

UK Tax Disputes Digest

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Introduction

Welcome to the autumn 2025 edition of our UK Tax Disputes Digest: a high-level summary of key developments in contentious tax over the last few months for tax and legal 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 in relation to unallowable purpose disputes.

We also cover a number of notable tax cases and other interesting procedural decisions. This includes the most recent case law development on determining the “place of effective management” in the context of the residence of trustees for the purposes of a double tax treaty and a significant caselaw development in the oil and gas space.

About the team

The CMS Tax Disputes and Investigations team provides a full-service contentious tax offering. This includes advising both corporate and private clients on all areas of direct and indirect tax covering tax dispute prevention, management and resolution. We seek to protect against tax risk, manage interaction with HMRC and conduct litigation at all stages of the courts and tribunals system including the Supreme Court.

With 17 partners, 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. The UK team works alongside the CMS global network which has tax capability in over 70 offices to assist clients with international issues.

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

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In focus: Unallowable Purpose Disputes – a Focus on Evidence

HMRC have recently written to companies with open enquiries concerning the application of the unallowable purpose rule. These ‘nudge letters’ indicate that corporates should consider their position in light of recent court decisions, see our article in the [winter 2024 edition](#) of this publication for further details. HMRC have also updated their guidance for the relevant decisions and indicated that they will “continue to investigate and challenge cases” where they believe that “the facts, circumstances and evidence” show that the unallowable purpose rule applies.

In light of HMRC’s significant recent successes in relation to unallowable purpose, it must be anticipated that the unallowable purpose rule will continue to prove contentious. The breadth of the rule is such that it will frequently be relevant, including in relation to commercially motivated transactions.

This article therefore provides a brief recap of key points arising from recent unallowable purpose case law and practical insight arising from unallowable purpose disputes.



The unallowable purpose legislation (sections 441 and 442 CTA 2009) seeks to disallow any debits where, in an accounting period, the main, or one of the main purposes of a company being party to a loan has an ‘unallowable purpose’, i.e. a purpose which is not amongst the business or other commercial purposes of the company. A tax avoidance purpose is specifically excluded from being one of the commercial purposes of the company. Where these provisions apply, debits attributable to the unallowable purpose are disallowed, on the basis of a just and reasonable apportionment.

A key issue is the need to determine why the taxpayer has entered into the relevant transaction in the way that it has. Evidence is therefore key.

The importance of this may be illustrated by the *Oxford Instruments* case ([2019] UKFTT 0254 (TC)). The FTT considered that the burden of proof was on the taxpayer to show that the closure notice was incorrect. The taxpayer was unsuccessful in meeting this burden and the debits were not deductible as the only purpose of issuing the relevant promissory note was to secure a tax advantage. The purpose of issuing the promissory note is considered to be a factual finding of the FTT. Therefore, any challenge must satisfy the *Edwards v Bairstow* [1956] AC 14 test which has a very high bar. *Oxford Instruments* did not appeal. Therefore this indicates the importance of evidence and the findings of fact at First-tier, both for s441 cases and “purpose” or other factual tests more generally.

A key consideration from recent case law has been whether the mere fact that a taxpayer has considered the availability of tax relief for interest cost as part of its ordinary decision-making processes is sufficient to trigger the application of the rules.

In Blackrock Holdco 5, LLC v HMRC [2024] EWCA Civ 330 the Court of Appeal considered this issue, acknowledging that,

“It is unrealistic to suppose that it will not form part of ordinary decision-making processes about methods of funding a company. Indeed, it might well be wrong for directors to ignore that consideration in deciding what is in the best interests of the company concerned ... it cannot have been Parliament’s intention that the inevitable consequence of taking out a loan should engage the unallowable purpose rules, subject only to consideration of whether the value of the tax relief is sufficient to make it a “main” purpose. Something more is needed.”

A detailed analysis will be required in any given context in order to determine whether there is “something more” than ordinary decision-making. HMRC’s updated guidance includes commentary on their approach to enquiries. It is noted that evidence of both unallowable and commercial purposes should be considered.

Case law has noted that memory is fallible, which supports the importance of contemporary documentation (see e.g. *Gestmin SGPS SA v Credit Suisse (UK) Ltd* [2013] EWHC 3560 (Comm)). Therefore care should be given to accurately reflecting transactions, rationale and discussions in detail. This includes retaining documents of key decision makers, not just at the point of a relevant transaction but also on a continuing basis where tests require application over each accounting period. The evidence should be complete and cover both tax and commercial drivers, rather than being provided on a standalone basis.

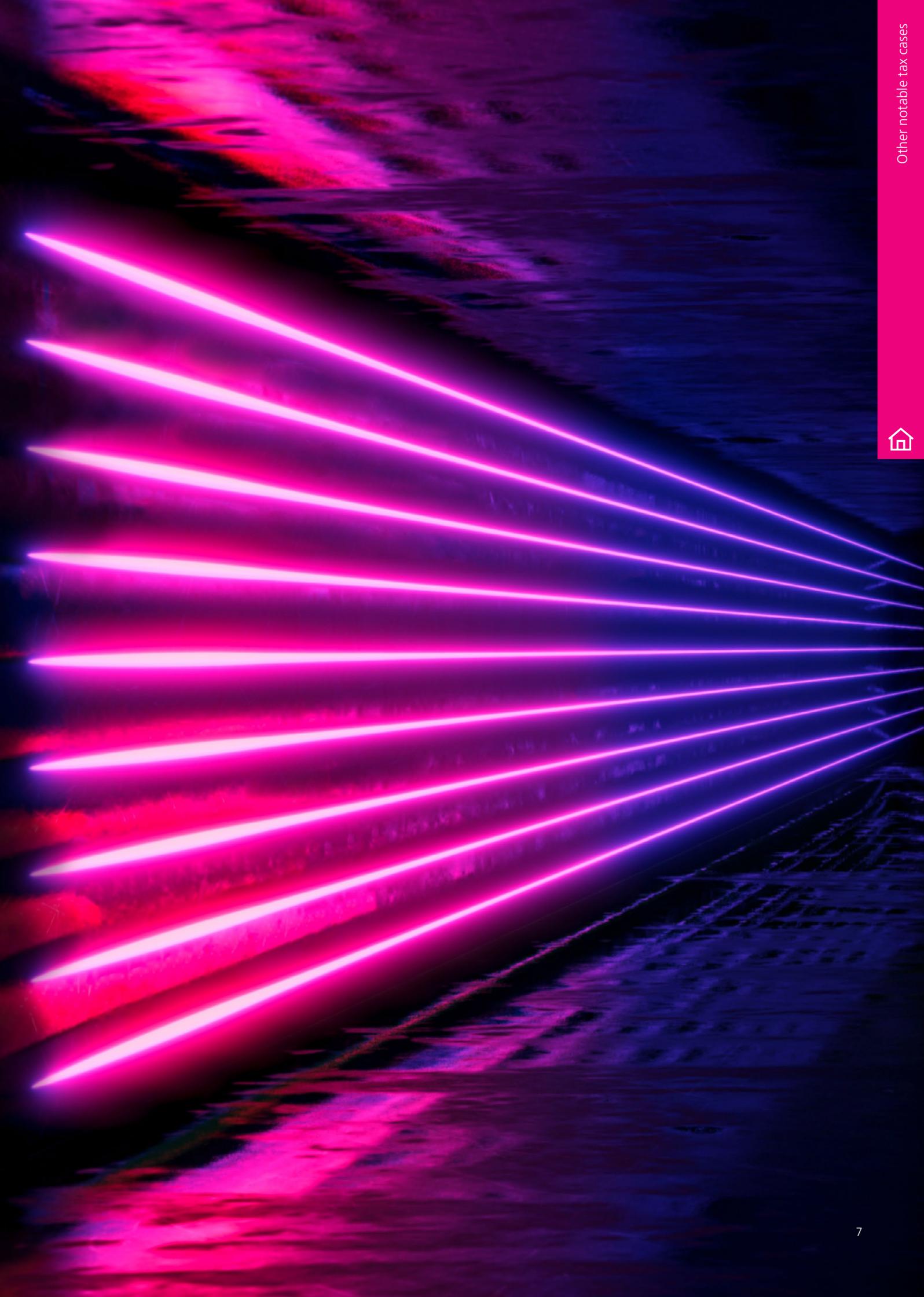


HMRC's guidance notes that the stated intentions of relevant individuals involved in decision making is helpful but "not determinative". Wider objective evidence may be considered and "it is likely that inferences will need to be drawn".

Similarly, evidence should be retained for an appropriate length of time. Purpose disputes take a long time to litigate. This is in part because of the front loading of disclosure review which can take place during HMRC enquiries and investigations. Although on the taxpayer side review tools can be used to speed up disclosure processes there remain delays in allowing for HMRC review. However, with the advent of AI and HMRC's increased focus on productivity, this may improve. HMRC consider there to be significant resource needs to investigate purpose enquiries. As such, they often use an iterative approach to information requests. This can prolong enquiries and require multiple rounds of taxpayer time and input. HMRC deploy both formal and informal information requests when running enquiries.

In summary, taxpayers should take care to retain contemporaneous evidence for a suitable amount of time. Records should be sufficiently detailed and fact-heavy enquiries, such as those on unallowable purpose, may run on for many years and require multiple rounds of disclosure and discussion with HMRC. Court approved review tools may be used to assist with disclosure review and responding to HMRC's information requests. A proactive approach to records and data can assist with responding to HMRC and seeking to close enquiries as efficiently as possible.

Should you wish to discuss your approach to disclosure, enquiry management or tax risk, please get in touch with our tax disputes specialists.





Other notable tax cases

In *HMRC v Dolphin Drilling Ltd* [2025] UKSC 24 the Supreme Court unanimously dismissed the taxpayer's appeal, concluding that the words "incidental to another use" required a use that arises out of the primary use, rather than an independent but secondary use. In practical terms this meant that significant, specifically contracted-for accommodation functions on support vessels could trigger the application of the 'hire cap', limiting the tax deductibility of lease payments. For offshore oil and service companies, there are potentially important implications for projects where inter-affiliate leasing arrangements are used.

Background

The case concerned the application of the oil contractors ring fence, which is set out in Part 8ZA Corporation Tax Act 2010 (the "**Act**"). Not to be confused with the general ring fence regime applicable to UK exploration and production activities, the contractors ring fence applies to companies in the supply chain that lease certain mobile assets to those carrying on those activities. In particular, the regime imposes a "hire cap" (at section 356N), which limits a contractor's ability to deduct for corporation tax purposes payments it makes under a lease of a "relevant asset" from an associated person.

The taxpayer, Dolphin Drilling Ltd, ("**Dolphin**") had been invited by Total E&P UK Ltd ("**Total**") to tender for the provision of a tender support vehicle ("**TSV**") at the Dunbar oil platform in the North Sea. The nature of the Dunbar platform was such that a TSV was required to provide tender assisted drilling ("**TAD**") services to support a proposed drilling campaign on the platform.

Dolphin proposed to use a semi-submersible drilling rig called the Borgsten Dolphin (the "**Borgsten**"), which could be converted into a TSV and was hired from an associated entity of Dolphin. The Borgsten, in addition to the space to be used for the TAD services, had the capacity to accommodate 102 persons on board, of which it was expected there would be around 47 surplus berths beyond those to be used by Dolphin and its subcontractors.



Total subsequently awarded the contract to Dolphin, and the contract originally included a requirement that the Borgsten supply accommodation for its own crew and 40 Total personnel. Subsequently, it was agreed that the accommodation of the vessel would be increased to 120 people, in return for an additional sum paid to cover the modification costs.

In Dolphin's tax returns it assumed that it was entitled to take account in the calculation of its profits for corporation tax purposes the entirety of the fees it paid to its associated entity for the hire of the Borgsten. HMRC's view, however, was that the hire cap should apply to restrict the tax deductions available to Dolphin as a result of the Borgsten being a "relevant asset" within section 356LA of the Act.

This definition broadly encompasses assets that are mobile, and which can either be used to drill exploration or production wells (which was not relevant to the TSV) or to "provide accommodation for individuals who work on or from another structure used in a relevant offshore area".

However, an asset otherwise falling within this second category is excluded (under section 356LA(3) of the Act) if *"it is reasonable to suppose that its use to provide accommodation for offshore workers is unlikely to be more than incidental to another use, or other uses, to which the asset is likely to be put"*, and the central issue in contention was whether the exclusion applied to the Borgsten.

The First-tier Tribunal ("FTT") found in favour of Dolphin, holding that the exclusion did apply, and this was upheld in the Upper Tribunal on appeal by HMRC. The Court of Appeal allowed HMRC's appeal, concluding that the exclusion did not apply, and the taxpayer appealed to the Supreme Court.

Decision

The central focus of the Supreme Court was on what it meant for one use to be "incidental to" another, which should be given its ordinary meaning, and in considering the alternative approaches taken by the lower courts.

The FTT had broadly concluded that something was incidental to another matter if it was subordinate, or secondary, to it. Since the primary use of the Borgsten was providing TAD services, and the provision of accommodation was a secondary use, the exclusion was capable of applying. In contrast, the Court of Appeal had found that the words in question were ordinary words, and that use A was incidental to use B, "if it arises out of use B, something that is done because of use B, or in connection with use B, or as a by-product of use B". This was not the case if use A were an unconnected and independent purpose in itself.

The Supreme Court preferred the approach taken by the Court of Appeal – with the unanimous judgment wholly agreeing with the key analysis in the Court of Appeal – and concluded that unless use A arose out of use B, it

was independent and not incidental to use B. Since the provision of accommodation did not arise out of the TAD services, it was not incidental to them, and the exclusion was not capable of applying.

The Supreme Court did note that in principle, the use of accommodation on a TSV which was "trivial or casual" may not be more than incidental to the provision of TAD services, but concluded that, "those are not the circumstances of this appeal where Total stipulated for the use of extensive accommodation on the Borgsten and extra accommodation on the Borgsten was created for and paid for by Total".

Dolphin had argued that the case raised a point of law of general public importance because of the frequency of the use of the words "incidental to" in other taxing statutes. The Supreme Court concluded, however, that it was not appropriate for it to make any rulings on the phrase "incidental" or "incidental to" as it appears in other statutory contexts as it is important to read those words in their specific statutory context.

Comment

Given the deductibility of leasing costs is likely to have a material impact on the tax position of contractors, the case is a potentially significant one for the UK oil and gas supply chain (in particular, companies that lease multi-purpose offshore assets). It is not uncommon for TSVs to have surplus accommodation which could be used to provide accommodation services to offshore workers. The Supreme Court's decision confirms that if a vessel's accommodation function is a significant independent part of its use – especially where it is specifically contracted for and paid for by the operator – the hire cap will apply, limiting the tax deductibility of lease payments. Whether it can be said that such provision arises out of or in connection with other services will need to be carefully considered by taxpayers in light of the Supreme Court's decision and considering the factual findings of the FTT on which those findings were based.

In this context, it is interesting to note the comment that the provision of accommodation services may still fall within the exclusion where they are "trivial or casual", even if it this was not the case here. This suggests that on different facts there may be a route to such accommodation services still being accepted as incidental. This does though seem to partly replace the question of what is meant by incidental with the question of what is meant by trivial or casual, and (unless HMRC guidance is forthcoming on the point) this may be an area of focus for taxpayers who wish to determine whether the hire cap applies to them.

The Supreme Court's conclusion that the phrase "incidental to another use" refers to use which arises as a result of a primary use (as opposed to a use which is merely less important than the main use) may also have wider relevance in other legislative provisions, notwithstanding the comments of the Supreme Court regarding the importance of statutory context.



In *Haworth & Ors v HMRC* [2025] EWCA Civ 822, the Court of Appeal has clarified the meaning of a place of effective management (“**POEM**”) in determining the residence of trustees under the UK/Mauritius tax treaty (the “**Treaty**”), confirming that the test is different from that for central management and control.

Background

The taxpayers were settlors of separate family trusts that held shares in a UK-incorporated company. Under the advice of tax advisors situated in the UK, the taxpayers engaged in a “*Round-the-World*” sale scheme. Under this scheme: (i) the Jersey-resident trustees of both trusts were replaced with trustees resident in Mauritius; (ii) the shares were sold; and (iii) UK-resident trustees replaced the Mauritian trustees within the same tax year. The taxpayers argued that, by virtue of the Treaty, no UK capital gains tax (“**CGT**”) was payable on the disposal because Mauritius was the POEM of the trustees at the time of the sale. HMRC disagreed.

This matter progressed through the FTT and UT which both agreed with HMRC. They concluded that the POEM was the UK by reference to *Smallwood v Revenue and Customs Comrs* [2010] EWCA Civ 778 (“**Smallwood**”). *Smallwood* identified a POEM as the site of top-level management rather than the day-to-day management of trustees. It subsequently located the POEM at the source of the overarching scheme the trustees had complied with. The taxpayers argued that *Smallwood* was the incorrect legal test, and the courts ought to have applied the central management and control (“**CMC**”) test from *Wood v Holden* [2006] EWCA Civ 26. Under the CMC test, the trustees would be resident in Mauritius as that was where the binding decisions regarding the shares were made.

Decision

The Court of Appeal found that the FTT and UT had applied the correct legal test and dismissed the appeal. The Mauritian trustees had followed a plan devised and orchestrated from the UK. In determining the POEM, the Court of Appeal stated that courts should consider the full circumstances of a scheme and not confine their assessment to the moment of disposal. The place of “realistic, positive” management was therefore in the UK and the *Smallwood* test was the correct legal test to identify a POEM. The Court of Appeal further reasoned that a POEM was not a place of CMC because: (i) a company or trust can only ever have one POEM at a point in time (in contrast to a place of CMC); and (ii) a POEM, as a term used in a tax treaty, should be considered from an international perspective and not by reference to case law or legal concepts specific to the UK (in contrast to the CMC test).

Comment

The Court’s decision provides clear confirmation that the POEM test in Treaties is different from the CMC test for corporate residence. The POEM test looks at where overall management happens, which is not necessarily the same as where the trustees are resident at any given time. It also demonstrates the potential relevance of an “overarching plan” in these contexts.



In *The Prudential Assurance Company Ltd v HMRC* [2025] UKSC 34, the Supreme Court has found that a performance fee paid in consideration for intra-group fund management services was subject to VAT, where it was invoiced and paid after the supplier left the recipient's VAT group.

Background

In this case, the Supreme Court considered whether the effect of the VAT grouping regime, in particular section 43 of the Value Added Tax Act 1994, is that no VAT is chargeable on an intra-group supply of services even where the supplier has left the group by the time consideration for the supply is invoiced and paid.

The taxpayer, the Prudential Assurance Company Ltd ("**Prudential**"), carried on a with-profits life and insurance business. Silverfleet Capital Limited ("**Silverfleet**") provided Prudential with investment fund management services in relation to the with-profits fund.

Silverfleet received consideration comprising: (i) a management fee, payable quarterly; and (ii) performance fees, which were payable in the event that the performance of certain sub-funds exceeded a set benchmark rate of return.

When Silverfleet was providing its services, Prudential was the representative member of a VAT group of which Silverfleet was also a member. However in November 2007 Silverfleet left the VAT group, as a result of an MBO, and ceased to provide the management services to Prudential.

Many years after Silverfleet had stopped making the fund management supplies to Prudential and left the VAT group, the hurdle rate for the performance fee was passed. Silverfleet therefore invoiced Prudential for performance fees of £9,330,806. The issue in dispute was whether VAT was due, given that at the time Silverfleet invoiced Prudential for the fee they were no

longer in the same group, or not due on the basis that it arose out of services provided when they were in the same group.

Decision

The Supreme Court, agreeing with the Court of Appeal and Upper Tribunal, concluded that the relevant supply was treated as being made when the performance fee was invoiced, pursuant to regulation 90 of the VAT Regulations 1995 (SI 1995/2518) ("**Regulation 90**"), which governs time of supply for continuous supplies of services. In particular, the court found that the VAT grouping provisions must be read alongside the time of supply rules, and that there is no special time of supply rule in relation to VAT groups.

Given that, at the time the performance fee was invoiced, the companies were no longer VAT grouped, the performance fees were subject to VAT. The Court also considered that HMRC's interpretation of the effect of the timing rule in Regulation 90 in relation to the performance fee was consistent with the Principal VAT Directive.

Comment

This decision clarifies the impact of the time of supply rules in relation to continuous supplies between members of VAT groups. The outcome of this case will be a key consideration in any circumstances where the consideration for an intra-group supply includes a performance or success (or any other type of contingent) fee, which crystallises after the supplies have been made.



Interesting decisions from the tribunals

In *Trevor John Masters v HMRC* [2025] UKFTT 00967 (TC), the FTT has found that under the UK-Portugal Double Tax Convention, the UK did not have taxing rights over SIPP withdrawals by a Portuguese tax resident.

Background

The FTT in this case examined whether withdrawals from a Self-Invested Personal Pension (“SIPP”) were “paid in consideration of past employment” under the UK - Portugal Double Tax Convention (the “DTC”). In allowing the taxpayer’s appeal, the FTT decided that the withdrawals were “paid in consideration of past employment” within Article 17 of the DTC and, as Mr Masters was resident in Portugal at the relevant time, the DTC allocates the taxation rights over them to Portugal. The decision provides useful commentary on the interpretation of a DTC, including consideration of the OECD commentary.

Mr Masters was a member of a defined benefit occupational pension scheme (the “Pension Scheme”) between March 1983 to November 2015 as a company employee. All the Pension Scheme benefits would be paid in consideration of past employment. In April 2016, Mr Masters arranged for his entitlement in the Pension Scheme to be transferred as cash equivalent to a newly created SIPP (the “TJM SIPP”).

Mr Masters left the UK in March 2019 and was resident in Portugal for the 2019-20 tax year with Non-Habitual Resident (“NHR”) status. Prior to 2019-2020 Mr Masters was UK tax resident. At the time, NHR’s benefitted from exemption of foreign source pension income from taxation in Portugal if taxed by the source state or not deemed to be obtained in Portugal. During the 2019-2020 tax year, Mr Masters withdrew funds from the TJM SIPP (the “SIPP Withdrawals”) which the Portuguese authorities did not tax on the basis of the NHR scheme.

The SIPP Withdrawals were subject to the deduction of

UK income tax at source, which was the subject of this appeal. Subsequently, Mr Masters requested a no tax (“NT”) code from HMRC. This was rejected by HMRC. Mr Masters submitted his UK self-assessment tax return for the 2019-2020 tax year, claiming relief for the tax deducted. Mr Masters sought to rely on the DTC to treat the SIPP Withdrawals as taxable in Portugal only, allowing him to claim the relief and obtain a NT code.

Article 17 of the DTC provides that pensions paid “*in consideration of past employment to a resident of a Contracting State*” will be taxable only in that State. Article 20 of the DTC provides a similar provision for items of income that are not expressly mentioned in the DTC provided that the resident is “subject to tax” in that State.

HMRC enquired into the request for a NT code and the 2019-2020 tax return. HMRC issued separate closure notices in May 2021 and review conclusion letters in November 2022, rejecting Mr Masters’ claims for an NT code and tax relief on the basis that:

1. Article 17 of the DTC does not apply to the SIPP Withdrawals because they are not “*paid in consideration of past employment*”; and
2. pursuant to Article 20 of the DTC, the SIPP Withdrawals are taxable in the UK because they are not “*subject to tax*” in Portugal.

HMRC argued that the relevant causal connection between Mr Masters’ employment and the SIPP Withdrawals was broken so that they did not meet the condition of being “*paid in consideration of past employment*”.



Decision

The FTT allowed Mr Masters' appeal and decided that the SIPP Withdrawals were "*paid in consideration of past employment*" thus Article 17 applied. The FTT considered that the relevant causal connection was not broken because Mr Masters had transferred his entitlement in the Pension Scheme to the TJM SIPP directly. None of the funds had become his property until the SIPP Withdrawals were made.

The FTT contrasts this with the situation where an employee receives a salary from their employer and then pays some of that salary into a SIPP. Here, the causal connection would be broken because the salary had moved into the hands of the employee before passing into the SIPP. Other facts in the case strengthened the relevant causal connection, including the proportionately short period of time that Mr Masters' entitlement had been held in the TJM SIPP compared to the Pension Scheme. Although it was not necessary for the tribunal to consider Article 20, in the alternative the FTT considered that the "subject to tax" condition required actual and effective taxation. As the SIPP Withdrawals were exempt from Portuguese tax they were not actually taxed in Portugal, so Article 20 would not apply to prevent the UK from taxing the SIPP Withdrawals.

Comment

This case will be of particular interest to individual taxpayers with large entitlements held under a SIPP and who may be seeking the most tax-efficient retirement destinations. The FTT confirmed that SIPPs may fall under the provision of Article 17, reducing HMRC's ability to apply UK income tax to such pensions. However, caution should be advised, as the decision also suggests that a case-by-case analysis will be implemented for any SIPPs situated outside the UK. As taxpayers will be aware, the application of tax treaties and issues of tax residency are highly fact dependent. Similarly, it is key to ensure that detailed records are held to support residence and treaty claims, particularly where matters relate to years or decades earlier which are important for determining the issues.



In *Tinkler v HMRC* [2025] UKFTT 01016 (TC), the First-tier Tribunal considered the extent to which HMRC may rely on new legal arguments not explicitly stated in its closure notices. The Tribunal held that such arguments, including those based on Section 66 of ITA 2007 and GAAP, may be introduced provided they support the conclusions already set out in the closure notice. The decision clarifies the flexibility HMRC has in framing its legal case at appeal stage, while reaffirming that closure notices define the jurisdictional boundaries of a tax dispute.

Background

Mr Tinkler filed self-assessment tax returns for the years 2010-11 to 2016-17. In every year but one he claimed losses from a combined trade involving horse breeding and horse racing. HMRC opened enquiries and subsequently issued closure notices concluding that the losses had been overstated, primarily on the basis that the racing activities did not form part of a trade.

In its Statement of Case, HMRC introduced additional grounds not explicitly stated in the closure notices.

These included:

- Valuation issues in relation to *Sharkey v Werner* (1955) 36 TC 275 and UK GAAP;
- In the alternative, whether a combined trade was carried on commercially with a view to profit for the purposes of Section 66 ITA 2007; and
- Whether, in the alternative, the racing expenses failed the “wholly and exclusively” test under s34 ITTOIA 2005.

Mr Tinkler applied to the Tribunal to determine whether the s66 and GAAP issues fell within the scope of the closure notices and so HMRC were prevented from raising them.



Decision

The Tribunal held that HMRC was entitled to rely on the ‘GAAP issue’ for all relevant years, as it underpinned the amendments made to Mr Tinkler’s returns. It also found that the ‘Section 66 issue’ was within scope for all years except 2013–14, where the closure notice referred to overstated profits rather than losses.

The Tribunal emphasised that closure notices must be read in context and that its jurisdiction is defined by the conclusions stated in those notices, not the reasoning behind them. It reaffirmed that new legal arguments may be advanced at appeal provided they relate to the same identified or obvious subject matter as the closure notice.

Mr Tinkler was granted permission to amend his grounds of appeal to address the GAAP, s66 and wholly and exclusively issues. The substantive hearing will proceed on an “in principle” basis, with quantification deferred.

Comment

This decision clarifies the scope of tax appeals and the flexibility afforded to HMRC in advancing legal arguments. It is particularly relevant for practitioners handling complex enquiries where HMRC may advance arguments based on multiple statutory provisions or in respect of accounting principles. Careful consideration should be given to the scope of the closure notice and how this is dealt with by taxpayers in tribunal appeals.

The outcome of the substantive hearing in Tinkler may provide further commentary on the established body of case law on “wholly and exclusively” and trading matters.



Other developments

Spending Review 2025

The Chancellor presented the Spending Review 2025 to Parliament in June. This did not include any new tax announcements, but it did set out details of HMRC's funding settlement for the period up to 2028–29 for resource expenditure, and 2029–30 for capital expenditure. The review indicated a continued focus on HMRC resource and capability, to be concentrated on compliance and debt management, so that HMRC can close the "tax gap" and improve tax collection. This includes (as announced at the Autumn Budget 2024) funding for an additional 5,500 compliance staff and 2,400 debt management staff.

Another area of focus was digital transformation and reducing post, with the government forecasting that at least 90% of interactions with HMRC will be via digital self-serve by 2029-2030. There is an intention to make HMRC a "digital first" organisation, including using AI to help taxpayers with enquiries and to raise productivity within HMRC.

HMRC's document "Departmental Efficiency Plans" which accompanies the Spending Review identifies efficiency gains "of almost £14bn by 2028-29...through a combination of improved outcomes and reduced cost". Upstream compliance is named as one area of efficiency whereby HMRC aim to prevent non-compliance proactively rather than reactively, to prevent costly compliance and litigation. Case management tools and automation are referenced. This could mean additional compliance checks and enquiries for taxpayers, in addition to HMRC seeking to utilise technology throughout their review processes.

HM Treasury publishes 'Tax Policy Making Principles'

HM Treasury released a policy paper in June setting out the principles that will guide how the Government will design and deliver tax policy changes.

This confirmed that the Government will make tax policy changes through a single major fiscal event cycle, to increase predictability and stability. The paper indicates that the Government intends to take a more "flexible" approach to consultations (moving away from a strict 12-week consultation period). Draft legislation will typically continue to be published on "Legislation day" (L-day) in the summer, but the Government will, where appropriate, look to publish technical consultations at other points in the cycle sufficiently in advance of the introduction of the Finance Bill to make it easier for interested parties to respond.

The paper states that the following principles underpin the Government's approach to tax policy making:

- Predictability and stability;
 - The single major fiscal event cycle will provide a predictable and stable framework for the delivery of tax changes.
- A smart and agile approach to consultation;
 - The Government will engage stakeholders fully and flexibly when developing tax policy, prioritising dynamic and frequent engagement with tax professionals at both ministerial and official levels. Where formal consultation is required, it will be targeted and precise, only seeking information that is genuinely needed, and will last a proportionate amount of time.
- Transparency;
 - The Government is committed to transparency, and will make sure that its rationale for tax policy changes and assessments of policy impacts are clear.

These principles will enable the Government to deliver change quickly, whilst making sure that the impacts of tax policy changes are fully understood.

New Business Brief : VAT Deduction on the Management of Defined Benefit ("DB") Pension Funds

HMRC have published Business Brief 4 (2025), concerning VAT deduction on the management of DB pension funds.

Until the Brief was published, HMRC's policy was that, where there was dual use of investment costs by an employer and the trustees, a method of apportionment on a fair and reasonable basis to determine how much input tax could be deducted by each party was required.

The Brief states that HMRC no longer view investment costs as being subject to dual use. Instead, all the associated input tax incurred will be seen as the employer's and deductible by the employer, subject to normal deduction rules. This means that all input VAT incurred on both the administration and investment services relating to DB pension funds will be seen as the employer's and deductible by the employer, subject to normal rules.

In addition, where trustees are supplying pension fund management services to the employer and charging for them, they will also be able to deduct input tax incurred for the purpose of providing those services, provided they are VAT-registered. Any deductions by the trustees will be subject to normal deduction rules.

The new policy applies from 18 June 2025 and any claims for additional input tax will be subject to the normal 4-year cap. HMRC state that they will publish guidance to explain the policy change by autumn 2025.



Regulations amending the UK's CRS and FATCA reporting regime and implementing the Crypto-Asset Reporting Framework ("CARF") in the UK

The updated regulations expand the scope of the CRS reporting in the UK to include electronic money institutions and certain e-money products and to exclude most charities. The regulations also introduce a new mandatory registration requirement for Financial Institutions and reform the penalty provisions. The introduction of a new mandatory registration requirement – even where the Financial Institution has no accounts to report – is in line with the trend towards increasing HMRC's data and information-gathering powers.

The amendments relating to the CRS come into effect from 1 January 2026, i.e., in relation to the 2026 reporting year. However, the amendments relating to reformed penalty provisions and mandatory registration for certain Financial Institutions came into force from 16 July 2025.

Regulations implementing the CARF in the UK will come into effect on 1 January 2026. The CARF requires UK reporting crypto-asset service providers ("RCASPs") to collect information in relation to in scope transactions, on an annual basis. The regulations provide for mandatory registration of reporting crypto-asset providers and contain specific penalties for non-compliance.

HMRC annual report and accounts

HMRC released their annual report and accounts for 2024-2025 in July, along with supporting statistics. This provides useful insight into HMRC's activity over the period and key areas of focus, including which sectors and taxes are investigated most by HMRC.

Key points from the report are as follows:

- Total tax revenues were £875.9bn, a 3.9% increase on the previous year;
- The tax gap (i.e. the difference between the amount that is theoretically due to HMRC and the amount that is actually collected) in 2023-2024 (the most recent year for which this data is available) sat at 5.3%. An estimated £48bn of tax was "protected" by tackling avoidance, evasion and error in 2024-2025. The foreword emphasises the Government's commitment to closing the tax gap, noting the 5,500 increase in compliance staff and 2,400 debt management staff over the next 5 years. Taxpayers should expect continuing focus on this area, including increased compliance activity;
- 310 prosecutions were brought as a result of HMRC criminal proceedings, with a 91% success rate in achieving convictions.

The technical notes indicate that "international" matters (including transfer pricing, withholding tax and CFC issues) are a significant area of focus for HMRC, with £15bn tax under consideration for Large Business and £3bn for Wealthy/Mid-sized Business, continuing a trend from recent years.

Other areas of interest are VAT legal interpretation and "boundary pushing", employment issues and the intangible asset regime. Employment in particular has seen a significant increase in tax under consideration of c£4bn in Large Business (being £5.6bn for 2024-2025 increasing from £1.7bn for 2023-2024).

Key sectors of HMRC interest include banking (£8bn), retail (£7bn), telecoms (£8bn) and pharma (£4.5bn) within Large Business. The tax under consideration in Large Business increased to £52.6bn from £44.9bn in the previous period. Wealthy and Mid-sized Business showed an increase also from £11.8bn for 2023-2024 to £14.2bn for 2024-2025.

A technical note on "compliance yield" accompanied the annual report. HMRC state that compliance yield is the estimate of revenues that would otherwise have been lost if not for HMRC's compliance activity and the impact of policy changes to address non-compliance.

HMRC plan to focus on "upstream" compliance, such as the provision of clear guidance and the use of user-friendly digital interfaces, aiming to collect a greater proportion of tax from interventions that take place before a tax return is submitted. Upstream compliance yield increased as a proportion of total yield from 34% in 2023-2024 to 41% in 2024-2025.

HMRC customer surveys

HMRC have released the results of its customer surveys for 2024.

As previously, a large majority (91%) of Large Businesses rated their "appetite for risk" in terms of boundary pushing tax planning as low. Where businesses were involved in litigation, around 80% agreed that complex legislation or unclear legislation were a key factor in the dispute, around half reported that unhelpful guidance was a factor, and just under 30% that HMRC's administration of the tax system was a factor.

Policy report on Uncertain Tax Treatment ("UTT") regime

HMRC have released a policy report on the UTT regime, which requires businesses to bring uncertain tax positions to HMRC's attention when certain conditions are met. The report notes that whilst it is too early to estimate the tax protected by the UTT regime since it became effective on 1 April 2022, more than £900 million of uncertain tax positions have been notified to

HMRC. HMRC's view is that the UTT regime has positively impacted taxpayers' behaviour in engagement with HMRC and the timeliness of reporting. The report concludes that the UTT policy is meeting its objectives of changing businesses' behaviour by increasing tax position transparency for some taxpayers who were not transparent and promoting equality for those who already were transparent.

HMRC Transformation Roadmap released

The Government has released a Transformation Roadmap for HMRC, outlining its plan to modernise and reform the tax administration system. Three priority areas are noted:

- Improving day-to-day performance and the overall customer experience;
- Closing the tax gap; and
- Driving reform and modernisation of the UK's tax and customs system.

The Roadmap also sets out that the Government plans to address the tax gap caused by "*legal interpretation disputes*". This refers to cases where there is no avoidance but where a taxpayer's interpretation of the law, and how it applies to the circumstances, is different from "*that intended by the legislation*". HMRC aim to tackle this tax gap by providing clearer expectations in guidance products, and by legislative changes in areas most prone to disputed legal interpretation. In addition, HMRC plan for systemic changes to business systems and processes.

Digital transformation is at the heart of the Roadmap. By the end of 2028, HMRC investment plans include:

- Delivering a Digital Disclosure Service to enable taxpayers and intermediaries to correct mistakes and pay liabilities and penalties for all taxes due;
- Providing caseworkers with enhanced AI-powered systems, to speed up casework;
- Providing a secure digital channel for three-way communications between HMRC, customers and intermediaries.

The Roadmap confirms that HMRC do not intend to introduce Making Tax Digital for corporation tax but confirms it is developing an approach to the future administration of HMRC that is "*suited to the varying needs of the diverse CT population*".

Draft legislation for the Finance Bill 2025-2026 released on L-Day

On 21 July 2025, as promised, the Exchequer Secretary to the Treasury delivered a statement to parliament and HMRC released a large number of draft clauses for inclusion within the Finance Bill 2025-2026, for technical consultation. These were accompanied by policy papers and explanatory notes. A number of responses to

consultations released at the Autumn Budget 2024 and Spring Statement 2025 were also published, as were some new consultations.

Obbligations on third-party data holders to report information to HMRC

Draft clauses were released to implement the first phase of the government's reforms to improve HMRC's bulk data gathering powers and safeguards, as first announced at a consultation released at the Spring Statement 2025.

HMRC already receives certain information on:

- Financial accounts in relation to bank and building society interest paid, and interest from other sources paid, in relation to those accounts; and
- Card sales, from providers of card acquiring services.

At present, the obligation to report only arises where a notice is sent to the relevant data holder (e.g., financial institution) by HMRC. The draft legislation makes this reporting requirement mandatory without the need for the receipt of a notice, increases the timeliness and frequency of reporting required, contains provisions regarding the standardisations of data submission, requires suppliers to collect and report tax identifiers for matching to taxpayer records, mandates due diligence checks on data quality, and reforms the relevant penalty regimes for breach of the requirements.

The stated objectives are for HMRC to be able to more accurately pre-populate more sources of income in tax returns, as well as ensure that taxpayers are not able to hide or misrepresent their income to HMRC.

Modernising and mandating taxpayer registration with HMRC

These measures are designed to require tax advisers who interact with HMRC on behalf of clients to register with HMRC and meet certain eligibility requirements from 1 April 2026.

Under the draft legislation, the meanings of "tax adviser" and "interaction" with HMRC are drawn widely. Tax advisers who do not register with HMRC will not be able to contact HMRC by any method on behalf of a client. The requirement to register is not limited to those who file tax returns on behalf of clients.

The eligibility criteria for registering with HMRC include confirmation that the tax adviser has no tax returns or amounts of tax outstanding, and, if the tax adviser is an organisation, a confirmation of the same in relation to senior managers. The draft legislation currently envisages that individual tax advisers will not need to register if their employer is registered and their interaction with HMRC is in the course of the employer's business.



HMRC will be able, by notice, to require tax advisers who are registered to provide information or evidence reasonably required for monitoring whether the eligibility conditions are met. The draft legislation also envisages that HMRC may stipulate, in a notice or other document, standards expected of tax advisers in their dealings with HMRC.

Proposals to close in on promoters of marketed tax avoidance

Draft clauses released will make changes to the current legislation that targets those who promote or enable marketed tax avoidance. This includes the following.

The Disclosure of Tax Avoidance Schemes (“DOTAS”) and Disclosure of Tax Avoidance Schemes for VAT and Other Indirect Taxes (“DASVOIT”)

The draft legislation introduces a criminal offence for the failure of a promoter of tax avoidance arrangements to notify arrangements to HMRC, and amends the civil penalty provisions so that HMRC can directly issue DOTAS penalties without needing the approval of a tribunal.

Universal Stop Notices (“USNs”)

USNs will apply to all promoters and enablers of marketed tax avoidance and prohibit the promotion of the avoidance arrangements detailed in the USN (going a step further than Stop Notices, which apply only to promoters who are named in the notice).

Promoter Action Notices (“PANs”)

PANs will oblige businesses to cease providing products or services to promoters and enablers of tax avoidance where such products or services are connected to the promoter or avoidance and HMRC suspects that the promoter or enabler is in breach of a USN or Stop Notice. PANs will not apply to legal services where legitimate legal or tax advice is provided.

Connected Parties Information Notices (“CPINs”)

CPINs will allow HMRC to issue notices compelling or requiring persons that HMRC reasonably suspects are connected to the promotion of a marketed tax avoidance scheme to provide relevant information to HMRC.

Promoter Financial Information Notice (“PFINs”)

PFINs will enable HMRC to obtain access, with tribunal approval, to financial or banking data concerning promoters and parties connected to the promotion of avoidance, where that data is held by financial institutions.

Legal Professionals

Allowing HMRC to publish legal professionals’ details, where such legal professionals are facilitating the promotion of avoidance schemes.

Enhancing HMRC’s powers to tackle tax advisers who facilitate non-compliance

Draft clauses have been published to amend HMRC’s powers to investigate and sanction tax agents whose conduct facilitates non-compliance in the tax affairs of their clients. The aim is to deter tax advisers from harming the tax system and hold advisers accountable if their actions facilitate non-compliance.

Carried interest reform

As announced at the Autumn Budget 2024, carried interest will be treated as deemed trading profits, subject to income tax and Class 4 NICs, with effect from 6 April 2026. There is no grandfathering for carried interest granted before that date. “Qualifying” carried interest will be subject to a 72.5% multiplier, giving an overall highest marginal effective rate of about 34.1%.

Draft legislation has now been published. Key points are as follows:

- No minimum co-investment requirement will apply and no minimum holding period will apply for the holder of the carried interest rights. However, the existing average holding period requirement for the fund assets of at least 40 months under the income based carried interest rules will remain;
- Employees and non-employees, such as partners, will be taxed under the same regime. However employees can still be liable under the existing employment-related securities rules;
- Non-resident individuals working in the UK can be subject to UK income tax on carried interest, subject to certain exceptions.

IHT on unused pension fund benefits

Draft legislation has been published which will have the effect of bringing most unused pension funds and death benefits within the value of a person’s estate for inheritance tax with effect from 6 April 2027.

Death in service benefits payable from a registered pension scheme will remain outside the scope of IHT.

Personal representatives will be liable for reporting and payment of IHT on unused pension funds, as opposed to pension scheme administrators (as originally proposed). Further draft legislation will be published to cover the exchange of information between pension scheme administrators and personal representatives.

Reform of Agricultural Property Relief (“APR”) and Business Property Relief (“BPR”)

Draft legislation was published which was generally in line with the reforms proposed at the Autumn Budget 2024 and the further technical consultation in relation to trusts. It was announced that the £1m allowance will remain non-transferable between spouses, but will rise in line with CPI from 6 April 2030 (in line with other nil-rate bands).

The reforms will take effect from 6 April 2026.

Reform of offshore-anti-avoidance legislation

A response to the call for evidence released at the Autumn Budget 2024 was released. The call for evidence concerned potential reform of “offshore anti-avoidance legislation” including the transfer of assets abroad rules, the settlements code and the attribution of gains rules. The response indicates that there was broad agreement that the rules should be reformed and simplified. The Government confirmed that it will give further consideration to these matters, including taking forward further consultation, and that an update will be provided at the Autumn Budget 2025. However the Government indicated that any amendments are not expected to take effect before the 2027-2028 tax year.

Potential technical amendments to the four-year foreign income and gains (“FIG”) regime

No draft clauses were released, but certain technical amendments to the FIG regime were announced in the Statement of the Exchequer Secretary to the Treasury. Some examples of upcoming technical “fixes” are given in the statement, but it contained nothing in the way of major concessions (the possibility of which had been the subject of press speculation).

PISCES tax implications

Draft legislation was published which will allow Enterprise Management Incentives (“EMI”) and Company Share Option Plan (“CSOP”) agreements to be amended to enable the exercise of options in connection with a PISCES window, without risking their tax advantages. HMRC’s previous publications had indicated that such amendments would be treated as changes to fundamental terms to the relevant option, causing the loss of the original tax benefits. In addition, HMRC released a Technical Note clarifying the treatment of shares as Readily Convertible Assets (“RCAs”) in the context of PISCES.

Technical amendments to the UK implementation of the Pillar Two legislation

The published draft clauses consist of updates to the current UK legislation in line with administrative guidance published by the OECD in January 2025. They also make amendments identified from responses to stakeholder consultations and to ensure that the UK legislation continues to be consistent with the commentary and administrative guidance to the rules agreed at OECD level.

Consultation on Land Remediation Relief (“LRR”)

HM Treasury released a new consultation seeking views on the effectiveness of LRR, in particular whether it is successfully encouraging development of brownfield land. LRR is a 150% corporation tax relief aimed at incentivising the regeneration of brownfield land and reducing the pressure to develop greenfield sites. The consultation asks whether the design of the relief can be improved, in particular with regard to the activities that qualify for relief, eligibility restrictions and the mechanism of support (with some stakeholders suggesting that an above-the-line credit would be more attractive). The Government also aims to understand the impact of the relief, in particular its value as compared with overall development costs.

Other L-Day legislation and publications

Draft legislation was also released:

- On R&D tax relief rules, in particular the exemption from restrictions for contracted-out R&D for companies with a registered office in Northern Ireland;
- To bring Employee Car Ownership Schemes within the scope of the benefit-in-kind rules as company cars from 6 October 2026;
- For changes to charity tax rules in relation to tainted donations, approved charitable investments (requiring all investments to be for the benefit of the charity and not for the avoidance of tax) and attributable income for charities and community amateur sports clubs;
- To make recruitment agencies or end-clients accountable for PAYE on payments to workers supplied through umbrella companies;
- Implementing Making Tax Digital for Income Tax, and associated penalty reform.



HMRC brings first corporate criminal offence prosecution under the Criminal Finances Act 2017 (“CFA 2017”)

HMRC have commenced their first corporate criminal offence prosecution for the crime of “failure to prevent the facilitation of tax evasion” under section 45 of the CFA 2017, relating to alleged R&D credits repayment fraud. As of 31 December 2024, HMRC stated that they had 11 live corporate criminal offence investigations, but that no charging decisions had yet been made, with further “live opportunities” under review. As part of prior releases of investigation data, HMRC stated that they did not consider the number of investigations to be the “sole measure of success - the legislation was introduced to drive behavioural change and for organisations to put in place preventative procedures that reduced the opportunity for facilitation to occur in the first instance”.

Changes to interest rates for late payments and repayments

A reduction in the Bank of England base rate from 4.25% to 4% was announced on 7 August 2025. As a result, the late payment interest rate for most taxes sits at 8%, effective from 27 August 2025 for non-quarterly instalment payments. Interest charged on underpaid quarterly instalment payments sits at 6.5% with effect from 18 August 2025, with overpaid quarterly instalment interest set at 3.75%. Repayment interest continues to be set at base rate minus 1% (with a minimum floor of 0.5%) and is therefore, at the time of writing, 3% for most taxes and duties.

New Guidelines for Compliance “Help ensuring documents filed with HMRC are correct and complete” (“GfC 13”)

HMRC have released a new set of Guidelines for Compliance, intended to assist taxpayers with understanding HMRC’s view and expectations regarding certain misunderstood or novel risks across tax regimes. GfC 13 sets out the steps HMRC consider that taxpayers should take to ensure that they can declare that documents and returns being submitted to HMRC are correct and complete, in relation to matters of both fact and law. The guidelines are targeted at those who are considering applying a “novel” or “improbable” interpretation of the law, including where advice has been sought. The Guidelines state that returns should not be filed based on an “improbable” interpretation of the law, i.e., where a taxpayer believes it is unlikely a court or tribunal would agree with that interpretation. An interpretation of the law will not be “improbable” when the law is “finely balanced between reasonable interpretations, with no clear position most likely to be found correct by the courts and tribunals”. A “novel” interpretation of the law is an interpretation that a court or tribunal has not yet considered. HMRC advise that

taxpayers must have “good reason” to believe such “novel” interpretation is correct, should consult a professional advisor experienced in that particular area, and must believe, on balance, that a court or tribunal will be likely to find that interpretation correct.

HMRC note that GfC 13 does not represent a change in policy, and that whilst taxpayers do not have to adopt HMRC’s view of the law, carefully considering HMRC’s view may help reach a position the taxpayer believes to be correct.

Spanish court rules non-residents may deduct related expenses when calculating tax due on rental income

The Spanish National Court has ruled that individuals who are resident outside the EU and EEA and who rent Spanish real estate to third parties are entitled to deduct related expenses when calculating the tax due on rental income. The outcome of the case challenges the current discrepancy between the tax treatment of individuals resident in Spain, the EU and the EEA, and the tax treatment of individuals resident outside the EU/EEA. At present, the latter individuals are taxed on gross rental income without the possibility of deducting expenses. The National Court ruled that this unequal treatment violates the free movement of capital under Article 63 of the Treaty on the Functioning of the European Union. Those who own and rent out property in Spain may consider proactively challenging their Spanish tax returns to preserve relevant time limits. It is expected the decision will be appealed to the Supreme Court. Please contact the Head of Tax Litigation at CMS Spain, Antonio Puentes, for more information.

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.

Persons with significant control (June 2025)

HMRC are writing to individuals who they have identified as being “persons with significant control” requesting them to check that they have declared all of their income and gains for tax year 2023-2024. Recipients are either asked to check their return for 2023-2024 and to correct any errors by 25 July 2025, or



to check whether they should have submitted a tax return for that tax year and, if required, to do so by 25 July 2025 or, if not required, to contact HMRC to confirm that position. The letter contains warnings that whilst any changes made by the taxpayer in light of the letter may be treated as “unprompted” disclosure, later discovery by HMRC of uncorrected errors relating to this issue will be treated as “prompted”, likely increasing any penalties chargeable.

Written off or released directors loans (June 2025)

HMRC are writing to directors who have between April 2019 and April 2023 (i) received a director’s loan that has been written off or released; and (ii) may not have declared the amount as income on their self-assessment tax return. HMRC state that taxpayers should use the digital disclosure service to declare any undeclared income.

Unallowable purpose cases (July 2025)

As mentioned in this edition’s In Focus article, HMRC have commenced a nudge letter campaign aimed at companies where it has opened an enquiry into the application of the unallowable purpose rule. The letters ask recipient companies to consider their position in light of three recent Court of Appeal decisions in HMRC’s favour, and notes that HMRC consider the principles derived from those three cases to be relevant to the particular taxpayer’s enquiry. HMRC offer a without prejudice discussion with the taxpayer, with the aim of resolving the ongoing enquiry.

Marginal rate relief (August 2025)

HMRC are writing to companies which they have identified as paying the wrong amount of corporation tax as a result of errors in claiming marginal rate relief through failure to take into account and declare associated companies. Two letters are being sent which take slightly different approaches and tones. Both letters

request that recipients check company tax returns for accounting periods including 1 April 2023 (when marginal rate relief commenced), make amendments where within deadlines to do so or voluntary disclosures where not, or inform HMRC why no associated companies need to be declared. One letter contains a section explaining that HMRC may open a compliance check should the recipient take no action.

Facilities management suppliers claiming input VAT deduction on utilities (September 2025)

HMRC are writing to suppliers of facilities management services, which claim VAT input tax deductions on utilities supplies used in their business. The letter notes that where a facilities management company does not enter into the contract with the utility supplier, the company is not the recipient of the supply, and therefore cannot recover the associated input VAT. Recipients are requested to review the relevant utilities contracts to determine whether they hold the contracts for the utilities supplies and also the appropriate invoices. Should the facilities management company have recovered input VAT where it is not the recipient of the supply, it is requested to correct any errors, and the letter warns late payment interest and penalties may be due. Recipients are also asked to inform their CCM of the outcome of their review, even if there are no errors regarding input VAT recovered.

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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