December 2023

Tax Update

Contents

1. General

1.1 Season's Greetings

We wish all our readers a merry Christmas and a happy and healthy New Year.

The next edition of Update will be published in January 2024.

1.2 Company wins appeal on information notice

An information notice was varied to allow a company to send to HMRC only those emails that were relevant to the matter, not those caught by a wider email search but irrelevant.

The company underwent refinancing in 2014, and claimed interest on the new debt. HMRC considered refusing this on unallowable purpose grounds. The bond had been transferred to a different company in 2017. As part of its investigation, HMRC issued an information notice. This, rather than requiring specific documents, listed a number of terms that the company should carry out email searches for, including "avoidance" and required it to provide copies of all the emails that matched the search terms.

This identified over 11,000 emails. The company's adviser reviewed these, and sent HMRC the 1,695 emails that it considered relevant to the refinancing and transfer of the bond. HMRC argued that all the emails should be provided.

The taxpayer appealed, arguing that the notice was invalid as it did not specify nor describe the documents it asked for, that the emails not sent were not reasonably required for the purposes of the investigation, as they were irrelevant, and that the notice should be varied to limit the dates for documents requested, and exclude documents HMRC had agreed were not required or were privileged.

The FTT found that the notice was not invalid just because it asked for email searches rather than documents, but that the requirements were too wide. For example, any email with the phrase "avoidance of doubt" was caught, and some emails caught related to personnel matters such as maternity leave. The FTT stated that had the taxpayer appealed before it sent any of the emails it would have allowed the appeal on the basis that it was too broad. As the position had changed by the time of the hearing with some documents set, it simply varied the notice to exclude the emails deemed irrelevant by the adviser.

Parker Hannifan (GB) Limited v HMRC [2023] UKFTT 971 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08992.html

2. Private client

2.1 New disclosure facility for underpaid tax on cryptoassets

HMRC has launched a new online disclosure facility, that can be accessed with a Government Gateway ID. This is solely for reporting underpaid tax on cryptoassets, both income and capital gains.

The facility is similar to the existing disclosure processes available, with no specific mitigations offered, other than those that naturally come from promptly telling HMRC about underpaid tax. However the facility has been announced alongside the backdrop of a renewed focus from HMRC on tackling tax non-compliance in respect of cryptoassets, which includes a new tranche of letters being issued to taxpayers where HMRC suspects non-compliance. Penalties can be significantly higher when HMRC enquire, than when a disclosure is made unprompted.

Examples of disclosure scenarios include where unreported gains have arisen from either large disposals or high frequency trading, where income has been received from mining activities, or where cryptoassets have been received as remuneration. The tax calculations can be complicated, so HMRC suggests appointing a specialist adviser to assist with the disclosure process.

A guidance note on how to pay tax on cryptoassets has been published alongside this facility (link below).

If you need any tax advice on cryptoassets, or on making a disclosure to HMRC please do get in touch.

www.gov.uk/guidance/tell-hmrc-about-unpaid-tax-on-cryptoassets

www.gov.uk/guidance/pay-tax-on-cryptoassets

2.2 Appeals on seed enterprise investment scheme refused

The FTT found that companies did not meet the conditions for investment to qualify under the seed enterprise investment scheme (SEIS). The companies were not trading and there was not enough risk to capital.

Ten companies, all of which had the same sole director, appealed against HMRC's decision not to grant them the right to issue SEIS certificates to their investors.

The director planned to produce audio-visual content to sell at religious sites in India and Nepal. He set up one company for each of the intended sites, ready to develop the material, the nature of which changed during planning. He made advance assurance applications for each, and HMRC confirmed that based on the information he provided on financial and business plans, investments could be made under SEIS, subject to final authorisation. HMRC refused the final applications.

The FTT carefully considered the details of the initial investments, and what activities were conducted. It agreed with HMRC that the conditions to issue SEIS certificates were not met. The companies did not meet the risk to capital condition, as there was no intention to take on staff, nor increase turnover, and the primary reason for having separate companies was to allow more SEIS relief to be claimed. The trading condition was also not met, as the companies were not trading on a commercial basis. Some work for the companies was done by another group out of goodwill, not commercially, and there was not enough evidence that the companies were creating unique intellectual property.

This case highlights that meeting these conditions can be complex, particularly as here getting advance assurance was not enough to ensure the claims were successful. If you would like any tax advice on enterprise investment schemes (EIS) or SEIS, please do contact our expert Rebecca Combes.

www.evelyn.com/people/rebecca-combes/

Legend of Golden Temple Ltd & Ors v HMRC [2023] UKFTT 988 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08999.html

2.3 AI did not help CGT case

The taxpayer's appeal to the FTT against failure to notify penalties was based on cases which had been generated by an AI system. The AI system had not cited real tax cases, but made them up. Regardless of this issue, she did not have a reasonable excuse for failure to notify.

The taxpayer sold a rental property without informing HMRC. She had also not declared the rental income. When this was discovered, she paid the CGT of over £16,000, but appealed against the failure to notify penalty. She had not taken professional advice nor researched whether or not to declare the sale, but claimed that she thought she would hear from HMRC after the sale was registered on the Land Registry.

In her submission for the appeal, she cited nine previous FTT cases that demonstrated taxpayers winning on reasonable excuse grounds of ignorance of the law or mental ill health. The judge was unable to trace official records or the full text of these, and found that they had been made up by the AI system that was used to write the submission.

This point was not determinative, but the FTT found that she did not have a reasonable excuse for failure to notify, so was subject to the penalty. A reasonable person would have contacted HMRC or an adviser, rather than putting some money aside as she had done. Her mental health problems had not prevented her from arranging the sale of the property and dealing with tenants, so did not prevent her from looking into CGT liabilities.

While generative AI presents many exciting opportunities, this case highlights its current limitations and the risks around using AI tools to gather and analyse complex tax information without seeking appropriate professional tax advice.

Harber v HMRC [2023] UKFTT 1007 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC09010.html

2.4 Property income found to be investment not trading

The FTT found that although a taxpayer had renovated and sold three properties, the requirements for this to be classed as a trade were not met. The gains were taxable as capital rather than income.

The taxpayer appealed four discovery assessments, three closure notices, and associated penalties. The amount at stake was almost £1m.

The discovery assessments were for rental income from letting a flat, where the taxpayer argued that expenses exceeded rent. The FTT found that this was a careless mistake rather than deliberate behaviour, so allowed the appeal on that point as that meant that the years were out of time to be assessed.

The closure notices related to capital gains on the sale of three properties that the taxpayer had renovated . HMRC argued that the renovation and sale of these three amounted to a trade, so profits should be taxed as income. The taxpayer was a builder, so HMRC considered it linked to his job.

The taxpayer argued that he had occupied each property as a family home, albeit for short periods.. The moves were due to family reasons, and the renovations to make the properties suitable for his family to occupy them. The FTT considered the background to the transactions, ran through the badges of trade, then considered the question in the round. Though some badges were met, such as financing and renovation, it found that it was more likely than not that the purchases were to acquire a family home, and the sales were due to changes in circumstances. There was no trade, any gains were taxable as capital. It also found that private residence relief was available on this basis.

Ives v HMRC [2023] UKFTT 968 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08989.html

2.5 Resounding SC win for taxpayer on transfer of assets abroad

The SC found that the transfer of assets abroad (TOAA) code did not apply to taxpayers who caused a company to transfer its business to an overseas company, overturning the CA ruling. HMRC's cross appeal was dismissed.

The taxpayers transferred their telebetting business from a UK company to a Gibraltar company, as it was commercially imperative to be able to offer customers a reduced rate of betting duty. The UK resident taxpayers, a family group, were directors and shareholders of both companies, so paid tax in the UK on salary and dividends. HMRC sought to tax them on the entire profits of the transferee company, in proportion to their shareholdings, on the grounds that they had made a transfer of assets abroad. Much of this profit had been reinvested in the development of new streams of the business. When the laws relating to betting duty were amended, the telebetting business was bought back to the UK.

The UT found that TOAA did not apply, as the taxpayers had not made a transfer, just the company. The CA overruled this, finding that they had procured the transfer, and that although the transfer was to save the business, this was inextricably linked to tax avoidance of betting duty.

The SC found for the taxpayers. It agreed that TOAA only applied to individuals who transfer assets abroad, the most natural interpretation in its view. It did not apply to transfers by companies, regardless of how large a shareholding the individual the charge might apply to had. There was nothing in the legislation about individuals being treated as controlling a company. As the taxpayers had not personally transferred the assets TOAA did not apply.

HMRC v Fisher & Anor [2023] UKSC 44

www.bailii.org/uk/cases/UKSC/2023/44.html

3. PAYE and employment

3.1 Third party payments were taxable employment benefits

The FTT found that gifts made to employees from the chairman's own pocket were taxable as employment income. They were made by reason of employment.

On sale of a company, the majority shareholder, who was also the chairman, made payments to the employees from his personal resources, though paid through the company. PAYE and NICs were initially deducted, then the company tried to reclaim this on the grounds that these were non-taxable gifts.

The FTT found for HMRC that these payments were taxable. They were not direct earnings, but should be taxed as employment benefits. Although freely made gifts, the reason the employees got them was by reason of their employment, they had no independent relationship with the chairman. The payments were also calculated by length of service.

OOCL UK Branch v HMRC [2023] UKFTT 996 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC09007.html

3.2 Inducement to accept changes to pension scheme found to be earnings

The CA has overturned a UT decision, finding that payments made to employees to compensate for future reduced pension payments were taxable as earnings. The payments were made to induce the employees to work willingly in the future, not just to put them in the same position as before.

A large company decided to change its pension scheme arrangements, and made payments to employees to facilitate the change. HMRC held that for 1,100 of the employees the payments derived from the employments, and should be subject to IT and NICs as earnings. The FTT agreed with HMRC, finding that that the change to pension arrangements was part of a wider renegotiation of working conditions, and could not be separated from the integrated package. Although the employees lost a right to purchase additional pension benefits, only 7% of scheme members used that right.

The UT overturned that decision, finding for the employer that the payments were compensation for the expected lower pension payments, and reduction in future employer contributions, so were non-taxable as they simply put the employees in the same position as before the change.

The CA overturned the UT decision and reverted to the FTT view. It found that the rule the UT had applied, which originated in an earnings from work case, did not have to apply to pension rights. The payments were an inseparable part of an overall package offered to compensate for a loss in another area. The payments were earnings.

HMRC v E.ON UK Plc [2023] EWCA Civ 1383

www.bailii.org/ew/cases/EWCA/Civ/2023/1383.html

4. Business tax

4.1 Goodwill belonged to the individuals not the company

A firm of financial advisers transferred its business from a company to an LLP. The taxpayers contended that their accounts, which HMRC had not challenged as being GAAP compliant, showed that the goodwill had never belonged to the company. Each adviser had a client bank that was personal to them, and held that goodwill personally. When it was transferred into the LLP the payments made for it were made directly to the taxpayers. HMRC argued that the goodwill belonged to the company, so the money reached the taxpayers as a distribution from the company as the LLP owed it to the company.

The FTT agreed with the taxpayers that the SC NCL case set a clear precedent that accounts prepared in accordance with currently accepted accounting principles "are the best guide as to the true and fair view of the profit or loss of the company in the relevant accounting period" and that there was no basis to conclude that the accounts were anything other than GAAP compliant.

On this basis the company did not own the goodwill, but just fixed assets, Stating as HMRC did that the company owned the goodwill would mean that over £2m was missing from the balance sheet for several years, a material inaccuracy, which was not a conclusion that could be drawn from the evidence.

The FTT distinguished classic goodwill, where the asset is a client base providing ongoing income, from a personal relationship that might be leveraged to bring new business. It found that the relationships themselves represent a valuable asset which vested with each of the individuals, and which could, subject to the decision of a client to transfer that relationship to another advisor within the company, be taken from the company without restriction.

In conclusion, it was found that the goodwill belonged to the individuals, and so there could be no distribution from the company.

Smith & Anor v HMRC [2023] UKFTT 912 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08977.html

HMRC v NCL Investments Ltd & Anor [2022] UKSC 9

www.bailii.org/uk/cases/UKSC/2022/9.html

5. Tax publications and webinars

5.1 Tax publications

The following Tax publications have been published.

- Transmission and exchange of payment data to fight VAT fraud - Central Electronic System of Payment information
- Tax efficient giving to UK charities
- What the Autumn Statement 23 means for individual taxpayers
- Environmental taxes: Autumn Statement 2023
- Autumn Statement 2023: The impact on businesses
- Autumn Statement 2023. Clarity on changes to R&D tax relief

6. And finally

6.1 ChatGPT can't chat CGT

2.3 is a cautionary tale for our times: don't just check your work, check your AI's work.

With this in mind, *And finally* had a few goes at getting AI to write this segment of the newsletter. The AI's jokes took a slightly cavalier attitude towards topics such as imprisonment for tax avoidance and Government finances, so we will not reproduce them in full here. We were however delighted when it added this under its comment:

Disclaimer: This comment is intended for entertainment purposes only and does not reflect my opinion or advice on any tax matters. Please consult a professional tax adviser before making any tax decisions.

Well done AI. Now we just need to wait for the first AI system to pass some tax qualifications.

Glossary

Organisations		Courts	Taxes etc	
ATT – Association of Tax Technicians	ICAEW - The Institute of Chartered Accountants in England and Wales	CA – Court of Appeal	ATED – Annual Tax on Enveloped Dwellings	NIC – National Insurance Contribution
CIOT – Chartered Institute of Taxation	ICAS - The Institute of Chartered Accountants of Scotland	CJEU - Court of Justice of the European Union	CGT – Capital Gains Tax	PAYE – Pay As You Earn
EU – European Union	OECD - Organisation for Economic Co-operation and Development	FTT – First-tier Tribunal	CT – Corporation Tax	R&D – Research & Development
EC – European Commission	OTS – Office of Tax Simplification	HC – High Court	IHT – Inheritance Tax	SDLT – Stamp Duty Land Tax
HMRC – HM Revenue & Customs	RS – Revenue Scotland	SC – Supreme Court	IT – Income Tax	VAT – Value Added Tax
HMT – HM Treasury		UT – Upper Tribunal	LBTT – Land and Buildings Transaction Tax	