

UK Tax Disputes Digest

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Introduction

Welcome to the summer 2024 edition of our UK Tax Disputes Digest: a high-level summary of key developments in contentious tax over the last few months for heads of tax, finance directors, general counsel and other in-house professionals.

As with previous editions, we have seen a continued increase in HMRC activity across various areas. Both individual and corporate taxpayers would be well-advised to check their tax position as soon as possible to prepare for any potential HMRC investigation into their tax affairs.

In this edition, we look at just a few of these developments, including the latest in relation to HMRC's position on the salaried member rules and the latest series of HMRC nudge campaigns.

We also cover a number of notable tax cases and other interesting procedural decisions. This includes the most recent case law development on the unallowable purpose test within the loan relationship rules and some landmark decisions in relation to VAT and management expenses.

About the team

With 14 partners in our London office, the CMS tax team is one of the largest in the City and advises high-profile clients across a wide range of sectors and all areas of tax. As part of that general tax practice (and the CMS global network with tax capability in over 70 offices), our tax team regularly helps both individuals and corporates with all aspects of tax dispute prevention, management and resolution.

The CMS disputes team is one of the UK's leading contentious practices with some 500 disputes lawyers in the UK alone. We regularly appear before all courts and have more sector and practice expertise among our disputes lawyers than any other firm. We are one of only a few firms to routinely appear in The Lawyer's annual reports on leading cases both for first instance and appeal cases.

The firm's contentious tax practice pools the resources of the CMS tax and disputes teams, including dedicated tax disputes specialists.

For more information on our team and the type of work we undertake, please see [here](#).

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In focus: Unallowable purpose – where are we now?

The Court of Appeal has recently published judgments in three cases on unallowable purpose, which represent significant victories for HMRC. It is therefore appropriate to reflect upon the current state of evolution of the unallowable purpose rule.

The unallowable purpose rule (section 441 of the Corporation Tax Act 2009 (“**CTA 2009**”)) operates to restrict the deductibility of interest in some circumstances, including where the obtaining of UK tax deductions is a main purpose of the borrower in being party to the loan.

Whilst, at the inception of the loan relationship rules, reassurance had been given that the unallowable purpose rule would only be invoked to counter especially aggressive taxpayer positions, in recent years it has become clear that HMRC’s appetite for arguing that a particular taxpayer has an unallowable purpose has significantly increased. This, coupled with the success of HMRC in litigation on this point, initially resulted in significant taxpayer uncertainty around the precise scope of the rule and the circumstances in which it would be invoked, especially in the context of acquisition funding.

However, some clarity emerged in May 2023, when HMRC issued new guidance providing valuable insight into its current thinking on the circumstances in which the unallowable purpose rule should, or should not, apply. The guidance is relatively comprehensive and contains fairly extensive examples of hypothetical factual scenarios and HMRC’s view of whether the unallowable purpose rule would apply to each. In some cases these examples are reminiscent of factual scenarios from recent case law.

A greater degree of clarity as to HMRC’s practice in relation to particular scenarios is welcome. However, residual uncertainty remains, in particular, in relation to fact patterns not directly addressed by the guidance.

The timing of publication of HMRC’s guidance seemed perhaps surprising, given that there were several prominent cases on unallowable purpose in the process of being litigated at the time, leading to much speculation as to whether HMRC’s guidance might be rapidly superseded. (At the time of publication of the guidance, two of the cases referred to below were

about to be heard by the Court of Appeal and the third had been heard by the Upper Tribunal (“**UT**”), but the judgment had not yet been published.)

Fast forward to now, when HMRC has recently secured three important Court of Appeal victories and it seems clear that HMRC currently has the upper hand in the development of the unallowable purpose rule. This is therefore an appropriate moment to reflect upon the current scope of the rule, in light of the three Court of Appeal judgments discussed below.

Blackrock Holdco 5, LLC v HMRC ([2024] EWCA Civ 330)

This case involved a financing structure for the acquisition of a target, undertaking a US business, by a US-headed group.

The aim of the acquisition structure, from a tax perspective, was to create a UK tax deduction for the interest on the funding, available for surrender to UK members of the taxpayer group, with no corresponding taxable interest receivable.

Importantly (and this had been thought to be a potentially key point of distinction from the other case on acquisition financing, discussed below) the UK Newco which claimed the deductions was not the entity which made the acquisition. A US entity in which UK Newco owned preference shares made the acquisition, this feature of the transaction being determined by regulatory considerations.

The Court of Appeal concluded that the UK Newco’s place in the structure was entirely driven by tax considerations. The sole reason for its existence was to obtain tax advantages for the group. It therefore had a main purpose of securing a tax advantage. However, it also had a commercial main purpose, because it was anticipated that it would not only meet its obligations under its loans but also make a profit. However, the Court concluded that, “On the facts there is no

principled basis to identify any particular amount or proportion of the debits as being attributable to the commercial purpose". Accordingly, the Court concluded that all of the debits should be attributed to the main purpose of securing a tax advantage and therefore be disallowed.

JTI Acquisition Company (2011) Limited v HMRC ([2024] EWCA Civ 652)

This is the most recently decided case of the three discussed in this article. It again related to the acquisition of a US company by a US-headed group. The tax structuring aimed to achieve the result that interest payable gave rise to UK interest deductions which could be surrendered to UK group companies, with no corresponding taxable interest receivable.

In this case, the UK newco incurring the interest debits in respect of which deductions were claimed was the entity making the acquisition. For this reason, it had been hoped that this case might be likely to give rise to an attribution of debits to a commercial purpose, leading to a proportion of the interest debits being deductible on the basis that the UK Newco's purpose in being party to the loan relationship was to part-fund the acquisition.

However, the Court declined to interfere with the conclusion of the First Tier Tribunal ("**FTT**") that, although there was a bona fide commercial reason to acquire the target that did not mean that making UK newco the purchaser, and its assumption of debt, had a commercial purpose. Accordingly, no apportionment of debts to a commercial purpose was found to be appropriate and the entirety of the debits fell to be disallowed.

Kwik-Fit Group Limited (and others) v HMRC ([2024] EWCA Civ 434)

The facts of this case relate not to acquisition financing but, instead, to a reorganisation of intra-group debt undertaken in 2013.

A number of intra-group debts owed by the appellants were assigned to an intermediate holding company ("**Speedy 1**") within the Kwik-Fit group. Certain additional receivables were created in Speedy 1's favour. The interest rates on the amounts owed to Speedy 1 were also increased.

Speedy 1 had existing tax reliefs of around £48m, in the form of non-trading loan relationship deficits, brought forward from earlier periods.

The anticipated result was that the non-trading deficits would offset Speedy 1's interest income (significantly accelerating their use, from an anticipated 25 years to under 3 years). The interest cost of the appellants would generate tax relief for their use or be surrendered as group relief.

The Court of Appeal noted that the real benefit, the one that would make the group better off as against HMRC, was not the receipt of interest income in Speedy 1 (viewed in isolation), but the generation of interest deductions in the Appellant entities.

The Court noted that the existing loans of Speedy 1 had a commercial purpose and interest was charged at an arm's length rate and that, "In most circumstances of that kind there would be no question of the unallowable purpose rule applying". However specific factual features were present. The Appellants agreed to take on the obligation to pay significant additional interest, without any non-tax reason for doing so. The increase in interest rate was to maximise the savings available, whilst avoiding any risk that it was excessive. The new loans were found not to have their own commercial purpose, instead the Court concluded that the intended tax advantages were the main purpose.

Section 442(5) of the CTA 2009 provides that references to a tax avoidance purpose "are references to any purpose which consists of securing a tax advantage for the company or any other person". Here, the aim was to benefit "the whole group". The Court concluded that this was sufficient for the legislation to apply.

On apportionment, the Court said that the appellants had no commercial purpose in entering into the new loans and therefore the FTT was fully entitled to treat all of the debits on those loans as attributable to the unallowable purpose. It was also held that the FTT had been entitled to attribute all of the debits arising from the increase in rates on the pre-existing loans to the unallowable purpose. However, HMRC accepted that, once Speedy 1's losses were used up, it would no longer be just and reasonable to deny relief for the debits. Therefore, only to that extent, the availability of deductions was preserved.

Conclusion

It is now abundantly clear that the unallowable purpose rule has far wider application than had, for a significant period of time, been understood. HMRC is likely to derive much ammunition from these cases.

Whilst there was found to be a commercial purpose in both *Blackrock and Kwik-Fit*, only in the latter case was there a limited attribution of debits to that commercial purpose.

There is much emphasis in the judgments of the Court of Appeal in these cases on the specific facts and it is increasingly clear that how the facts are presented in the initial stages of litigation is critical. This further evidences the need to record and retain contemporaneous evidence of the commercial purposes underlying the relevant loans.

Other notable tax cases

HMRC v Hotel La Tour Ltd [2024] EWCA Civ 564

The Court of Appeal allowed HMRC's appeal in this case which related to the recovery of input tax in relation to services which were used in, and had a direct and immediate link with, the supply of shares.

The issue was whether the taxpayer, Hotel La Tour Ltd, could deduct input tax incurred in connection with a sale of shares in its subsidiary Hotel La Tour Birmingham Ltd. The taxpayer had decided to develop a new hotel in Milton Keynes and to sell its subsidiary, whose business was mature, in order to fund the new development. The taxpayer engaged various third parties to assist with the sale of the subsidiary by performing various services, including market research, buyer shortlisting, financial modelling and tax compliance. The aim was to maximise the proceeds of the share sale, in order to fund the development.

The taxpayer sought recovery of the VAT on the basis that the purposes of the disposal was to fund its wider business, which included making taxable supplies. This approach was challenged by HMRC, but the taxpayer succeeded before the FTT and the UT. This had given rise to a degree of hope that, where a taxpayer was fundraising in order to fund taxable business activity, VAT in relation to share sales may be recoverable.

However, HMRC appealed to the Court of Appeal and succeeded. The Court said that where the input tax has a direct and immediate link with an exempt transaction, VAT cannot be recovered. It concluded that, in this case, the input tax incurred in relation to services which had a direct and immediate link with the share disposal.

HMRC v Altrad Services Ltd & Anor [2024] EWCA Civ 720

The Court of Appeal allowed HMRC's appeal from the UT in this case concerning structured finance leasing arrangements. The Court applied the Ramsay principle, determining that the sale of assets to a bank by the taxpayers, as part of a sequence of arrangements, did not constitute a "disposal event" under section 61(1)(a) of the Capital Allowances Act 2001 ("**CAA 2001**") because the taxpayers did not "cease to own" the plant or machinery involved, as required by the relevant statute.

The taxpayers had claimed capital allowances for expenditure on certain qualifying assets and sought to create additional qualifying expenditure through further arrangements, without incurring real financial costs or affecting their existing allowances. This involved selling assets to the bank in return for long-funding leases and cross-options, aiming to trigger a cessation of ownership under section 61(1)(a) (and so qualify for the additional deduction) and engage the funding lease rules of the capital allowances framework.

The Court of Appeal criticised the arrangements for attempting to "subvert the basic scheme of the legislation", by generating fresh allowances without real cost, beyond scheme fees and implementation expense, and said that such use of the capital allowances regime was unlikely to have been Parliament's intention.

The decision focused on whether the taxpayers, in a practical sense, ceased to own the assets upon sale to the bank. In line with the Ramsay approach, the Court looked at the effect of the scheme in its entirety and concluded that the taxpayers retained ownership of the assets throughout, commenting that the scheme's sole purpose was tax avoidance without commercial substance. The Court agreed that the individual transactions entered into were legally effective, but that Supreme Court precedent indicated that a purposive approach pursuant to the *Ramsay* principle can still apply to a series of transactions, even if each step is legally effective on its own.

Centrica Overseas Holdings Ltd v HMRC [2024] UKSC 25

The Supreme Court has unanimously dismissed the taxpayer's appeal in this case on the deductibility of "expenses of management". The Court found that the taxpayer's (an intermediate holding company's) expenditure on professional advisory services relating to the sale of a subsidiary was capital in nature and was therefore not tax deductible as expenses of management. The Court of Appeal had held that the professional fees in question were "expenses of management", and there was no appeal from that decision.

Section 1219 of the CTA 2009 allows a deduction for "expenses of management of the company's investment business", but not where these relate to expenses of a "capital nature".

The taxpayer had argued for a narrower interpretation of "expenses of a capital nature", suggesting that it should exclude only acquisition costs of an investment business and certain fixed capital expenses (such as the acquisition costs of a building from which the investment business is conducted). However, the Court found that the "well-established principles" in case law which distinguish between capital and revenue expenditure in the context of trading companies apply equally to expenses of management, and that the phrase had the same meaning as "items of a capital nature" in section 53(1) of the CTA 2009 (which excludes the deduction of such expenditure in relation to trading companies).

The Court emphasised the heavily fact-dependent nature of determining whether particular expenditure is revenue or capital, and that, whilst there is no single test or criterion which is decisive, a good starting point is the objective reason for the expenditure.

In this case, the Court found that there was no difficulty in deciding which side of the capital/revenue divide the expenditure fell, holding that the investments of a holding company are clearly capital assets and so the expenditure in disposing of those assets is "of a capital nature" and so not deductible as expenses of management.

HMRC v GE Financial Investments [2024] EWCA Civ 797

The Court of Appeal has allowed HMRC's appeal, concluding that a company whose shares were stapled to those of a US company was not entitled to double tax relief under the US / UK double tax treaty ("**DTT**").

GE Financial Investments ("**GEFI UK**") was part of a US headed group and had its shares "stapled" to those of a US subsidiary, GEFI Inc ("**GEFI US**"). The effect of the stapling for US domestic tax purposes was that GEFI UK was subject to US tax on its worldwide income. Additionally, GEFI UK was the limited partner of a Delaware limited partnership (the "**Delaware LP**"), holding a 99% share, with GEFI US, as general partner, holding the GP's usual 1% share. The Delaware LP held loans with other US entities in the group and received interest income from them. GEFI UK paid both US and UK tax on the interest income and claimed double tax relief under the DTT.

The issues before the Court were (1) whether the share staple between GEFI UK and GEFI US had the effect that GEFI UK was a resident of the US for the purposes of the DTT and, if not, (2) whether GEFI UK carried on business in the US through a permanent establishment (by being the limited partner of the Delaware LP).

On (1), the Court held that GEFI UK was not a resident of the US for the purposes of the DTT, agreeing with HMRC that Article 4(1) of the DTT required both liability to worldwide taxation and one of the listed connecting factors to the state concerned (or a factor of a similar nature to those listed). The fact that the share stapling arrangement made GEFI UK liable to US tax on its worldwide income did not amount to a criterion of a similar nature to those listed in Article 4(1), such as domicile, residence, place of management or place of incorporation.

As regards issue (2), the Court also held that GEFI UK was not "carrying on business" in the US through a permanent establishment for the purposes of Articles 11(3) (Interest) and 7 (Business Profits) of the DTT, because the Delaware LP's activities were passive, sporadic and isolated and it was acting merely as a passive holding vehicle for some loan receivables.

HMRC v HFFX LLP [2024] EWCA Civ 813

The Court of Appeal has allowed HMRC's appeal in this case relating to the taxation of incentivisation arrangements. GSA, an investment management business, moved its high frequency trading team to a limited liability partnership (HFFX LLP). The members of that team became partners, rather than employees, and they were seconded by HFFX LLP back to the primary trading entity.

Half of what would have been the individual members' payout was allocated to GSAM, a corporate member of HFFX LLP, which invested the amount in GSAM-managed funds. At intervals, GSAM sold tranches of those investments and contributed the net proceeds back to HFFX LLP as "Special Capital". GSAM then allocated the Special Capital to individual members, who were able to withdraw it.

HMRC succeeded in arguing that the allocations of Special Capital by GSAM were taxable as miscellaneous income under section 687 of the Income Tax (Trading and Other Income) Act 2005. The Court found that the decisions taken by GSAM in favour of the individual members in relation to the allocation of Special Capital, in combination with their rights under the partnership deed were capable of amounting to "a source" from which the receipt of the Special Capital was derived. As such, the allocation of the Special Capital was subject to income tax.

Peter Marano v HMRC [2024] EWCA Civ 876

The Court of Appeal has allowed HMRC's appeal, concluding that section 103 of the Finance Act 2020 ("**FA 2020**") removes the requirement for HMRC to prove that an officer of the Board has been involved in giving certain notices to a taxpayer. That section states that HMRC may do "anything capable of being done by an officer of Revenue and Customs". This includes the giving of notice requiring submission of a tax return pursuant to section 8 of the Taxes Management Act 1970 and issuing penalty notices pursuant to Schedule 55 to the Finance Act 2009 (the provisions in question in this case).

The taxpayer had argued for a narrower construction of section 103 of the FA 2020, with the effect that it merely allowed HMRC to entrust to some other officer responsibility for completing the assessment procedure after the Board or an inspector or other officer of the Board had taken the decision to make an assessment. The Court, agreeing with the UT, held that the section was intended to put beyond doubt that acts carried out by HMRC by the use of automated functions are valid without the need, on each occasion, to prove the direct involvement of an officer.

Interesting decisions from the tribunals

FTT allows the taxpayer's anonymity application on the ground of serious risk to mental health

In *L v HMRC* [2024] UKFTT 00401 (TC), the FTT allowed the taxpayer's application for anonymity in respect of her substantive tax appeal on the basis of serious risk to health, particularly mental health, and as a "convenient" means of ensuring sensitive information in an employment settlement agreement remained confidential.

Background

The taxpayer made an application to the FTT for the hearing of her substantive appeal to be in private and for the substantive decision to be anonymised, so as not to enable the identification of the taxpayer. The application for a private hearing and anonymity, on which HMRC was neutral, was made on two grounds.

First, that the taxpayer would suffer a serious risk to health, in particular mental health, should the application not be granted, given her individual circumstances.

Secondly that she would be at risk of serious financial harm should the application not be granted, on the basis that a public hearing of her substantive appeal would impact the prospects of her retaining her current employment under a temporary contract and her future career prospects. The taxpayer was pursuing an alternative career path following her previous employment in the financial services sector which had ended, pursuant to a settlement agreement, following a claim for discrimination.

Decision

Rule 32 of The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 provides that hearings must be in public, subject to the FTT's power to allow a hearing to be held in private where it meets at least one of five specified grounds listed therein.

The FTT allowed the taxpayer's application and concluded as follows. There was a serious and objective risk of harm to health and possibly even life if the application was refused, given the nature of the taxpayer's condition and the circumstances that trigger it. The FTT, citing *Michael Adebolajo v Ministry of Justice* [2017] EWHC 3568, noted that even a subjective fear of serious physical harm that was real to the taxpayer would have been sufficient to justify anonymity. This risk "weigh[ed] heavily" into two of the specified grounds: protection of a person's right to respect for their private and family life, and prejudice to the interests of justice.

The FTT, having allowed the taxpayer's appeal on the ground of serious risk of harm to health, did not need to decide the second ground of serious financial harm. However, it noted that it would have required "more evidence as to the objective reasonableness of the unquestionable subjective fear of the commercial risk", simultaneously acknowledging the challenges of obtaining such direct evidence, and that because tax cases frequently deal with significant sums in dispute (either in absolute or relative terms), allowing anonymity "on the basis of a fear of commercial consequences based on circumstantial assertion is significantly more challenging".

The FTT referred to the settlement agreement, saying that it was "reasonable to expect" that it contains a confidentiality clause and a clause in which the former employee made the settlement without admission of liability. The former employer would not be a party to the tax appeal and therefore there was an acknowledged need to keep critical details of the settlement agreement confidential. Anonymising the hearing and the judgment provided a convenient means of doing so.

Comment

As demonstrated by the authorities cited by the FTT, the majority of anonymity applications in relation to tax appeals have historically been refused, and the "courts and tribunals have tended to adopt a reasonably hard line on the question of anonymity".

Therefore, this decision is unusual, and seems to be decided largely on the basis of the individual health circumstances of the taxpayer. Nevertheless, it could have wider implications, particularly in relation to confidential settlement agreements.

FTT dismisses the taxpayer's appeal regarding capital allowances treatment on a hive-down of an oil and gas pipeline to a wholly owned subsidiary, where the activity was within the ring fence trade before the transfer but partly outside afterwards

In CATS North Sea Limited v HMRC [2024] UKFTT 00512 (TC), the FTT considered the interaction of the oil tax ring fence trade provisions and the capital allowances code. It held, dismissing the taxpayer's appeal, that the transfer of trade provisions applied to the hive-down of an interest in the CATS Pipeline from Amoco (UK) Exploration Company LLC ("**Amoco**") to its wholly owned subsidiary, the taxpayer (CATS North Sea Limited, "**CNSL**"). However, following the transfer, one of the activities the taxpayer was carrying out was outside the oil and gas statutory 'ring fence' ("**ORF**"), such that a disposal and balancing charge arose.

Background

Before the hive-down, Amoco, a member of the BP plc group, owned a 36.2% interest in the CATS Pipeline. Its activities involved the transportation of hydrocarbons extracted by the BP group and non-BP group companies from the CATS Pipeline user fields and the receipt of tariffs as consideration for that transportation. Amoco filed its company tax returns on the basis that the activities in respect of the CATS Pipeline were oil-related activities which formed part of its trade inside the statutory ring fence ("**IRF**") applying to oil and gas activities.

Immediately following the hive down of Amoco's interest in the CATS Pipeline to the taxpayer, only the transportation of BP group hydrocarbons was IRF. The transportation of non-BP group hydrocarbons was ORF, as these were not associated companies of the taxpayer, nor was the taxpayer a participator in the Everest oil field.

Subsequently, Amoco sold the entire issued share capital of the taxpayer to a third-party ultimately controlled by Antin Infrastructure Partners Luxembourg II SARL

("Antin") for approximately US\$388m. Following the share sale, all CATS Pipeline activities carried out by the taxpayer were entirely ORF, as BP group companies were no longer associated companies of the taxpayer and there were no Antin group companies transporting hydrocarbons through the CATS Pipeline.

Decision

The FTT held that there was a transfer of a trade without a change of ownership (within Part 22 of the Corporation Tax Act 2010 ("CTA 2010")) in respect of the hive-down. Amoco had transferred part of its IRF trade to the taxpayer (its wholly-owned subsidiary) which, by virtue of section 279 of the CTA 2010, was deemed to be carrying on two trades upon the hive down – an IRF trade and an ORF trade. This was on the basis that the activities carried on by Amoco before the transfer and the taxpayer after the transfer were the same, and it was irrelevant that as a matter of the corporation tax rules relating to oil and gas, Amoco had been carrying out an entirely IRF trade before the hive-down, whereas following the hive-down the taxpayer was not. The FTT noted that the transfer of trade provisions consider the substance of the activities in question, rather than their classification for tax purposes.

Having determined that the transfer of trade provisions applied, the FTT turned its attention to consider the capital allowances consequences of the hive-down and subsequent share sale. It held that the carrying out of activities partly ORF by the taxpayer triggered a disposal event under s61(1)(e) of the CAA 2001 because, while Amoco had transferred an entirely IRF trade to the taxpayer, the taxpayer was in fact carrying out both an IRF trade and an ORF trade, which are considered separate qualifying activities under section 162 of the CAA 2001. This resulted in a balancing charge for the taxpayer of approximately £169m based on a tax written down value of -£2m and a market value of plant and machinery (capped at Amoco's historic cost) of £167m.

Further, it was held that the effect of the election made by Amoco under s231(1) of the Finance Act 1994 in relation to the CATS Pipeline was restricted to petroleum revenue tax, and so had no applicability to issues of corporation tax and/or ring fence trades.

Comment

This decision is of interest not only to oil and gas companies that may be considering a hive-down (a common feature of corporate acquisitions for upstream and associated assets in recent years), but provides useful discussion on the application of a purposive approach to statutory construction which is of wider interest.

FTT allows taxpayers' appeal against closure notice, taking a "common sense" view as to the interpretation of finance agreements entered into by the taxpayers

In Mahadevan Krishnamohan & Anor v HMRC [2024] UKFTT 00346 (TC), the FTT allowed the taxpayers' appeal against a closure notice, which closed an enquiry into the taxpayers' self-assessments for the year 2014/15 and brought into charge approximately £336,000 in additional tax for each of the two taxpayers. The crux of the appeal related to terms for the provision of finance for a property acquisition made by the appellants and particularly whether the transactions were the grant of an option and therefore part-disposals chargeable to capital gains tax under section 144 of the Taxation of Capital Gains Act 1992 ("**TCGA 1992**").

Background

The appellants were introduced to a property called Cliveden Stud Farm, a substantial property with an asking price of £5.8m. On 18 November 2013, the appellants entered into an agreement, entitled "Option Agreement", with Sheen Development Limited ("**Sheen**") (the "**First Sheen Agreement**") to secure £600,000, to pay for the deposit required to exchange contracts on Cliveden Stud Farm. The First Sheen Agreement provided Sheen the option to buy the freehold and/or leasehold interest of three properties owned by the appellants, exercisable by Sheen at any time after the option period (initially 12 months, but subsequently extended) elapsed. If the taxpayers repaid the deposit plus an additional fee, the option agreement would terminate.

The subject of the appeal relates to this First Sheen Agreement but the FTT's rationale applies to all subsequent agreements the appellants entered into as these contained similar terms.

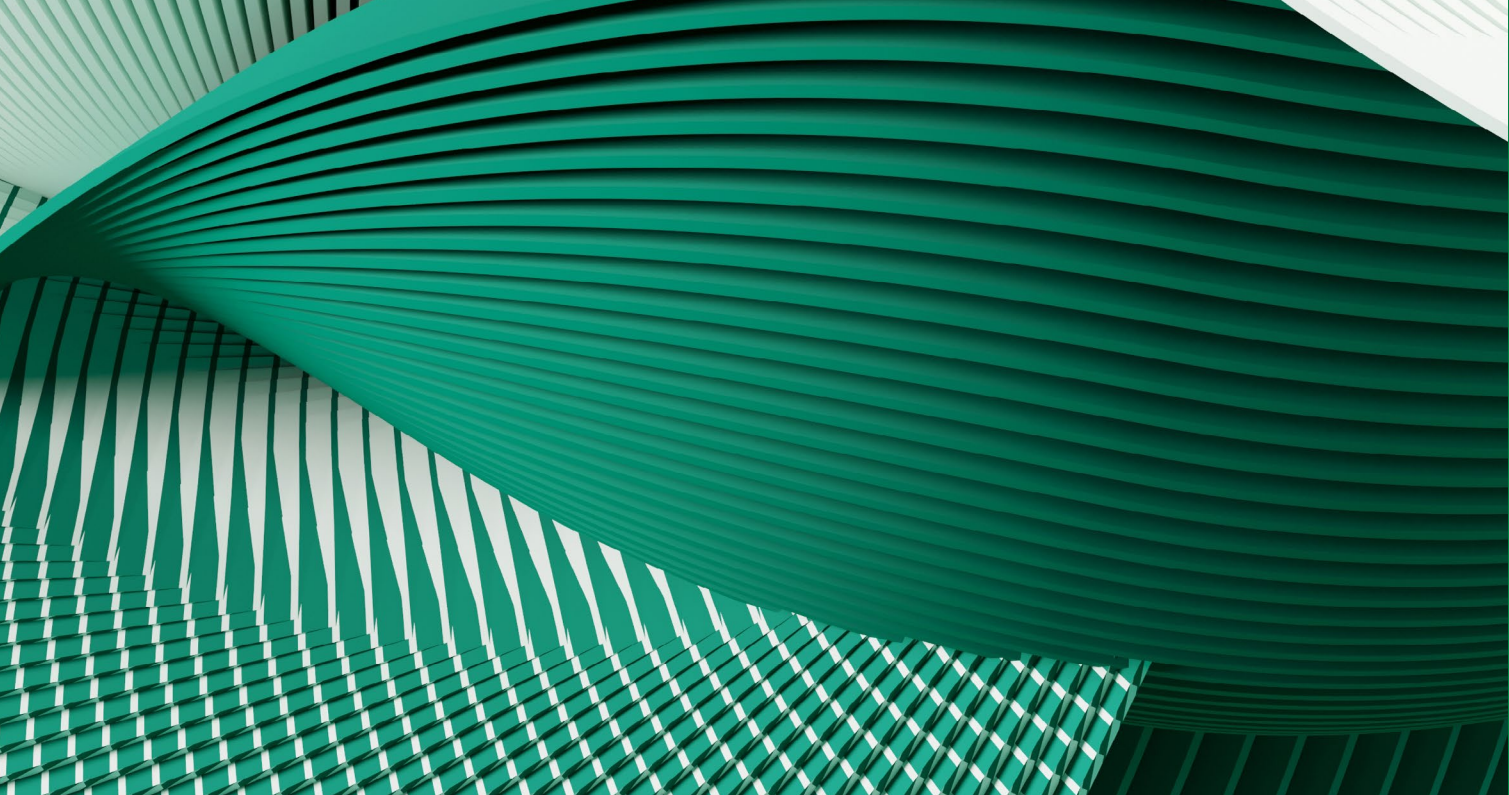
Decision

The appellants focussed on the revocable nature of what they had granted to Sheen under the First Sheen Agreement, noting that what they had granted to Sheen was not a binding option until the time for exercise arose. The appellants argued that if the grantor could revoke the grant at will and could do so before the time came for it to be exercised, then there was never any moment in time when the grantee was in a position to exercise the option (as explained in *Gardner v Blaxhill* [1960] 2 All ER 457). Sheen had to wait until the option period had elapsed before it could choose whether to give notice to exercise the option.

In response, HMRC argued that an option had been granted to Sheen under the First Sheen Agreement, albeit the option was revocable at will by the appellants. The appellants had essentially bound themselves and would need to take action to unbind themselves. Furthermore, HMRC contested that it was not uncommon for option agreements to have clauses or conditions preventing the option from being exercised immediately and that such a clause did not prevent an agreement from being the grant of an option.

The FTT concluded that while HMRC was able to direct it to examples of where the right to exercise an option became available only after a specified event, HMRC had not been able to identify any authority where the courts or tribunals had concluded that an option had been granted despite the relevant agreement providing that what had been granted could be removed at will by the grantor before it could ever be exercised by the grantee.

The FTT decided that the First Sheen Agreement, despite being titled an option agreement, was an agreement by the appellants that if they did not pay £600,000 plus a further £108,000 (equal to 18% interest pursuant to the terms of the agreement) to Sheen within 12 months of the date of entering into the agreement, then Sheen would have the right – "at that stage and, critically, only at that stage" – to decide whether it wanted to buy the three properties secured under the agreement. It is clear on the facts of this case that the agreement was such that the appellants would grant an option to Sheen in a year's time if, and only if, certain defined circumstances came to pass. Those circumstances were within the control of the appellants



and they did not come to pass in this case. As such, the appellants did not enter into an irrevocable disposition and were able to avoid selling the properties secured under the First Sheen Agreement by paying the agreed amount to Sheen within the contractual timescale.

Comment

The FTT agreed with HMRC that an option does not need to be immediately exercisable. However, where the grant is dependent on a subsequent event, it is relevant to look at whether the grantor can control the events which must occur for the grantee to have the relevant choice.

It is clear that the FTT will take a purposive approach in its analysis of transactions, looking at their substance and the contractual nexus to determine their nature.

FTT holds that share buybacks, intended to bank EIS relief by crystallising gains, were transactions in securities with a main purpose of obtaining an income tax advantage

In Hugh Edward Mark Osmond & Anor v HMRC [2024] UKFTT 00378 (TC), the FTT considered whether the main purpose or one of the main purposes of the appellants being party to the share buybacks was to obtain an income tax advantage, as defined in section 687 of the Income Tax Act 2007 ("**ITA 2007**"). The FTT concluded that the appellants had a main purpose of obtaining Enterprise Investment Scheme ("**EIS**") relief. This meant that they would pay income tax of zero (as the consideration was allegedly subject to capital gains tax ("**CGT**"). Since this is less than the income tax which would have arisen on a payment of the consideration as a qualifying distribution, an income tax advantage arose.

Background

This case relates to share buybacks by Xercise2 Limited (the "**Company**"). The appellants, Hugh Osmond and Matthew Allen, disclosed these buybacks on their self-assessment returns for the year ending 5 April 2015. They filed these returns on the basis that the consideration for the share buybacks represented a return of capital and was therefore subject to the CGT regime. However they argued that the disposal benefited from EIS disposal relief, pursuant to section 150A of the TCGA 1992, meaning there was no CGT payable. HMRC took the contrary view, arguing that the Transactions in Securities ("**TIS**") regime (pursuant to Part 13 Chapter 1 of the ITA 2007) applied, with the result that the consideration was subject to income tax and not CGT. HMRC issued counteraction notices and assessments accordingly.

HMRC argued that it is wrong to consider EIS relief solely as a CGT relief. This is because the term "income tax advantage" is the subject of a specific statutory definition (contained in section 687 of the ITA 2007);

- "(1) ... a person obtains an income tax advantage if—
- (a) the amount of any income tax which would be payable by the person in respect of the relevant consideration if it constituted a distribution exceeds the amount of any capital gains tax payable in respect of it, or
 - (b) income tax would be payable by the person in respect of the relevant consideration if it constituted a distribution and no capital gains tax is payable in respect of it."

Based on that definition, and the appellants' admitted purpose that the share buyback was to secure the benefit of EIS disposal relief, HMRC argued that the appellants as a matter of law had a main purpose of obtaining an income tax advantage in entering into the share buybacks.

The appellants argued that the sole purpose of the share buyback was to bank EIS disposal relief, so as to ensure it was not lost as a result of a change in legislation. The appellants did not aim to extract value from the company, and if they could have secured the relief without undertaking a transaction they would have done so. The appellants accepted they obtained an income tax advantage as a result of the transactions, however, they argued this was not their main purpose; rather, it was an unintended consequence of their primary aim to secure EIS disposal relief, and as such should be disregarded.

Decision

The FTT found that the share buybacks had a main purpose of obtaining an income tax advantage. It found as a fact that a main purpose of the parties for the share buybacks was to enable the appellants to crystallise the EIS disposal relief which they had "preserved and nurtured for many years".

The FTT therefore said that it followed "as a matter of remorseless statutory logic" that a main purpose was also to obtain an income tax advantage, as that phrase is defined. The amount of income tax which would have

been paid had the consideration been paid by way of a qualifying distribution was always going to exceed the CGT payable on the consideration in light of the benefit of EIS disposal relief.

It rejected the appellants' argument that for there to be a "main purpose" of obtaining an income tax advantage which would have generated the higher income tax charge there needs to be a consciously considered comparable transaction, as the "alternative" transaction (being a qualifying distribution) is built into the definition of income tax advantage. The FTT accepted that the appellants did not wish to extract funds from the Company.

The FTT commented that the TIS regime "deliberately casts its net very widely" and concluded that this result did not give rise to injustice or absurdity.

The FTT held that the consideration the taxpayers received was within the TIS definition of "relevant consideration". It further concluded that although the counteraction notices issued by HMRC omitted relevant information, they were nevertheless valid.

Comment

The FTT's decision confirms that even if, factually, obtaining an income tax advantage was not a main purpose of undertaking a transaction, the legal position may be different, in light of specific statutory drafting. In the current environment, taxpayers may have similar issues regarding an intention to secure existing reliefs, in light of perceived change of law risk. In such cases any relevant statutory main purpose tests will clearly merit careful consideration.

UT dismisses HMRC's appeal in a case concerning the application of Article 12(5) of the Ireland / UK DTT to the assignment of a debt claim

In HMRC v Burlington Loan Management DAC [2024] UKUT 00152 (TCC), the UT found in favour of the FTT's decision that the Ireland / UK DTT was merely the backdrop against which the transaction took place and that the anti-abuse provision at Article 12(5) of the DTT did not apply.

Background

The case involved the secondary market in claims against Lehman Brothers International (Europe), a UK company. One such claim was sold by SAAD Investments Company Limited ("**SICL**"), a company resident in the Cayman Islands, to a broker, and then by the broker to an Irish resident company, Burlington Loan Management DAC ("**BLM**"). Both SICL and BLM knew that SICL would suffer 20% UK withholding tax on interest payments made directly to it, while BLM would not because of the Ireland / UK DTT. The pricing for the transactions effectively split the benefit of the gross payment. There was no mechanism to adjust the price if BLM in fact suffered UK withholding tax on the interest. HMRC submitted that the case should fall within the anti-abuse provision of the DTT (Article 12(5)) because SICL was taking advantage of the DTT by selling to BLM for a greater sum than it could have realised itself.

Decision

The UT agreed with the FTT that the question of whether a person had a main purpose of taking advantage of Article 12(1) by means of the creation or assignment of a debt claim was a question of fact that required a consideration of all of the relevant evidence and the proper inferences to be drawn from it. The UT also accepted that Article 12(5) was concerned with the subjective purposes of the persons concerned, and that these purposes could be conscious or subconscious, but the mere fact that the assignment had certain inevitable and inextricable consequences did not of itself mean that achieving those consequences was the purpose or a main purpose of that assignment.

The UT rejected HMRC's argument that Article 12(5) should be interpreted as requiring only that the person concerned knew that the purchaser of the debt claim was exempt from UK withholding tax and that it was a main purpose of the person to benefit from that exemption, regardless of whether the person knew the specific basis of the exemption or whether the exemption was attributable to the DTT. The UT held that such an interpretation was inconsistent with the text and the purpose of Article 12(5), which was aimed at

preventing the abuse of the DTT not the avoidance of UK withholding tax. The UT also held that the question of whether there was an abuse of the DTT had to be answered by reference to both contracting states, and that it was not a proper starting point to assume that interest on the debt claim should be subject to UK withholding tax in the absence of the DTT.

The UT upheld the factual findings of the FTT that neither the seller nor the purchaser of the debt claim had a main purpose of taking advantage of Article 12(1) by means of the assignment. The UT found that the FTT was entitled to take into account the fact that there was a market for the debt claim in which UK withholding tax was not an issue for potential purchasers for a variety of reasons, and that the seller and the purchaser were transacting at arm's length with a view to getting the best price. The UT also found that the FTT was entitled to conclude that the purchaser's ability to rely on Article 12(1) was merely part of the setting in which the assignment took place, and that the purchaser was not seeking to abuse the DTT but to expect that the DTT would apply to it in the normal way as an Irish resident company that beneficially owned the interest. Further, the UT found that the FTT was entitled to conclude that the seller's only purpose in entering into the transaction was to sell the debt claim for the best available price, and that it did not care about or seek to take advantage of the DTT, which it did not know about until after the commercial terms were agreed.

Comment

This case is an important reminder of the role of treaty anti-avoidance provisions. Whilst in some cases this judgment will provide reassurance to financial market participants in transactions involving an element of withholding tax arbitrage, it is worth noting that the UT stated that in some circumstances Article 12(5) may apply even where there is no artificiality.

UT dismisses HMRC's application for a penalty pursuant to paragraph 50 of Schedule 36 to the Finance Act 2008

In Paul Baxendale-Walker v HMRC [2024] UKUT 00154 (TCC), the UT found in favour of the taxpayer, striking out HMRC's penalty application under paragraph 50 of Schedule 36 to the Finance Act 2008 ("**FA 2008**") on the basis that the statutory pre-conditions for imposing such a penalty were not satisfied.

Background

The UT recently considered an application by Paul Baxendale-Walker ("**PBW**") to strike out an application by HMRC for a tax-related penalty of £14m under paragraph 50 of Schedule 36 to the FA 2008. The penalty was sought by HMRC on the basis that PBW had failed to comply with an information notice that required him to provide information or documents for checking his tax position. PBW could not appeal the information notice itself (it had been approved by the FTT, so there was no right of appeal) but he appealed against the penalty. The UT allowed PBW's strike out application, finding that HMRC's application for a penalty had no reasonable prospect of success because the statutory pre-conditions for imposing such a penalty were not satisfied.

Decision

The UT applied the approach to strike out applications under Rule 8(3)(c) of The Tribunal Procedure (Upper Tribunal) Rules 2008, which is to follow the approach for summary judgment applications under Part 24 of the Civil Procedure Rules. This means that the UT must consider whether the applicant's case has a "realistic" (more than merely arguable) as opposed to a "fanciful" prospect of success, and if the issue is a short point of law or construction, the UT should decide it if it has all the evidence necessary and the parties have had an adequate opportunity to address it in argument.

The main issue in this case was the interpretation of paragraph 50(1)(a) of Schedule 36, which provides that a tax-related penalty can only be imposed where "a person becomes liable to a penalty under paragraph 39". Paragraph 39 provides that a person is liable to a penalty of £300 if they fail to comply with an information notice. PBW argued that he had not become liable to a penalty under paragraph 39 because he had appealed against the penalty imposed by HMRC on 15 March 2023, and that appeal was still pending. He relied on the UT's decision in *HMRC v Sukhdev Mattu* [2021] UKUT 0245 (TCC), where it was said that if there remains an outstanding appeal to the FTT in respect of a paragraph 39 penalty, then the person has not "become liable to a penalty".

HMRC argued that a person becomes liable to a penalty under paragraph 39 as soon as they fail to comply with an information notice, regardless of any subsequent appeal. HMRC relied on the distinction in Schedule 36 between becoming liable to a penalty, being assessed to a penalty and appealing against a penalty. HMRC also pointed out that the time limits for assessing a penalty under paragraph 39 or applying for a penalty under paragraph 50 are based on the date on which the person became liable to the penalty, not the date on which any appeal is determined.

The UT agreed with HMRC's interpretation of paragraph 50(1)(a) as a matter of ordinary statutory construction. It held that there was no need to give a different meaning to the phrase "becomes liable to a penalty" for the purposes of paragraph 50(1)(a) and (b) where a person has an extant appeal against a penalty assessment in order to avoid infringing the principle against doubtful penalisation or the person's rights under the European Convention on Human Rights. It noted that the necessary safeguard against doubtful penalisation was in paragraph 50(1)(e), which requires the UT to decide that it is appropriate to impose a penalty, taking into account any live challenge to the paragraph 39 penalty. It also distinguished the decision in *Sukhdev Mattu* [2021] UKUT 0245 (TCC), which did not determine the point in question and was based on the parties' agreement.

However, the UT found that HMRC's application for a penalty failed on another ground, which was that the paragraph 39 penalty imposed on 15 March 2023 was invalid, because it was assessed and notified before PBW had failed to comply with the information notice.

HMRC had purported to extend the deadline for compliance with the information notice from 15 March 2022 until 15 March 2023.

The UT considered two alternative scenarios: either HMRC had the power to extend the time for compliance with the information notice (as they claimed), or they did not (as PBW claimed). In either scenario, the UT concluded that one of the requirements of paragraph 50 was not met, and therefore the application for a penalty had no reasonable prospect of success.

In the first scenario, assuming that HMRC had power to extend the time for compliance with the information notice, then their purported assessment of the taxpayer on 15 March 2023 was invalid, because at the time of the assessment PBW had not yet failed to comply with the information notice.

In the second scenario, assuming that HMRC did not have the power to extend the time for compliance with the information notice, then the period in which they could apply for a paragraph 50 penalty expired on 15 March 2023, but they did not apply to the UT until 28 March 2023.

Comment

This case illustrates some important points about the operation of Schedule 36 and the penalty regime under it. It is perhaps disappointing that the UT did not, in its concluding remarks, set out a firm conclusion on the extent to which HMRC can vary an information notice, which is clearly an important issue for taxpayers and HMRC alike.

Other developments

New OECD Pillar Two administrative guidance and HMRC guidance

In June, the OECD released another tranche of administrative guidance for inclusion into the commentary to the Pillar Two Model Rules. The intention of the administrative guidance is to ensure consistent and common interpretation of the rules, provide certainty for groups within scope, and facilitate co-ordinated and transparent outcomes amongst implementing jurisdictions. As such, the guidance is intended to provide clarity on how the rules operate in relation to particular circumstances, where the outcome may not already be clear from the Model Rules or existing commentary. This fourth tranche of administrative guidance includes direction on:

- the application of the recapture rule applicable to deferred tax liabilities (“**DTL**”), including a simplified procedure which allows groups to aggregate various DTL categories in order to determine whether a DTL reverses within five years (and therefore does not need to be recaptured);
- the methodology for determining fixed tax assets and liabilities for Pillar Two purposes when the rules result in divergences between GloBE and accounting carrying value of assets and liabilities;
- the cross-border allocation of current and deferred taxes, allocation of profits and taxes on certain flow-through tax structures; and
- the treatment of securitisation vehicles.

Additionally, in July, HMRC released guidance reminding taxpayers that they should prepare to comply with Pillar Two in the UK. The guidance includes links to other previously published OECD and HMRC guidance, legislation and commentary, an update on the new online service for Pillar Two compliance, and relevant contact details for HMRC’s Pillar Two team.

Change in HMRC's guidance on salaried member rules

HMRC is understood to be scrutinising LLP's and their members' approach to the salaried members rules, and have recently changed their published guidance. The broad aim of the rules is to ensure that any member of an LLP who is, in reality, treated more like an employee than a partner is subject to the same tax treatment as an employee. The rules have regard, amongst other factors, to the level of the relevant individual member's capital contribution to the LLP.

The updated guidance in HMRC's Partnership Manual indicates that increases in capital contributions made solely to fall outside of the salaried member rules will be ineffective for that purpose. Additionally, a new example has been added (at PM259200) which makes it clear that HMRC's view is that the targeted anti-avoidance ("TAAR") rule applies where a capital contribution is increased pursuant to an arrangement that allows members to alter their contributions in each period in order to avoid meeting the relevant condition.

Previous guidance, that had said that a genuine contribution intended to be enduring and giving rise to real risk would not trigger the TAAR, has been removed (from PM259310).

Finance (No.2) Act 2024 receives Royal Assent

The Finance (No.2) Act 2024 received Royal Assent on 24 May 2024. The Act included a number of provisions announced by Rishi Sunak's government in the Spring Budget 2024, including: a reduction in the higher rate of CGT applicable to residential property; the abolition of multiple dwellings relief for SDLT; updates to certain creative reliefs and credits; the introduction of the Energy Security Investment Mechanism to the Energy Profits Levy; the power to make provision by regulation for a new UK-based unauthorised contractual scheme (the Reserved Investor Fund); and amendments to the transfer of asset abroad rules in the wake of the Supreme Court's judgment in *HMRC v Fisher No 2* [2023] UKSC 44.

HMRC publish tax gap statistics and analysis

HMRC have estimated that the tax gap for tax year 2022/2023 stands at 4.8%. The "tax gap" is the difference between the amount of tax that should be paid to HMRC and what is actually paid.

According to HMRC's report, the tax gap has reduced over time, from 7.4% in 2005/2006 to 4.8% in 2022/2023. The tax gap for each of VAT, income tax, national insurance contributions, CGT and excise duties has decreased since 2005/2006, but the corporation tax gap has increased by 2.5% in that same period, from

11.4% to 13.9%. The tax gap for small businesses is by far the largest component of the tax gap by taxpayer group (representing 60% of the overall tax gap), and the tax gap for wealthy taxpayers and individuals makes up a very low proportion (5% each).

New government's publication of draft legislation for inclusion in Finance Bill 2024-2025

On Monday 29 July, the new Chancellor of the Exchequer made a statement to the House of Commons, in which she announced that the Budget would be held on 30 October 2024. Immediately after this statement, HMRC published draft legislation for inclusion in the next Finance Bill, alongside explanatory notes, policy papers and technical consultations.

This included draft legislation for the abolition of the furnished holiday lettings tax regime (as announced at the Spring Budget 2024 by the previous government) and for implementing the transitional country-by-country reporting safe harbour anti-arbitrage rule into the UK's Pillar Two domestic tax legislation.

A technical consultation, draft legislation, and a business brief were also published in relation to the Labour party's manifesto commitment to end the VAT exemption for school fees. These documents confirm the government's intention for such fees to be subject to VAT at the standard rate of 20% from 1 January 2025, and for any fees paid from 29 July 2024 (the date of the publication) in relation to terms commencing on or after 1 January 2025 to be subject to VAT.

After the Chancellor's statement, HM Treasury released a number of publications relating to tax. These included policy papers on reforming the taxation of non-domiciled individuals, changes to the Energy Profits Levy and a call for evidence on the taxation of carried interest.

- In relation to non-domiciled individuals, the government intends to implement the four year "foreign income and gains" regime proposed by the previous government (with certain transitional reliefs made less beneficial) and a residence-based inheritance tax regime.
- The rate of the Energy Profits Levy will be increased to 38%, the levy will be extended to 31 March 2030 and certain beneficial investment allowances will be removed.
- The call for evidence on reform of carried interest invited stakeholder engagement, with the deadline for written submissions passing on 30 August.

HMRC release performance reports and customer survey outcomes

In July, HMRC released a number of reports and outcomes of customer surveys covering their performance in the last year, quarter and month. The annual report for 2023 to 2024 states that total tax revenues increased by 3.6% from the previous year to £843bn, with an estimated £41.8bn as a result of “tackling avoidance, evasion and error”. The reports reflect HMRC’s increasing emphasis on online self-service, noting that 83.1% of customers were satisfied or very satisfied with HMRC’s online services and 69% of customer interactions were via online self-service channels.

Customer survey responses were categorized by type of taxpayer. Large businesses were far more likely than most to positively score their interaction with HMRC during 2023, with 81% giving a positive score, in comparison to mid-sized businesses (53%), small businesses (70%), individuals (58%) and agents (37%). This possibly reflects the fact that the majority of large businesses have a CCM, with 93% of large businesses describing their interaction with their CCM as ‘good’ or ‘very good’.

Updated guidance on the publication of UT decisions

The President of the UT (Tax and Chancery Chamber) has published updated guidance on the publication of UT decisions. The main change in procedure is that where permission to appeal from the FTT to the UT has been refused by the UT following an oral renewal hearing, the UT will now publish the oral renewal permission to appeal decision. The guidance states this is for reasons of access to justice, and because generally HMRC will be aware of the wider body of permission to appeal decisions whereas private parties and their advisors will not.

HMRC contact financial services businesses in relation to VAT exemption

HMRC have sent letters to businesses in relation to the financial services VAT exemption. The letters note HMRC’s recent success in several cases on the exemption, and their concern that businesses are applying the exemption incorrectly, in particular in the following areas:

- fund accounting and administration services used by the recipient for both SIFs and non-SIFs;
- services treated as VAT exempt finance intermediary services, but that have been undertaken post-trade; and
- middle and back office functions

Recipients are invited to confirm whether they agree with HMRC’s position, and whether they have filed or will continue to file in line with HMRC’s approach. In addition, responses are requested to include the average amount of VAT impacted per annum.

HMRC decrease interest rates for late payment and repayment

In line with the Bank of England Monetary Policy Committee’s announcement on 1 August 2024 to decrease the Bank of England base rate from 5.25% to 5%, HMRC announced a reduction in interest rates for late payment and repayment. The changes came into effect on 12 August 2024 for quarterly instalment payments and 20 August 2024 for non-quarterly instalment payments. Late payment interest is set at base rate plus 2.5%, meaning that the interest rates from those dates will be reduced from 7.75% to 7.5%. Repayment interest is set at base rate minus 1% (with a minimum floor of 0.5%), meaning that the interest rates from those dates will be reduced from 4.25% to 4%.

Latest HMRC nudge letter campaigns

The behavioural science of “nudge theory” has become an increasingly used weapon in HMRC’s arsenal over the last decade or so – i.e. the idea that people can be better directed towards a desired course of action through suggestion rather than obligation. UK taxpayers may have noticed the same concept at work when completing their online tax returns, where certain information is now pre-populated based on figures held by HMRC (the idea being that the taxpayer will likely accept those figures by default).

Over the last few months, HMRC have launched several new nudge letter campaigns on various issues, as summarised below.

Business Asset Disposal Relief (“BADR”) lifetime limit (May 2024)

HMRC’s Wealthy team is writing to taxpayers who have included a BADR claim in their 2022/2023 self-assessment tax return and either had exceeded the BADR lifetime limit prior to that tax year, or exceeded it via the claim in that return. The letter reminds recipients of the lifetime limit of £1m. Recipients are required to amend their 2022/2023 self-assessment return within 30 days of the date of the letter and are made aware that it is likely additional tax will be due and that interest is due where tax has been paid late.

Electronic sales suppression (May 2024)

HMRC are sending letters to businesses which they suspect to be undertaking “electronic sales suppression”, the process of under-declaring sales via misuse of a till system. The letter directs recipients to disclose undeclared sales within 30 days of the date of the letter via the relevant page on the government website. The letter includes a warning that if HMRC do not agree with the details provided in the disclosure they may open a civil or criminal investigation, and if the recipient makes no disclosure at all HMRC may undertake a full business audit, open a civil or criminal investigation and / or send a tax assessment based on HMRC’s information, including interest and penalties.

Construction Industry Scheme (“CIS”) returns for insurance businesses (July 2024)

HMRC’s Large Business directorate is sending letters to insurance businesses that may commission construction work (either directly or through a loss adjuster) to make them aware of their CIS obligations. The letter sets out the conditions for a business to be a “deemed contractor”, when the obligation to register for the CIS arises, and what must be included on a CIS return. Recipients are required to determine whether they are a deemed contractor and, if so, to register for the CIS and start making deductions for contract payments within 90 days of the letter, as well as comply with the CIS on an ongoing basis. If the recipient takes no action, recipients are warned that HMRC may commence a compliance check and that any disclosure the recipient subsequently makes will be treated as “prompted” (with the relevant impact on penalties).

Persons with significant control (“PSCs”) (July 2024)

HMRC’s Wealthy team is sending nudge letters to PSCs. One tranche of letters is sent to PSCs to remind them to include all sources of income in their self-assessment tax return for 2023/2024, and to amend their return for 2022/2023 by 23 August 2024 should they have failed to do so in that return. The other tranche is sent to PSCs who have not filed self-assessment tax returns, reminding them to do so and to include all forms of income in that return.

Discrepancies in self-assessment tax returns (July 2024)

HMRC have commenced sending letters to tax agents, relating to potential self-assessment discrepancies in 2022-23 tax returns affecting multiple clients. The discrepancies alleged relate to differences between self-assessment tax returns for the tax year 2022/2023 and information that HMRC have received from the taxpayers’ employers via P14 and P11D forms and / or information that HMRC has in respect of the High Income Child Benefit Charge. HMRC will follow up with the agent in relation to the specific taxpayers and discrepancies in the coming weeks, and ask agents to

agree with relevant clients to make voluntary amendments to correct relevant returns by 31 January 2025. The letter notes HMRC will not charge penalties in relation to discrepancies which are amended in this way, but will charge statutory interest on any tax not paid on time.

CIS deductions from subcontractors’ payments (July 2024)

HMRC are sending letters to CIS contractors, to remind them to make the correct CIS deductions for payments made to subcontractors. Recipients are recommended to verify their subcontractors’ status, either via the free HMRC online service or, if more than 50 subcontractors need to be verified, via appropriate commercial software. The letters contain a warning that HMRC may start a compliance check, and if they discover any errors, any subsequent disclosure by the contractor would be treated as “prompted”, which would impact the amount of penalties payable.

Cryptoasset disposals (August 2024)

Letters are being sent to taxpayers whom HMRC believe have not properly declared their disposals of cryptoassets for tax purposes. The letters set out the various transactions that can constitute a cryptoasset “disposal”, and that CGT or income tax may be due, depending on the circumstances. Recipients are asked to rectify any failure to report by amending the relevant self-assessment returns if within time to do so, or, for previous years, to use HMRC’s online cryptoasset disclosure service. If a recipient believes that they have no tax to pay, they are asked to contact HMRC with evidence.

Investors’ relief claims (August 2024)

Two different letters are being sent to taxpayers who have claimed investors’ relief from CGT for the tax year 2022/2023. One letter is sent to those who have not provided HMRC with a computation, or enough information to show the criteria for claiming the relief have been met. Recipients are asked to amend their returns, provide HMRC with more detail of the transaction, or face a possible compliance check. The other is sent to those whom HMRC suspect do not meet the criteria. Recipients are asked to amend their returns or risk HMRC opening a compliance check.

Animal breeders and sellers (August 2024)

HMRC have commenced two nudge letter campaigns in relation to those who earn income from breeding or selling animals. The first letter states that HMRC have information demonstrating that the recipient has earned money from such activities, but has not declared some or all of that income to HMRC. Recipients are requested to make a voluntary disclosure, and warned of an investigation and higher penalties if no response is received. The second letter has a more investigative tone than the first, stating that the recipient “may” need to declare income from the breeding or sale of animals. Recipients of this letter are also asked to make a voluntary disclosure to HMRC if they have under-declared income, and are warned that HMRC may start a check into their tax affairs if no response is received. Both letters state that voluntary disclosure in response to the letters will be treated as “prompted” for the purposes of assessing any penalties due.

High Income Child Benefit Charge (August 2024)

HMRC are sending letters to individuals who may need to pay the High Income Child Benefit Charge for the tax year 2022/2023. Recipients are asked to use the information and flowchart in the letter to determine whether they need to amend their 2022/2023 self-assessment return, and, if necessary, to do so by 30 September 2024. The letter warns recipients that, if they owed tax from their 2022/2023 self-assessment tax return but did not pay it within 30 days of 31 January 2024, HMRC will charge daily interest and may charge a late payment penalty.

Any taxpayers who receive nudge letters, even those confident of their tax position, should seek professional advice as soon as possible. Whilst nudge letters do not make specific accusations and are rarely overtly threatening in tone, they are generally based on actual data held by HMRC. Taxpayers who ignore these letters do so at their peril – failure to take action or respond is likely to mean that there is an imminent risk of HMRC starting an investigation (either under civil procedures or, in cases of suspected fraud, using their criminal powers). Early disclosure may also mitigate penalties.



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