

Ghost of Tax Returns Past

Once the enquiry window has closed for your tax return, you should be confident that your tax liability for that year is carved in stone. But you've heard the Taxman can dig up old returns to extract further tax. Is this a true horror story or just a myth?

Certainty

The self-assessment system is supposed to give you confidence that once you paid the last instalment of tax for say 2002/03 on 31 January 2004 your tax bill is final and you can't be asked to pay any more. Unless the Taxman opens a formal enquiry before 1 February 2005 your 2002/03 tax return should be buried forever.

Raising the dead

The Taxman has two fall-back excuses he can use to resurrect tax files at a later date:

1. If he can prove you have committed fraud or negligence when completing your tax return (section 29(4) Taxes Management Act 1970); or
2. He makes a so-called discovery of information relevant to your tax bill which he could not be reasonably expected to be aware of when the enquiry window closed, (section 29(5) Taxes Management Act 1970).

Translation

So if you have been good and honest taxpayer and explained any calculated figures in the white space on your tax return, you should achieve the all important *certainty*. Well that was the position until the Taxman won a recent case: *Langham v Veltema* (2004) STC544 in the High Court.

What happened

Mr. Veltema was given a house by his company, worth £100,000 according to an independent valuer. Mr. Veltema self-assessed the tax due on this benefit in kind (the gift of the house) on his tax return, which was accepted without question by Tax Inspector A. When the company's tax return was submitted to a separate tax office Tax Inspector B questioned the value of the house given to Mr. Veltema. This value was eventually agreed by Taxman B at £145,000, who then told Taxman A that Mr. Veltema had not paid enough tax. However the enquiry window for Mr. Veltema's personal tax return had closed, so Taxman A had to use the discovery excuse (no. 2 above) to demand the additional tax.

A blinkered Taxman

The Judges ruled that Taxman A only had to consider the information in front of him when deciding whether Mr. Veltema's tax return was correct. Although the Taxman B had received additional information from the company's accounts when the enquiry window closed, the relevance of this data was not specifically drawn to Taxman A's attention.

Wide implications

This ruling has huge implications for family businesses who pay profits to a spouse or family member who is not the main worker. This is the so-called s.660 issue, where the Taxman wants to tax the main worker on the whole profits of the business. The spouse's entitlement to some of the profits is based on information shown in the

business accounts and in the company's Memorandum and Articles of Association which would not normally be submitted with the personal tax return.

This year's return

The Tax professional bodies are now recommending that any individuals who are potentially affected by the s.660 issue should send the following information in with their 2003/04 personal tax returns:

- their company or partnership accounts;
- the tax computations for the company or partnership;
- the memorandum and articles of association of the company, or partnership agreement; and
- a summary of what is done by each of the shareholders or partners in running the business.

Each document must be referred to in the white space on the tax return to ensure the blinkered Taxman is not oblivious to its relevance.

To ensure the Taxman cannot open up your long dead tax files you need to send him absolutely all the information he may need, even if this has already been sent to a different tax office.