**INCOME TAX**

**LECTURE 1**

**SLIDE 1 – INCOME TAX**

Hello, my name is Sarah Brooks. This online lecture relates to the subject area of taxation. During the Foundation Course, you will be studying three areas of taxation: income tax, capital gains tax and inheritance tax.

There are eleven on-line lectures that you will need to listen to prior to commencing the Foundation Course; six on income tax, three on capital gains tax and two on inheritance tax.

You will find it useful on at least one occasion when you listen to these on-line lectures if you refer to the accompanying PowerPoint slides.

This online lecture relates to income tax and as I have mentioned is one of six on-line lectures relating to income tax. After you have listened to all six online lectures relating to income tax please refer to the recommended reading for this topic and prepare the tasks for the small group session on income tax.

**SLIDE 2 – OUTCOMES**

In this first online lecture on income tax, I am going to be talking about the different sources of income tax law:

* explaining what is meant by the term income and
* identifying the different sources of income and
* explaining who pays income tax.

**SLIDE 3 – SOURCES OF LAW**

There are three main sources of Income Tax law: Statute, Case Law and Official Statements.

The main charging provision for Income Tax is the Income Tax Act 2007, however the Income Tax (Trading and Other Income) Act 2005 and the Income Tax (Earnings and Pensions) Act 2003 are also very important and will be referred to later on in these online lectures.

Imagine if every time anybody had a question or an issue regarding Income Tax it had to be referred to the courts there would be huge backlog of cases. As a result, Her Majesty’s Revenue and Customs, otherwise known as HMRC, issue what we call Official Statements. There are two types of Official Statements: statements of practice and extra statutory concessions. Statements of practice basically set out the views of HMRC on various points on taxation, clear up any doubts that you may have and if you fall within the criteria of an extra statutory concession HMRC will either waive the right to collect tax or give you a reduction.

**SLIDE 4 – WHAT IS INCOME?**

Before we can talk about Income Tax, we need to be able to understand what is meant by the term Income. There is no statutory definition of the word income, but it is commonly accepted that in order for something to be of an Income nature it has to have an element of recurrence to it rather than be a one-off payment. For example, the salary that you receive from your job. You receive that either on a weekly or monthly basis and it has an element of recurrence to it and therefore it is income. Other examples of income would be the profits that you receive from a business, rent from renting out a property or the interest that you might receive on your bank accounts. These all have an element of recurrence to them and are therefore Income. In comparison if you sell for example your holiday home that would be an example of Capital. It is a one-off transaction and therefore is not subject to Income Tax rather it would be subject to Capital Gains Tax which we talk about in later online lectures.

**SLIDE 5 – WHAT INCOME IS TAXABLE?**

Now we understand what Income is, something which has an element of recurrence to it, we can now talk about what types of Income are taxable. For Income to be taxable it must come from one of the sources set out in the Income Tax Trading and Other Income Act or the Income Tax Earnings and Pensions Act that I mentioned previously.

**SLIDE 6 – SOURCES OF INCOME ITTOIA/ITEPA**

The main sources of Income set out in the Income Tax Trading and Other Income Act which are subject to Income Tax are Trading Income, so income from your business or your trade. Property Income, so income from renting out a property and Savings and Investment Income and by this we mean the interest you receive on your savings or any dividends that you might receive on any shares that you hold. The Income Tax Earnings and Pension Act also sets out that any income that you receive from your employment, so your salary, is also subject to Income Tax.

**SLIDE 7 – WHO PAYS INCOME TAX?**

The final thing for us to consider in this first online lecture then is who pays Income Tax. Well individuals like you and me do, we pay Income Tax on our salaries, Sole Traders pay Income Tax on the profits made on their business and partners in a business also pay Income Tax. It is important to note at this point that the individual partners in a Partnership pay tax on their own personal share of the profits made by that partnership business. Personal representatives also pay Income Tax as do Trustees. Companies on the other hand do not pay Income Tax. Companies pay Corporation Tax and we will talk about that in more detail as part of the Business Law and Practice core subject area.

**SLIDE 8 – ANTI AVOIDANCE LEGISLATION**

The “general anti abuse rule” (GAAR) took effect from 17 July 2013 having been introduced by the Finance Act 2013. It applies to income tax and is intended to counteract tax advantages arising from tax arrangements that are abusive and use loopholes in the legislation to avoid the payment of tax.

A ‘tax arrangement’ is any arrangement which when viewed objectively has the effect of obtaining a tax advantage as its main purpose or one of its main purposes. For any arrangement to be caught it must also be ‘abusive’.

Abusive tax arrangements are ‘arrangements the entering into or carrying out of which cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances…’

There is a double reasonableness test. The main safeguard for the taxpayer and one of the key principles of the general anti abuse rule is the ‘double reasonableness test’. This requires HMRC to be able to show that the arrangements entered into ‘cannot reasonably be regarded as a reasonable course of action’.

Where tax arrangements are found to be abusive, then the tax advantages are counteracted in a way which is just and reasonable, so for example increasing the individual’s taxable income or decreasing allowable deductions.