issue?

HMRC issued determinations on a company charging Class 1A National Insurance contributions (NICs) and raised discovery assessments charging two individuals to income tax on the basis that cars were made available, and fuel was provided, to them by reason of their employment with that company. The individuals were in a partnership that provided services to the employer company. The First-tier Tax Tribunal considered the specific arrangements and whether the car and fuel benefits were properly charged ‘by reason of employment’

What does it mean to me?

The effectiveness of structures intended to mitigate car and fuel benefit charges ought to be reviewed

What can I take away?

The courts interpret ‘by reason of employment’ as being of wider application than ‘from an employment’. In addition, despite the strict application of the computational rules for calculating fuel benefits giving rise to a positive amount, this alone is not sufficient to enable a taxable benefit to be charged. The computational rules have effect only if the provision of fuel results in a real benefit being provided to the employee in economic terms

Southern Aerial (Communications) Ltd and the taxpayers, Mr and Mrs Jones, appealed against HMRC’s NIC determinations and assessments to income tax on car and fuel benefits purported to have arisen.

We do not consider the Social Security Contributions and Benefits Act 1992 since it is clear that s 10 of that Act seeks to impose Class 1A NICs where there is a charge to income tax on the taxpayers under the sections of ITEPA 2003 considered below.

Undisputed facts of the case

- The taxpayers are the exclusive owners and directors of the company, which was formed in 1981.
- In 2002, the taxpayers formed a partnership, the SAT Design Partnership (SAT).
- The company entered into distinct hire purchase (HP) agreements for two BMW convertible cars.
- The company had the power neither to sell nor otherwise part with the cars without the consent of the other parties to the HP agreements. Nor could it take ownership of the cars until all monthly instalments and the final one-off payments were settled.
- Although the company made the payments, they were not reflected as expenses in its accounts. Instead they were charged to its account with SAT, which claimed the interest expense and capital allowances for the cars.

Further findings of fact by the FTT

- Although Mr Jones insisted that SAT had been created to ‘hive off’ a part of the company’s business, the First-tier Tax Tribunal (FTT) found that, on the balance of probabilities, its primary purpose had been to avoid car and fuel benefit charges.

- The FTT accepted that the taxpayers might have preferred for SAT to enter into the HP agreements. But a lack of willingness to do so on the part of the finance companies made it commercial sense for the company to instead enter into those agreements.
- Since a breakdown of car use between private, partnership and company had not been provided to HMRC, the FTT concluded from the cross-examinations that the taxpayers at least used their cars for business. It would be artificial to split that between partnership and company.
- In the absence of evidence for HMRC's submission that the company's credit card had been used to pay for fuel, the FTT accepted that it was paid on the one in SAT's name.

Relevant legislation

Chapter 6 of Part 3 of ITEPA 2003 provides for the taxation of cars, vans and related benefits. In particular, s 114(1) ITEPA 2003 states that this chapter applies to a car which 'is made available (without any transfer of the property in it) to an employee', 'is so made available by reason of the employment' and 'is available for the employee's or member's private use'.

Section 117 ITEPA 2003 is specific: 'A car or van made available by an employer to an employee … is to be regarded as made available by reason of the employment.'

A car or van is available for private use under s 118 ITEPA 2003 unless 'the terms on which it is available prohibit such use' and 'it is not so used'.

When a car benefit arises, s 149(1) ITEPA 2003 seeks to impose a further fuel benefit charge 'where fuel is provided for a car by reason of an employee's employment'.

Decision – car benefit

Made available

It was not disputed that the cars were made available to the taxpayers. The FTT's findings of fact also showed that the cars were provided for the sole use of the taxpayers, and that they were free to use the cars for their personal use. As such, the FTT concluded that there remained only two further conditions that had to be satisfied for a car benefit to arise under s 114(1) ITEPA 2003. These were that the vehicle was made available 'without any transfer of the property in it' and 'by reason of employment'.

Transfer of the property in it

The words 'transfer of the property in it' refer to the transfer of ownership. In this case, the cars were owned by the finance companies. Although one of the HP agreements allowed for the transfer of rights and obligations under the agreement by consent, there was no evidence of such a transfer. The FTT ruled that the cars were made available under an informal arrangement, which could be seen as no more than a transfer of a possessory or a contractual right to use the vehicles. A transfer of the ownership did not occur. Hence, the FTT's view was that the cars were made available without any transfer of the property in it.

By reason of employment – s 117 ITEPA 2003

If the cars can be shown to have been made available by the company, s 117 ITEPA 2003 would automatically treat the provision as being by reason of employment (this was referred to as the irrebuttable presumption by the FTT). Since the company entered into the HP agreements, transferred payments for the cars from its bank account, received the vehicles and allowed the taxpayers to use them, HMRC submitted that they must be treated as having been made available to the taxpayers.

The appellants submitted that the company could not realistically have made the cars available to the taxpayers because the substance of the matter was that the full cost of the HP agreements was borne by the taxpayers, as partners of SAT, through the recharge mechanism. They pointed to the respective treatments adopted by the company and SAT in their accounts.

Regardless of the underlying economic position, the FTT ruled that, in the absence of a sham or nominee arrangement, the legally binding HP agreement had to be taken at face value. Hence, the FTT ruled that, since the company was the only person in a position to legally make the vehicles available, the company had made the cars available. By reason of the presumption in s 117 ITEPA 2003, the cars were provided 'by reason of employment'.

By reason of employment – case law

It has been recognised in the courts that, 'by reason of an employment' is to be interpreted far wider than the words 'from an employment', which are more common among earnings provisions.

HMRC cited the judgment in the joint cases of *Wicks v Firth (HM Inspector of Taxes)* and *Johnson v Firth (HM Inspector of Taxes)* at the Court of Appeal. Oliver J stated that the 'by reason of employment' test 'involves no more than asking the question "what is it enables the person concerned to enjoy the benefit?"'. For this the FTT had an obvious answer – it was the company that 'made available' the cars through its HP agreements with the finance companies, notwithstanding that the costs of those arrangements had ultimately been recharged to and borne by SAT.

In addition, Lord Denning MR had noted in that decision that 'the fact of employment must be one of the causes, but it need not be the sole cause, or even the dominant cause (of the benefit being granted).' This was relied upon by the FTT in *DJ Cooper and others v HMRC* [2012] UKFTT 439 (TC) in ruling that cars, paid for by a partnership under an HP agreement and recharged to a company, were made available to the directors of that company 'by reason of employment', a case that HMRC understood to be similar to this.

Therefore, the FTT held, as in *Cooper*, that the 'by reason of employment' condition is met even if it had been decided that the cars had not been made available by the company, the employment being at least one of the causes of the cars being made available.

Decision – fuel benefit

In considering s 149(1) ITEPA 2003, and in particular whether fuel was 'provided', the FTT had to turn its attention to how the fuel was paid for. In this case it was by SAT credit card, which is a 'credit token' for the purpose of s 149(3). But this section fails to explain who discharges the debt for the credit token. Even though the debt was fully discharged by the partners, s 149(3) serves to treat the fuel as having been provided for the cars, with the 'cash equivalent' of that benefit being determined in accordance with ss 150 to 153.

The FTT did consider whether the fuel benefit could be treated as nil, in accordance with condition A of s 151. This requires that the fuel costs are made good 'to the person providing the fuel'. However, this would require

the partners to make good the fuel costs to SAT. Since the partners are the partnership for all practical purposes, the FTT considered this to be delving into the ‘realms of the metaphysical’, and was not a situation that Parliament could have considered in enacting s 151. Consequently, the FTT considered that the section required too strained an interpretation to assist the partners.

However, the FTT ruled that there was an overriding requirement that the benefits code in Pt III ITEPA 2003 required there to be an actual benefit to the employee (citing *HMRC v Apollo Fuels Ltd & others* [2014] UKUT 95 (TCC). Since the partners bore the full cost of the fuel through SAT, there was no benefit to the taxpayers that could bring the provision of fuel within the benefits code and, in particular, within s 149 ITEPA 2003.

As such, the income tax and NIC charges on car benefits were upheld. But the fuel benefit charges were discharged, which might at first sight appear a counter-intuitive result given that SAT met the full cost of the provision of the cars (by recharge of the costs of the HP agreements) and the fuel.

Those seeking to arrange matters in a way that does not render liability to car benefit charges should review paragraphs 70–73 of the decision.