

Personal tax update (Lecture P1261 – 25.47 minutes)

Employment expenses lack evidence

Summary – Employment related expenses were disallowed due to inadequate mileage records and lack of evidence to support other expenses claimed.

Derek Storey, trading as an employed scaffolder, submitted his Self Assessment tax returns for the years 2014/15, 2015/16 and 2016/17, claiming deductions against his employment income, totalling close to £32,000. The deductions related to mileage, subsistence, tools and related costs, and accountancy fees.

On 20 June 2018, HMRC opened enquiries into each of the three returns, with the taxpayer and his agent being asked to provide evidence of the expenses incurred and how they qualified as allowable expenses.

A month later, having received no response, HMRC sent a letter stating their intention to disallow the claim for employment expenses and add employment benefits which were not included in the 2015/16 tax return.

Derek Storey's agent responded on 8 August 2018, stating that their client drove a car for his employment. The response included a schedule of mileage and a schedule of expensed items for all years. Two weeks later, HMRC asked for more detail and supporting evidence. The agent stated that Derek Storey could not give any further information and that mileage was kept to the best of his memory. The Agent further explained that a van was also used in the period when mileage was claimed.

HMRC issued closure notices, making the following amendments:

- Car and fuel benefit were added to the 2015/16 return, as reported on the P11D;
- Mileage calculated using HMRC's Approved Mileage Allowance Payment rates were disallowed as there was insufficient evidence to support the figures claimed;
- The subsistence claims of £1,875 per annum were denied as no allowable travel had been established;
- A flat rate allowance of £140 per year in respect of tools was disallowed, as no receipts were provided;
- Accountancy fees were disallowed as they were not incurred in the performance of Derek Storey's duties.

Decision

The First Tier Tribunal agreed with HMRC's decision.

Evidence for the mileage claim was lacking. Derek Storey had use of a company vehicle so why was he claiming mileage for using his own car? Even if he was using his own car, Derek Storey's mileage 'log' recorded monthly totals, and not individual journeys and dates.

The First Tier Tribunal dismissed the appeal, disallowing every expense.

The penalty for carelessness was suspended, subject to the remaining tax liability being settled promptly. HMRC had not published detailed guidance on how to keep records and the types of supporting evidence that should be submitted. Consequently, it would not have been acceptable to say that Derek Storey was careless as he may not have known the level of record-keeping expected.

In Taxation (3 June 2020) Andrew Hubbard commented:

'This is an odd case. In the first place, the taxpayer is described as having the trade of an employed scaffolder, which seems to be a contradiction in terms. Second, the tribunal suspended the penalty "subject to the condition that the remaining tax liability is settled forthwith". It is difficult to see how this can be reconciled with the requirement in FA 2007, Sch 24 para 14 that "HMRC may suspend all or part of a penalty only if compliance with a condition of suspension would help [a person] to avoid becoming liable to further penalties under para 1 for careless inaccuracy". It is not clear to me that payment of tax has any relevance to the prevention of any future careless inaccuracies.

'Finally, there are the strange comments about the urgent need for HMRC to publish "detailed guidance to assist and cater for employees who find themselves facing a lacuna of having to submit to expenses by way of self-assessment returns where there has been no consideration of the same by their employer etc. in calculating an employee's tax liability". I do not really follow what that means. HMRC does publish guidance and, in any event, there was no evidence that the taxpayer's significant overclaims of expenses — he claimed for nearly double the total mileage his vehicle actually travelled — had anything to do with his inability to find any HMRC guidance.'

Derek Storey v HMRC (TC8090)

£40 million was taxable income

Summary – Payments totalling some £40 million were taxable income in the hands of the lawyer that received them. Furthermore, as the beneficial owner of stolen family jewellery, a capital loss of £1.6m was allowed.

Stephen Mullens, a lawyer, was for many years involved in the business affairs of Bernie Ecclestone and those of the Ecclestone family.

Between 1999 and 2013, he received some £40 million that he argued were not taxable income:

1. £2.25m was paid to induce him to resign from his then-partnership in a law firm and so enable him to provide his services uniquely to Formula 1;
2. Three payments totalling £36m were gifts made by or at the direction of Mrs Slavica Ecclestone by reason of a "personal relationship of friendship and affection" and nothing to do with any business relationship;
3. A payment of £187,000 was made by Mrs Ecclestone to cover a family holiday to Mauritius

HMRC argued that the sums were taxable.

Stephen Mullens appealed to the First Tier Tribunal.

Decision

The First Tier Tribunal found that the £2.25 million 'inducement' was received as consideration for future services and was held to be trading income.

The Tribunal questioned why would Mrs Ecclestone would have made three payments totalling £36 million to Stephen Mullens? The written submission explained:

"Born in Croatia, Mrs Ecclestone became a woman of vast wealth with the habit, quite common among people of her class and type, of making what, to most, would seem to be huge payments for no particular reason, rather as a rich aunt might give big presents to her nieces, nephews and close friends."

The First Tier Tribunal disagreed, finding that these arose from the business relationship between the parties and were in fact success fees relating to deals as well as dispute settlement work undertaken. Consequently, they were taxable income.

The Tribunal did accept that the £187,000 for a holiday was a genuine gift and was not taxable.

On another matter, Stephen Mullens accepted he had brought diamonds worth £2 million into the UK without declaring them or paying the relevant taxes due. The First Tier Tribunal accepted HMRC's argument that the assessment was not out of time due the fraudulent conduct admitted to by Stephen Mullens in the Contractual Disclosure Facility that he entered into.

Finally, Stephen Mullens had claimed a £1.6 million capital loss on jewellery that had been stolen from his home. HMRC had disallowed the claim, arguing that the jewellery was his wife's property, and was described as such in the police report. The Tribunal found that Stephen Mullens had bought the jewellery, it was a matrimonial asset and that he was the beneficial owner. Ownership of family assets is often unclear and relying on police statements made immediately after a crime was not appropriate.

Mr Stephen J Mullens v HMRC (TC08112)

No entrepreneurs' relief for partnership

Summary – Preparing to carry on an activity was held not to be trading and so gains on partnership assets sold during this time were ineligible for Entrepreneurs' Relief.

John Wardle was one of three partners who, in January 2014, established a partnership to develop, construct and operate renewable power plants at three locations in the UK.

On 1 May 2014, the Partnership commenced pre-trading activities. In 2015, prior to commencing trading and once the projects had reached the stage where construction could begin, it sold two plants to a third party.

John Wardle declared his share of the gains in his 2015/16 tax return and claimed entrepreneurs' relief.

HMRC refused the claim, arguing that under s.169S TCGA 1992, the partnership needed to be 'a business' and 'a business' is a trade, profession or vocation, and is conducted on a commercial basis and with a view to the realisation of profits.

John Wardle appealed arguing that a partnership's business disposed of during the pre-trading period came within the definition of 'a business' under s 169S(1). He argued that the legislation explicitly stated that a disposal of shares could qualify for relief where the company was conducting pre-trading activities. He argued that the legislation should be interpreted to allow the same treatment to partnerships.

Decision

The First Tier Tribunal preferred a straightforward reading of the definition in the legislation, concluding that the legislation was written in the present tense. The Tribunal found that 'is a trade' and 'is conducted on a commercial basis' suggested that the trading activity should already have started, and that preparing to carry on an activity was not the same.

The Tribunal pointed out that parliament 'had the tools available to make commencement of trading a pre-condition ... but chose not to do so'. There was therefore no reason to adopt an interpretation to ensure the same treatment for partnerships

Wanting to keep details of the disposals out of the public domain, John Wardle requested that the decision remain anonymous. Although he lost this request on appeal, the details are not included in the case summary, on the grounds that he might appeal the case. It seems he may well have achieved his goal anyway.

John Douglas Wardle v HMRC (TC08105)

Guarantee rights

Summary – The disposal of the beneficial interest in guarantee rights in a company resulted in a gain for the taxpayer but that gain did not qualify for entrepreneurs' relief as no ordinary shares had been sold.

Incorporated before changes in company law, Monarch Assurance Holdings Ltd was limited by both share capital or guarantee (or distribution) rights with the company's articles of association providing for two classes of member in the company: shareholder members and investor members. The rights carried the voting rights, rights to surplus assets after repayment of share capital, and a right to share in profits. Further, the shares could be transferred but there was no provision for the transfer of distribution rights.

In July 2008 John Tenconi became a director of the company and, in June 2009, became an investor member, acquiring four "distribution rights" for £100 each.

In 2015, another company, Soogen Holdings Limited wished to purchase the shares of a subsidiary of Monarch Assurance Holdings Ltd. At the time, Monarch Assurance Holdings Ltd had issued eight distribution rights such that John Tenconi held 50% of those rights and so also 50% of the voting rights in Monarch Assurance Holdings Ltd. It was accepted that the approval of the investor members would be required for the shares of the subsidiary to be sold, so Soogen Holdings Limited either needed to acquire such approval from a majority of the existing investor members or alternatively acquire distributions rights to enable it to provide such approval.

John Tenconi assigned a beneficial interest in his rights to Soogen Holdings Limited, in exchange for cash. Following completion he held the rights as nominee and trustee for Soogen Holdings Limited and would exercise the voting and other rights on their behalf. He also undertook to account to Soogen Holdings Limited for dividends or other receipts. Of particular importance to the deal, John Tenconi agreed to vote in favour of Soogen Holdings Limited's acquisition of the subsidiary.

John Tenconi initially claimed entrepreneurs' relief in respect of his disposal of the distribution rights but HMRC refused the claim. He then argued that there was no disposal or, alternatively, no capital sums were received which derived from assets so any sums received were not taxable.

Decision

The First Tier Tribunal found that the rights were an asset. John Tenconi had made a disposal to Soogen Holdings Limited of his beneficial interest in the rights (s21 TCGA 1992) and a chargeable gain arose as calculated by John Tenconi in his tax return.

The Tribunal found that the distribution rights were not shares and did not form part of the issued share capital of Monarch Assurance Holdings Ltd. The articles of association specifically stated that investor members were not required to contribute to the company's capital. The Tribunal stated that if it had been intended that entrepreneurs' relief should include gains relating to guarantee rights, the legislation would have stated this.

The appeal was dismissed and the closure notice upheld in full.

Although not required, the First Tier Tribunal stated that if there had been no actual disposal, there would have been a deemed disposal under s22 TCGA 1992 as exercising rights, including voting rights, as instructed by a third party would be the use or exploitation of those rights by the owner.

Mr John Tenconi v HMRC (TC08088)

Refurbishment costs

Summary – HMRC restricted the deduction for refurbishment costs on the sale of a property and, due to lack of supporting evidence, this was restricted further on appeal.

In 2003, Babatunde Iginla owned a residential property on Fulham Palace Road, which he sold in 2015. His 2015/16 tax return included a chargeable gain, having allowed nearly £100,000 that had been paid for refurbishing the Property.

When asked for evidence to support the refurbishment costs, his accountants supplied an undated invoice on the contractor's letter headed paper. The payment was made in Nigeria by the taxpayer's father who was now deceased as this 'was the only place at that point in time where additional finance could be sourced because the mortgagor could not extend any further loan for such enhancement. Additionally, the contractor was willing to accept payment in Nigeria at a pre-agreed exchange rate.' No bank statement was supplied supporting the payment as the accountant stated that "a bank statement is a confidential document which belongs to the account holder and in this instance [the Appellant] was not privy." The accountant went on to say that no payment had yet been made to his father's Estate as "the administrators were resolving many post-testamentary issues"

HMRC reduced the refurbishment deduction to £23,500 and issued a closure notice to reflect this new figure, as well as a number of matters/ corrections that had been made.

Babatunde Iginla accepted these other amendments as correct but appealed the refurbishment costs that had been disallowed.

Decision

The First Tier Tribunal found Babatunde Iginla to be a “less than straightforward witness” and concluded that HMRC were within their rights to request more evidence.

Having worked through the refurbishment costs on a line-by-line basis, the Tribunal allowed only £11,263 of costs, just about half of what HMRC had allowed. Babatunde Iginla’s CGT liability was increased accordingly.

Babatunde Iginla v HMRC (TC08081)

Access to communal garden

Summary – The purchase of a London property with a right to access a communal garden did not make the property purchase liable to mixed use SDLT rates.

In August 2018, Nael Khatoun acquired the freehold interest in a London property for a consideration of £9,375,000. On the same day, he signed agreements giving him access to a communal garden in return for an annual rent.

Initially, Nael Khatoun submitted an SDLT return, applying the residential rates to the property. Later, he amended the return on the basis that an equitable interest in a communal garden was not residential property and so the lower mixed-use rates applied, generating a repayment of £861,750 of SDLT.

HMRC raised an enquiry into the SDLT return and later issued a Closure stating that SDLT was due at the residential rates and the refund claim was disallowed.

The taxpayer appealed arguing that the right of access to the garden was a separate property interest which was not residential property.

Decision

The First Tier Tribunal agreed with HMRC.

Nael Khatoun’s right to enter and use the communal garden was a licence to use land as permission to enter and use the garden was revocable on three months’ notice. Whilst there was clearly a connection between the right being granted to Nael Khatoun to use the garden and his ownership of the property, the right did not itself pertain to the property; it pertained to the communal garden.

The purchase of the London property with access to a communal garden was subject to SDLT at the residential rates and not mixed-use rates.

Nael Khatoun v HMRC (TC08085)

Properties joined by glass conservatory

Summary – Multiple Dwellings Relief was denied as the annex to the main property was not capable of being ‘lawfully let as a dwelling’

Michael And Anthea Mullane acquired a house with an annex in August 2018. The property had originally comprised two separate buildings with the annex being a coach house. They were separated by a wrought iron frame through which one could walk to reach the garden.

The previous owner joined the two buildings by creating a “T” shaped glass conservatory style area five feet wide. Separate doors allowed entrance to the annex and to the main house via the kitchen and lounge. The annex door had no lock when then property was acquired but one has been added since.

The couple were considering letting out the annex. The ground floor of the annex comprised a large room and bathroom. A photo of the living room in the annex showed a microwave on a stool or low table. The first floor of the annex has a kitchen sink, drainer, and small work top and a fridge. At the time of completion, there was no cooker or washing machine or place designed to accommodate a washing machine in the annex. At the time of purchase, the property was advertised as a single dwelling with the rooms in the annex described as bedroom 3/study and bedroom 4. Finally, there were no separate council tax bills or utility bills for the annex.

Michael And Anthea Mullane initially submitted an SDLT return on the basis that this was a residential property but three months later they submitted an amended return claiming Multiple Dwellings Relief, reducing the SDLT to £16,400. Following an enquiry, HMRC declined the relief.

Decision

The First Tier Tribunal found that the fact that there was a conservatory linking the two properties did not indicate that there was only one dwelling. The main problem was the lack of a proper kitchen. The cooker and sink were too close together for safe use, and the open plan kitchen posed a fire risk.

The Tribunal concluded that the annex was capable of separate occupation, but not of safe, separate occupation. It could not lawfully be let as a dwelling.

The appeal was dismissed.

Michael And Anthea Mullane v HMRC (TC08100)

No repayment by HMRC

Summary – HMRC’s request to strike out an appeal was dismissed as a dispute relating to box 20.1 in the tax return was within the scope of the enquiry and therefore was within the scope of the tribunal’s jurisdiction.

Richard Cochrane submitted his 2003/04 tax return in July 2004. As part of that return he gave details of an arrangement that he entered into involving an IIP settlement of which he was settlor and life tenant and an option that was sold by the trustees of that trust. Following the subsequent exercise of that option by the purchaser, Investech Bank (UK) Ltd, Richard Cochrane believed that he had suffered an income tax loss of £1,052,800, allowable under para 14A Schedule 12 to Finance Act 1996. He claimed relief in his tax return and claimed a tax repayment of £415,079.16.

At box 20.1 of his return and in response to the question "Have you already had any 2003/04 tax refunded or set off by your Inland Revenue Office ...?" he responded "yes" and disclosed a repayment as £20,000.

Following a long enquiry into this return, it was agreed that the loss had arisen as a result of an ineffective tax avoidance scheme. HMRC wrote stating that Richard Cochrane owed some £25,000, which included the £20,000 previously been repaid to him.

Richard Cochrane claimed that he had made an error on his return and had never received this refund. He wrote to HMRC stating:

"I have reviewed considerable amounts of information in an attempt to reconcile the entry within your computations described as 'Tax already refunded in the year' in the sum of £20,000. I'm afraid that I have not been able to identify any repayment of 2003/4 income tax overpaid to Mr Cochrane. Please can you send me details of this entry, including the dates, amounts involved and the manner in which they have been repaid."

HMRC were unable to produce any evidence to support the £20,000 repayment and replied stating:

"of course this does not mean that a repayment was not made, simply that no records for it can now be traced."

Richard Cochrane concluded that as neither party could identify the £20,000 it was reasonable to conclude that the sum had not in fact been repaid. He submitted an amended tax return, having removed the box 20.1 entry.

HMRC did not accept the amendment and issued a closure notice for the full amount.

Richard Cochrane appealed.

HMRC applied to the First Tier Tribunal to strike out the appeal on the grounds that the box on the tax return that Richard Cochrane had ticked (in error) was not part of the return and so could not be the subject of an appeal to the tribunal.

Decision

The First Tier Tribunal concluded that as box 20.1 was in the return, any dispute as to its effect was within the scope of the enquiry and the closure notice, and therefore within the scope of the tribunal's jurisdiction.

The Tribunal stated that it would expect to see bank account information from Richard Cochrane to prove there was no repayment received from HMRC.

The Tribunal concluded by saying that it was astonished that HMRC had no record of payments made, "if indeed a repayment was made."

HMRC's application to strike out the appeal was refused.

Richard Cochrane v HMRC (TC08078)