July 2023

Tax Update

Contents

1. General

1.1 HMRC initiative to deal with old post

Significant delays in dealing with correspondence have led to a new HMRC initiative to try and deal with post over a year old.

HMRC has acknowledged the significant delays in processing some letters. A taskforce has now been established that will work specifically on post that is over 12 months old and is still waiting for a response.

The taskforce seems to be an extension of the Agent Account Manager service., and a new special contact form has been introduced which agents can use to identify and progress post over 12 months old. This new initiative will be reviewed on 4 August, with a possible extension if the trial is successful.

www.tax.org.uk/hmrc-announces-taskforce-to-address-old-post

1.2 Tax gap stays at 4.8% for 2021/22

HMRC has published its annual report on estimating underpaid tax and has concluded that increased revenues have not changed the percentage of tax due that is not paid. In absolute terms this has risen from £31bn in 2020/21 to £36bn in 2021/22.

Key points from its estimates include:

- 30% of the tax gap is from CT.
- 35% is from IT, NICs, and CGT combined.
- The VAT gap is trending down.
- The biggest contributor to the tax gap is small businesses (56%).
- 'Wealthy' individuals account for 5%, all other individuals for 6%.
- In the analysis of behavioural reasons, failure to take reasonable care was the largest contributor at 30%.

www.gov.uk/government/news/tax-gap-holds-steady-at-48

2. Private client

2.1 High income child benefit charge appeal stayed

The FTT has stayed a high income child benefit charge (HICBC) appeal pending determination of the test case on this matter. The taxpayer's appeal against penalties was allowed, as his reasoning for not looking into the subject was valid. He was childless, but cohabiting with a partner who had children while keeping separate finances.

The taxpayer had been issued with HICBC assessments covering four tax years, as in that period he was cohabiting with a partner who had two children of her own. They maintained separate finances. When they commenced cohabiting he was unaware that she claimed child benefit, and he also earned under £50,000 a year. His earnings subsequently increased.

The FTT agreed that the taxpayer was unaware of the HICBC despite HMRC publicity campaigns, as he was unaware that child benefit was a relevant topic for him at the time. It also found that he had not received a letter HMRC claimed to have sent in 2013, with the probability being that it was never sent as the taxpayer earned under the threshold in 2013 and had only just started cohabiting. When he received a nudge letter in 2021, he asked his then wife and discovered that she was receiving child benefit, which she then stopped claiming.

The FTT:

- Found that the taxpayer had indicated that he planned to appeal by the required date such that HMRC was unable to apply retrospective legislation, and two of the appeals were stayed behind final litigation in the Wilkes case.
- Accepted the taxpayer's appeals against penalties, as he had a reasonable excuse for being unaware that HICBC was due in the circumstances above.
- Found that HMRC was out of time to assess two of the tax years, because as he was not careless the extended time limit did not appeal.

Ashe v HMRC [2023] UKFTT 538 (TC)

https://financeandtax.decisions.tribunals.gov.uk/Aspx/view.aspx?id=12756

HMRC v Wilkes [2022] EWCA Civ 1612

www.bailii.org/ew/cases/EWCA/Civ/2022/1612.html

2.2 COVID self-employment support payment misclaimed in two cases

The FTT has found in two cases that taxpayers who misunderstood the COVID self-employment income support scheme (SEISS) eligibility criteria must repay grants.

The first taxpayer worked through a company, but had until recently been self-employed. The second taxpayer had not traded in 2019/20, which was a requirement for eligibility. He was self-employed in 2018/19, and submitted a return for that year, but after failing to secure work he had claimed universal credit. He had alerted HMRC to the issue after receiving a later email from it about eligibility criteria.

Both claimed grants under the SEISS in the early days of the pandemic. HMRC sought to recover the grants paid in error, and the taxpayers appealed. They both pointed out that they had been invited to apply, the first sought to make a legitimate expectation argument, though accepting he was ineligible, and the other that he might actually have been trading.

Both appeals were dismissed. The FTT considered the claims process, including looking at screenshots of the online forms. Although the taxpayers' changes in circumstance had led to HMRC sending them emails to make a claim in error, eligibility was clearly explained online before the incorrect claims were made, including that they must still be trading. The FTT had no room to consider whether or not the law is fair. The second taxpayer had told HMRC during the investigation that he had stopped trading in November 2018, so was not eligible.

Ash v HMRC [2023] UKFTT 272 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08749.html

Hamill v HMRC [2023] UKFTT 451 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08827.html

3. Trusts, estates and IHT

3.1 Estate loses appeal on domicile

The FTT considered a domicile case with a complex family history, and found that the taxpayer died domiciled in England and Wales, his home for the last 43 years of his life, despite him declaring an Indian domicile. His plans to return to India were only vague and were not supported by evidence.

The taxpayer was born in pre-partition India, in the part that is now Pakistan (Karachi). His parents were living in Tanzania at the time, but his mother returned to her home city of Karachi for the birth. His father was born in the section that is now India, moved to Karachi when a child, then moved to Tanzania after his marriage. The taxpayer was sent to Karachi for the latter part of his education. Partition took place whilst he was at university in Karachi, as a consequence of which he moved to present-day India to complete the course. After graduation he returned to Tanzania.

When the political situation in Tanzania deteriorated, he and his family moved to India, his wife's home country, and a year later, in the early 1970s. they moved to the UK, as did much of his family. He had made a UK will for UK assets and an Indian will for non-UK assets.

His executors contended that he had retained a non-UK domicile for IHT, as he had only moved to the UK as he could not secure employment in India and intended to return at the end of his working life. On his retirement he had delayed his return due to his own and his family's medical issues. There was limited documentation available. On an HMRC form describing his domicile, he had described himself as domiciled in India, noted that he could stay in a relative's flat when in India, and that he intended to leave the UK when his personal affairs and health allowed.

The FTT found that he had acquired a domicile of choice in England and Wales. He had limited connections to India, with only two visits there during his 43 years of life in the UK before his death aged 87. Realistically, given his family connections in the UK, age, and state of health, he would not have been preparing to leave the country. He had no connection at all with modern

Pakistan, and had never lived in India for longer than his three years at college. The FTT commented that his plans to move to India were only a vague idea and were not supported by the evidence of his life overall.

The FTT made no finding on his country of domicile of origin.

Shah v HMRC [2023] UKFTT 539 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08842.html

4. PAYE and employment

4.1 Payment to employee benefit trust found to be earnings

The FTT has found that a payment to an employee benefit trust (EBT) was earnings of a director of the company that made the payment. The EBT had loaned the money to the director, and it was linked to his work for the company, despite this being a short term loan.

The taxpayer, a company, paid £800,000 to the trustee of an employee benefit trust (EBT), which made a loan of the same amount to a director of the taxpayer. HMRC classed the payment to the EBT as earnings of the director, and the taxpayer appealed.

The taxpayer argued that this was a genuine loan, which as the documents showed, was repayable on demand after five years. It argued that the EBT's purpose was to reward and incentivise employees in the short term, like with this short-term loan. The director was using shares in the taxpayer company as security for the loan, which he had purchased from his wife. Receipt of capital of a loan used to purchase shares in a close company is not taxable.

The FTT rejected this and found for HMRC. The payment to the EBT was paid by the company as a reward for the services the director supplied to the company. It was therefore earnings. There was no evidence that the £800,000 would have been paid to the director if the loan arrangement was not used, but the trustees made the payment to him because he was considered to have been under-rewarded. The fact that this ruling created double taxation did not affect the ruling, as it was simply a consequence of the arrangements put in place by the taxpayer.

M R Currell v HMRC [2023] UKFTT 613 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08855.html

4.2 Rent not an allowable deduction from employment income

The UT has disallowed a claim for accommodation expenses as a deduction from employment income, overturning an FTT decision that allowed the claim in part. This was incidental expenditure and none was an allowable deduction.

The taxpayer, an experienced dental surgeon from Southampton, chose to take a four year course to train as a maxillofacial surgeon in London. He rented modest accommodation locally and claimed the cost against his employment income while on the course. HMRC denied the claims, arguing that he was not required by his employment contract to live near the hospital, and he did not work from home. HMRC argued, therefore, that he did not incur the expenses in the performance of his duties, and derived personal benefit from the accommodation. To claim expenses against employment income, they must have been incurred wholly, exclusively, and necessarily for the purposes of the employment.

The taxpayer explained that London was the only available location to take the course, and his family could not move. He had found that the commute from Southampton left him too exhausted to discharge his obligations as a doctor safely. He was also required to spend two nights a week and one weekend in six on-call, when he had to be able to reach the hospital within 30 minutes. He was telephoned by the hospital on most other nights for advice. He had returned to the family home on his free weekends, using the accommodation only to study and sleep.

The FTT allowed his claim in part. It found that only the proportion of the accommodation costs related to the nights that he was on call was allowable, along with time taking telephone calls from the hospital, and visits to the hospital on nights that he was not formally on call.

HMRC disagreed with the FTT ruling and appealed to the UT on the basis the FTT had erred in law. The UT agreed with HMRC, and disallowed the taxpayer's appeal in full. Although he used the accommodation while performing his duties, the rent was not incurred wholly, exclusively and necessarily in the performance of his duties, but purely incidental expenditure. It put him in a position to do the work, but the cost was not incurred in the performance of his duties.

Kunjar v HMRC [2023] UKUT 154 (TCC)

www.bailii.org/uk/cases/UKUT/TCC/2023/154.html

5. Business tax

5.1 CA allows taxpayer's appeal on double tax agreement interpretation case

The CA overturned a UT decision that 'royalty income' was taxable in the UK. The CA deemed the receipts to be business profits within the terms of the relevant double tax agreement (DTA).

A Canadian resident bank made a significant loan to enable a Canadian resident company (the borrower) to acquire rights to explore and exploit an oil field in the North Sea, through the borrower's UK subsidiary. The borrower then sold those rights, partly in exchange for an entitlement to 'royalty' payments, calculated by reference to oil produced from the oil field. Subsequently, the borrower went into receivership. Under the insolvency proceedings, the bank was assigned the rights to the 'royalties'. The bank declared the royalties in its Canadian tax return, but not in the UK. HMRC disagreed with this treatment and considered that the UK had primary taxing rights over the payments under the UK-Canada treaty and so sent the bank discovery assessments. The bank appealed the assessments, first at the FTT, which sided with HMRC, then at the UT, which also sided with HMRC, and finally at the CA.

The CA disagreed with the FTT and UT decisions that the UK had taxing rights derived from the extraction of natural resources. The CA instead held that the payments were not taxable under the treaty, as they did not derive from the actual working of the oil field, but were merely payments derived by reference to oil production on the oil field. The CA held that while the payments were derived by reference to oil production on the oil field, the borrower had never held the actual right to work the oil field in the first place, which was originally held by its UK subsidiary. As such, the payments were not "income from immoveable property" and therefore not taxable in the UK.

This case is useful in that:

- It articulates the court's reasoning on aligning different articles within a treaty;
- It reiterates important principles of treaty interpretation, such as the status of the Vienna Convention and the equal weight of bilingual texts. It also highlights the CA utilising an 'ordinary meaning' approach to interpreting a treaty as opposed to a more narrow 'English meaning', as required by the Vienna Convention, where "income from immovable property" is deemed to arise only where there is a direct link to immovable property.
- It clearly states that 'post-date interpretive aids', such as commentaries that were published after a relevant treaty was signed and ratified, may be used "and given such persuasive force" provided they do not directly contradict the treaty.

Royal Bank of Canada v HMRC [2023] EWCA Civ 695

www.bailii.org/ew/cases/EWCA/Civ/2023/695.html

5.2 No deduction for costs of facilitating the disposal of mortgaged property

The FTT has found for HMRC in a complex case where a deduction was claimed for a payment of £33.5m to an Irish government agency. The company claimed that a deduction was due under either the loan relationship rules, or in computing the chargeable gain on the sale of a property.

The taxpayer's argument was that the payment should be viewed in two component parts: the amount paid to the government agency for the release of that agency's security over the property that the taxpayer was developing; and a payment made in relation to a guarantee in relation to another company's debts that secured the taxpayer ongoing access to development finance for the property.

The FTT firstly considered whether a payment by the taxpayer, a property developer, was deductible under the loan relationship rules in calculating profits for corporation tax purposes. The FTT held that the payment was instead made in the interests of the wider group of companies, in particular two individual shareholders/directors, of which the taxpayer was a member, and that a deduction should be denied under the loan relationship rules.

The FTT then considered whether a deduction was available in calculating the chargeable gain on the disposal of the property, and concluded that the sum was not paid wholly and exclusively for enhancing the value of the property. It was made in the wider interests of the group and not solely in the interests of the taxpayer itself. As such, no deduction was allowed and the appeal was dismissed.

This ruling helps to illustrate:

- That the substance of transactions needs to be considered in order to ascertain whether they are made for the benefit of an entity or the wider interests of the taxpayer's group, or it's individual shareholders.
- What qualifies as 'from a transaction for the lending of money' for loan relationship purposes.
- The significance of the "wholly and exclusively" requirements in section 38 TCGA92 for CGT acquisition and disposal costs.

Swiss Centre Ltd v HMRC [2023] UKFTT 449 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08825.html

6. VAT and Indirect taxes

6.1 Property with paddock mixed-use for SDLT

The FTT has found that a paddock adjacent to a property, on a separate title and leased out for grazing was non-residential. The taxpayers won their appeal to have the purchase of house and paddock treated as mixed-use for SDLT.

The taxpayers, a married couple, bought a house and a paddock in one transaction, and filed an SDLT return on the basis that this was a mixed-use property, as the paddock was non-residential. HMRC failed in their argument that the property was sold as an equestrian property, of which the paddock was a necessary part, and that the paddock was part of the garden and grounds.

The house and the paddock were on separate titles.

In this case, the FTT found for the taxpayers. The property did not have any stables and consisted solely of the actual garden and tennis court, with the paddock not being an integral part, and not visible from the house or gardens. A third party held a grazing lease over the paddock, which had separate access not over the rest of the property. The paddock had a separate title from the rest of the property, and the taxpayers would not have bought it if it had been possible to purchase the rest of the property without it.

There have been a number of cases on the definition of a mixed-use property for SDLT, which have often been won by HMRC at tribunal, so this is an interesting case demonstrating what the FTT is more likely to see as non-residential use.

Sutterwalla & Anor v HMRC [2023] UKFTT 450 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2023/TC08826.html

7. Tax publications and webinars

7.1 Tax publications

The following Tax publications have been published.

- Transfer pricing opportunities for fintechs
- Plastic packaging tax guidance update
- Transfer pricing post-Brexit: a simpler solution for brokerage firms
- Update on plastic packaging tax
- Red diesel: are you complying with the 2022 reforms?

7.2 Webinars

The following client webinars are coming up soon.

- Employee Ownership Trusts – 26 July

8. And finally

8.1 Happy Legislation Day!

Just before publication, what did we see but the draft Finance Bill 2023-24. Yes, this is one of the tax adviser's favourite days of the year: Legislation Day. The Budget may get the headlines, but this is where the delightful nitty-gritty of draft legislation appears, ready for months of input and wrangling before it forms the final Act.

We will bring you the details in next month's update.

www.gov.uk/government/publications/draft-finance-bill-2023-24-legislation-impacting-definitions-and-declaration

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	