

Business tax update (Lecture B1441 – 23.51 minutes)

Flawed post-cessation trade relief

Summary – With HMRC's enquiry being out of time, the taxpayer's claim for post-cessation trade relief was allowed, even though the payments did not fall within s.97 ITA 2007.

Anthony Dennison was a partner in Rowe Cohen, a firm of solicitors and also held a 33% interest in Legal Report Services Limited.

The partnership entered into a contract with this company whereby the company would arrange for medical examinations of clients of Rowe Cohen in return for a fee. Anthony Dennison acted as a representative of Rowe Cohen in negotiating those agreements but did not declare his interest in the company to the partnership.

In February 2004, Anthony Dennison sold his shares in the company to Expedia for £1.5 million.

Three years later, in February 2007, the partnership ceased trading and around June 2007, the former partners discovered that Anthony Dennison had sold shares back in 2004. They claimed breach of contract and breach of equitable and common law duties.

In September 2009, a settlement was reached and Anthony Dennison was required to make settlement payments totalling £300,000 to his former partners, split into two payments of £150,000. He also agreed to release his interest in a loan note issued by Expedia, as a result of which Expedia agreed to pay £100,000 to the former partners.

In a letter dated 28 April 2011, he claimed that he amended his 2009/10 tax return, claiming post cessation trade relief of £250,000, being the forfeiture of the loan note of £100,000 and the first settlement payment of £150,000.

In April 2012, Anthony Dennison was struck off the roll of solicitors.

In July 2012, HMRC opened an enquiry in to his 2009/10 return but did not send a copy to his agents, Smith & Williamson. There was also a dispute between the parties as to when this letter was posted and received.

On 28 February 2014, HMRC issued a closure notice disallowing the claim for post-cessation trade relief as the settlement payments related to fiduciary breaches and other duties as a partner, which did not qualify for relief.

On 21 August 2017, following review, Anthony Dennison notified his appeal to the Tribunal arguing that his claim was valid and that HMRC's notice of enquiry contained in the letter dated 27 July 2012 was out of time.

Decision

The First Tier Tribunal reminded us that s.9A TMA 1970 provides that HMRC may enquire into a return by giving notice to the taxpayer within the time allowed. Where a tax return is amended, this is the date up to and including the quarter day following the first anniversary of the date on which the amendment was made. For this purpose, the quarter days are 31st January, 30th April, 31st July and 31st October.

The First Tier Tribunal found that the taxpayer's 2009/10 tax return had been amended on 28 April 2011, meaning the quarter day was 30 April, giving a deadline of 30 April 2012. The First Tier Tribunal stated that even if HMRC had been correct and the amendment was not received until 1 May 2011, extending the deadline by 3 months, HMRC's enquiry letter dated 27 July 2012, would not have been received before 31 July 2012. In reaching this decision, the Tribunal referred to HMRC's guidance stating that letters sent by second class post should be sent at least four working days before any relevant time limit and where possible at least seven working days before any relevant time limit. The enquiry letter was out of time, the notice was invalid and the appeal allowed.

The Tribunal went on to consider whether, had HMRC issued the notice to enquire within time, whether the post-cessation trade relief claim would have been invalid.

The settlement payments related to claims made against the taxpayer for breach of contract and breach of equitable and common law duties that the taxpayer owed to his former partners.

To qualify as valid post-cessation payments, s.97(2)(b) ITA 2007 requires that the settlement payments must have been made "in respect of defective work done, goods supplied, or services provided in the course of the [relevant trade or profession]". Anthony Dennison claimed that this included payments for defective work by him in negotiating the settlement with the firm's suppliers, Legal Report Services Limited.

The First Tier Tribunal disagreed, stating that it had not been provided with any authority on the extent of the provision and stated that the legislation should be given its natural meaning. The payments were not "qualifying payments" within s.97 ITA 2007. Had the enquiry been within time, the appeal would have been disallowed.

Anthony Dennison v HMRC (TC09153)

'Total relevant expenditure' for R&D

Finance Act 2024 contained an amendment to the definition of 'R&D intensive' for the purpose of entitlement to 86% enhancement and 14.5% payable credit. It is 40% (30% for accounting periods beginning from 1 April 2024) of 'total relevant expenditure' aggregated with connected companies' relevant expenditure.

Total relevant expenditure is now defined as (inserted as s.1045ZA into CTA 2009) expenditure:

- Brought into account under GAAP in calculating the profits of any trade carried on by the company, or
- In respect of which the company is entitled to relief under s.1045 (pre-trading expenditure), or
- Any amounts deductible in the tax computation under s.1308 (capitalised qualifying development costs)

To avoid double counting expenditure incurred with connected companies is ignored as is amortisation of capitalised development costs if they were included in total relevant expenditure when incurred.

Previously, it either said or it was proposed that a company had to exclude costs which were not deductible for tax purposes.

Skin treatments

Summary – Skin treatments were not exempt medical care, but HMRC's assessment was not issued in time.

Gillian Graham qualified as a registered general nurse in 1994, initially working as an NHS intensive care nurse and then later, for large skin care clinics. From October 2001, she ran her own clinic in London under the name "Skin Science".

In 2011, she qualified as a nurse prescriber. Having assessed and diagnosed a client's issue, she was then able to prescribe the medication that she would be issuing as a skin care provider.

Typically, patients attended her clinic by choice and were not referred to her by a GP, specialist doctor or psychologist. Gillian Graham stated that the vast majority of her patients came to her as they are suffering from medical conditions caused by "UV damage" and were sometimes referred to her by beauticians who were unable to carry out the treatment required.

On 25 April 2017 HMRC wrote to Gillian Graham explaining that, from information provided in her Self Assessment returns, she had been trading in excess of the VAT registration threshold.

She replied, stating that she did not need to be registered for VAT as she was a registered general nurse and her work consisted of providing exempt medical care for patients.

Subsequently, HMRC wrote, stating that there was insufficient evidence to conclude that her supplies were VAT exempt. HMRC argued that the treatments were "overwhelmingly cosmetic and so do not satisfy the requirements of the medical care exemption." HMRC stated that she would be compulsorily registered for VAT from 1 May 2007. This was formally noted in January 2018.

HMRC issued a best judgement VAT assessment on 7 September 2018 for the period 1 May 2007 to 28 February 2018.

Believing that all her treatments qualified for exemption, Gillian Graham submitted a "nil return" on 27 October 2020, albeit with the period starting from 1 November 2007, rather than 1 May 2007, which resulted in the previous assessment being "cancelled" or "superseded". HMRC issued a new assessment on 18 March 2021.

Gillian Graham appealed against both the compulsory registration notified in January 2018 and the VAT assessment issued in March 2021.

Decision

To fall within the medical exemption for VAT, Gillian Graham needed to satisfy the First Tier Tribunal that the principal purpose of the treatments was for the protection, including the maintenance or restoration of health.

The Tribunal found that she had failed to do so. None of her patients had been referred to her by medical specialists. Which could be seen as an indication of her patients seeing their treatments as cosmetic rather than therapeutic. Indeed, patient reviews obtained by HMRC from the internet were focused generally on the cosmetic aspects of their treatment. Further, her advertising was indicative of the treatments being intended for cosmetic rather than therapeutic purposes, their focus being on improving appearance. The First Tier Tribunal concluded that the treatments offered included: fillers, hyaluronic acid, botox/toxin and retinol. These were 'overwhelmingly cosmetic' and did not fall within the medical exemption.

Both parties agreed that the relevant time limit was 'one year after evidence of facts, sufficient in the opinion of the Commissioners to justify the making of the assessment, comes to their knowledge' (S.73(6)(b) VATA 1994).

HMRC argued that the new assessment was issued within time. However, the only new information supplied, which caused HMRC to issue the March 2021 Assessment, was the taxpayer's nil return.

Gillian Graham argued that submitting a nil return was not new information for this purpose. The First Tier Tribunal stated 'that if an existing in-time assessment was cancelled mandatorily by reason of submission of a nil return, submission of that nil return and its contents and the extinguishment of the taxpayer's liability could be evidence of facts justifying the issue by HMRC of a new assessment.'

However, in this case, the nil return did not contain any new information. Although it contained a slightly different period and a slightly different amount, those differences were determined by facts known to HMRC more than a year prior to the assessment. The nil return itself "was not evidence of facts for the purpose of s 73(6)(b)".

The Tribunal stated that the issue to determine was whether the 2018 Assessment was automatically cancelled or extinguished by submission of the nil return. The First Tier Tribunal was not provided with any statutory reason why the submission of a nil VAT return must cancel a previous in-time assessment. It was 'simply a consequence of the administrative system put in place by HMRC.' The submission of the nil VAT return was not a fact that justified the later assessment. With the later assessment issued based on facts known to HMRC more than one year before it was issued, it was not made within time and this appeal was allowed.

Gillian Graham T/A Skin Science v HMRC (TC09152)

VAT assessment within one-year time limit

Summary – HMRC's VAT assessment had been made within the time limit set out in s.73(6)(b) VATA 1994.

On 29 April 2019, HMRC assessed Nottingham Forest Football Club Limited for VAT of approximately £350,000 for the period 08/15. The assessment arose as a result of errors that had innocently arisen following a change in the company's accounting systems. The VAT assessed was not under dispute, but rather the company claimed that the assessment had been issued out of time.

Section 73(6)(b) VATA 1994 states that an assessment shall not be made later than:

- two years after the end of the prescribed accounting period; or
- one year after evidence of facts, sufficient in the opinion of HMRC to justify making the assessment, comes to its knowledge

Nottingham Forest Football Club Ltd argued that HMRC had the required facts on 20 April 2018. Having visited the club on 16 April to understand the business and its accounting systems, the HMRC officer returned on 20 April 2018 to examine invoices and download general ledger data from current/new accounting system. Raising an assessment on 29 April 2019, meant that the 12-month deadline had expired.

HMRC argued their knowledge of the facts was only complete from 9 May 2018, when a back-up memory stick containing data from the club's previous accounting system was collected by the HMRC officer. On this basis, the assessment raised on 29 April 2019 was within time.

The First Tier Tribunal found in HMRC's favour and the case moved to the Upper Tribunal.

Decision

The Upper Tribunal's decision was neatly summarised in Tax Journal (31 May 2024) as follows.

The first ground of the taxpayer's appeal was that the First Tier Tribunal failed to apply the correct test for the one-year rule as set out in *Pegasus Birds Ltd v C&E Commrs* [1999] STC 95. In particular, the club suggested that email correspondence in May 2018 showed that the HMRC officer had everything he needed to make the assessment from the Navision data provided on 20 April 2018. However, the First Tier Tribunal had found that submissions made about the Sage data (provided on 9 May) were unsupported and therefore had to be disregarded. The Upper Tribunal considered that this ground must fail due to the absence of evidence provided to the First Tier Tribunal.

The second ground pertained to the burden of proof. The club disputed that the burden of proof fell on the taxpayer. Despite the volume of case law on the one-year time limit it appeared that there had never been a challenge to the proposition that the taxpayer bears the burden of proof. The Upper Tribunal concluded that it made sense for the appellant to have the burden of showing the assessment was made out of time. It was true that once the taxpayer had made a prima facie case then the evidential burden shifted to HMRC to rebut this with evidence of its own. However, it could not be said that the club had established a prima facie case. This ground was therefore rejected.

A final ground of appeal was made to set aside a finding of fact that had been made 'without any evidence or upon a view of the facts which could not reasonably be entertained' (*Edwards v Bairstow* [1956] AC 14 challenge). However, this ground was also held to be without merit.

Nottingham Forest Football Club Ltd v HMRC [2024] UKUT 145 (TCC)

Share sale costs: decision overturned

Summary – Input VAT incurred as a result of selling shares in a company could not be recovered as there was a direct and immediate link with an exempt supply.

Hotel La Tour Ltd owned a 100% subsidiary, a company that owned and operated a luxury hotel in Birmingham. Both companies were part of the same VAT group.

The holding company decided to sell the shares in its Birmingham company and use the proceeds from sale to develop a new hotel in Milton Keynes.

To facilitate the sale, Hotel La Tour Ltd incurred marketing, legal, tax and accountancy fees totalling £382,899.51 plus VAT of £76,822.95. The company filed its 09/17 VAT Return seeking repayment of the input tax incurred.

HMRC commenced enquiries, later concluding that this input VAT was not recoverable.

Hotel La Tour Ltd argued that the professional services were directly and immediately linked to its 'downstream taxable activities' to fund and so develop its Milton Keynes hotel.

On appeal, both the First Tier and Upper Tribunal found in Hotel La Tour Ltd's favour, concluding that the exempt share sale did not break the direct and immediate link with the taxable hotel activity. The purpose of the sale was fundraising, to later use those funds to make taxable supplies.

HMRC appealed to the Court of Appeal.

Decision

The Court of Appeal overturned the decision.

In applying the 'direct and immediate link' test, the First Tier and Upper Tribunals should have first considered if there was a direct and immediate link between the professional services and the exempt share sale. If no such link existed, then and only then should a link have been considered between the company's 'general (downstream) taxable activity'

In this case, the First Tier Tribunal had found that the professional fees were incurred as part of the process of selling the shares and so were directly and immediately linked with the exempt share sale. With such a link existing, the input VAT was not recoverable.

The Court of Appeal found that this position was not changed as a result of the two companies being part of the same VAT group. Hotel La Tour Ltd claimed that its intra-group management services should be disregarded, meaning that it was not engaged in any economic activity. With the share sale being outside the scope of VAT, the related professional fees should be treated as general overheads and the input VAT was therefore deductible as the group as a whole was making wholly taxable supplies. The Court of Appeal disagreed, stating that Hotel La Tour Ltd supplied management services to its Birmingham company, meaning it was engaged in economic activity in the form of managing its subsidiary. "That brings the share sale within economic activity, as an exempt supply."

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