

Personal tax update (Lecture P1431 – 21.12 minutes)

Gambler who worked

Summary – The taxpayer had deliberately failed to declare income from working at a family-owned pub and also on the gain arising on the sale of a property.

Steven Hague's main source of income was from gambling.

He also worked at a family-owned pub but, as his father knew that he might lose all of his money gambling, he held on to his money "for safekeeping" until it was "needed".

On 26 October 2007, Steven Hague sold a property that he had bought the previous year. Later, in March 2011, he purchased another property.

However, between 2007/08 and 2015/16, the period under appeal, there was no record of him having filed any tax returns to declare income received or capital gains arising.

Having investigated his affairs, HMRC issued nine discovery assessments totalling £67,177 for the years 2007/08 to 2015/16 covering his failure to declare and pay capital gains tax on the property sale, as well as income tax on his income. Further, nine penalty assessments were issued totalling £43,665.

Steven Hague appealed, arguing that the deposits into his bank account were family gifts and exempt gambling winnings. Further, he argued that he had made a loss on the property sale.

Decision

The First Tier Tribunal found that, as a matter of fact, Steven Hague had received wages in cash, and made a gain on the disposal of his property. Further, no income tax was paid on the wages and no gains were declared.

The assessments for the tax years 5 April 2015 and 5 April 2016 were within the ordinary four-year time limit (s.34 TMA 1970).

By not taking any steps to declare his income and gain, the Tribunal found that he had been negligent, meaning that the four-year limit was validly extended for raising the discovery assessments for the years 2007/08 to 2013/14.

The First Tier Tribunal found that HMRC had made 'best judgment' assessments based on the information made available or obtained from other sources. Steven Hague had not provided any reliable, alternative basis to reduce the assessments in any way.

The assessments and penalties were upheld.

The appeal was dismissed.

Steven Hague v HMRC (TC09074)

HICBC and military service

Summary – The taxpayer had taken reasonable care so that two of the five years of assessments were cancelled. However, he did not have a reasonable excuse, meaning the penalties were upheld in full.

Until 2014, Paul Baron was in the army and did not have any children of his own. When he moved out of army accommodation, he moved in with his partner who, since November 2009, had been claiming Child Benefit in respect of her children from a previous relationship. Paul Baron claimed he was not aware of this.

Prior to 2015/16 Paul Baron was not required to notify his liability to tax to HMRC or submit a Self Assessment tax return.

On 8 January 2021, HMRC issued a letter to Paul Baron highlighting the High Income Child Benefit charge (HICBC) and giving some explanation of when it applied.

This was followed up with a letter sent in June 2021 explaining that they considered that he was liable to HICBC in 2015/16 through to 2019/20. This letter included a calculation of the amount of the HICBC and the risk of penalties, including a failure to notify penalty.

HMRC issued discovery assessments totalling £3,258, covering 2015/16 to 2019/20 for liability to income tax relating to the higher income child benefit charge and penalties of £517 for failure to notify liability to the charge.

Paul Baron appealed arguing that:

- he did not have any children of his own and when the advertising campaign was launched by HMRC in 2013/14, he was a single man in the army, often away on operations;
- he did not know that the HICBC existed;
- HMRC should have made him aware of the problem well before the five years of assessments were issued;
- he had always been taxed through PAYE and had no reason to consider whether he had to submit Self Assessment tax returns.

Decision

The First Tier Tribunal confirmed there was no dispute about the facts or calculations.

At the hearing, HMRC accepted that the initial advertising campaign would not have been relevant to Paul Baron and he would not have been aware of the HICBC at that time. The First Tier Tribunal concluded that he would have become aware of the charge on receipt of HMRC's letter dated 8 January 2021.

The discovery assessments made in relation to 2017/18 to 2019/20 were made within the standard four-year time limit. During these years, he was liable for the HICBC and those discovery assessments were upheld.

The discovery assessments made in relation to 2015/16 and 2016/17, relied on the extended six-year time limit (s.36(1) TMA 1970), which requires Paul Baron to not to have taken 'reasonable care'

to avoid the insufficiency of tax. Given his ignorance of the HICBC until January 2021, he had taken 'reasonable care' in the two tax years 2015/16 and 2016/17. HMRC were not entitled to rely on the extended time limits for the assessments for those two years and those assessments were cancelled.

The Tribunal found that the penalties for failure to notify were validly issued but did Paul Baron have a reasonable excuse for his failure to notify liability to HICBC?

The Tribunal had already concluded that he had taken reasonable care but went on to consider when his 'excuse' ended and whether the failure was then remedied without unreasonable delay.

Having become aware of the potential for HICBC in January 2021, it was not objectively reasonable for Paul Baron to take no further action until after the letter that he received in June 2021. This was an unreasonable delay and consequently the Tribunal found that he had no reasonable excuse for the failure to notify. The penalties were upheld.

Mr Paul Barron v HMRC (TC09053)

SEIS denied

Summary – With the existence of disqualifying arrangements, HMRC were correct not to issue the company with compliance certificates for the Seed Enterprise Investment Scheme.

CHF Group raised funds for programmes through a "fund" under which third-party investors were invited to subscribe for shares in special purpose investee companies, each of which held the intellectual property rights to a particular concept or show.

The CHF Group raised funds from third-party investors who subscribed for shares representing 50% of the voting rights and economic equity in a special purpose investee company with the group's parent company, CHF Media Group Limited, holding the other 50%. Each company held the intellectual property rights to a programme or project.

Coconut Animated Island Limited (CAIL) was one such special purpose investee company, formed in May 2017 to exploit the intellectual property rights of a pre-school animation programme called Coconut Bay and related spin-offs.

The company made an advance assurance application to HMRC that the shares issued would qualify under the SEIS and in October 2017, HMRC confirmed that, on the basis of the information supplied, HMRC would authorise the company to issue compliance certificates to individual investors.

The agreement was entered into in July 2018 with substantially the same terms as those in the draft provided to HMRC. Under that agreement, the company would pay another CHF Group company for production services.

A month later, HMRC advised the company of the new risk-to-capital condition requirement being introduced for shares issued on or after 15 March 2018. Later, HMRC informed the company of their decision to refuse to authorise the issue of compliance certificates in respect of shares issued between 19 March 2018 and 5 April 2018.

The company appealed to the First Tier Tribunal who found that the company had met both risk-to-capital condition 'to grow and develop its trade in the long term' and the 'qualifying company requirement'.

However, the appeal failed as the First Tier Tribunal found that the shares were issued under 'disqualifying arrangements' as the money raised was 'paid to or for the benefit of a relevant person' meaning it was spent in consequence or anticipation of a disqualifying arrangement. The Tribunal stated:

“We cannot see how it is possible to reach a contrary conclusion on the facts in this case given the extensive involvement of members of the CHF Group in virtually every aspect of the ‘arrangements.’”

Coconut Animated Island Limited appealed to the Upper Tribunal on the grounds that Condition A was not met because the First Tier Tribunal had erred in law.

Decision

The Upper Tribunal confirmed that ‘Condition A requires that, as a result of the money raised by the share issue being spent on the qualifying trade, the whole or a majority of the amount raised by the share issue is, in the course of the arrangements, paid to or for the benefit of a relevant person.’

In determining whether Condition A was satisfied, the Upper Tribunal stated that they needed to address two issues.

1. What was the scope of any “arrangements” and were the sums raised by the share issue to which those arrangements related paid to CHF Entertainment Limited “in the course of” the arrangements?
2. Was CHF Entertainment Limited a relevant person in relation to those arrangements – i.e. was CHF Entertainment Limited a party to the arrangements or a connected person of a party to the arrangements?

The Upper Tribunal reviewed the arrangements with the CHF Group, finding that the group was heavily involved in the arrangements. At the time of the share issue these arrangements included the:

- incorporation of Coconut Animated Island Limited;
- acquisition by Coconut Animated Island Limited of the intellectual property from Mr Fenna, who conceived Coconut Bay and was the creative director of CHF Entertainment Limited;
- raising of funds by Coconut Animated Island Limited by the issue of shares to the investors in the CHF Fund, which included the group;
- agreement between Coconut Animated Island Limited and CHF Entertainment Limited for the production services to be provided by CHF Entertainment Limited.

It was accepted by the parties that the bulk of the proceeds of the relevant share issues were paid by Coconut Animated Island Limited to CHF Entertainment Limited for production services.

The Upper Tribunal concluded that CHF Entertainment Limited was a party to the arrangements and found that an amount representing the whole or the majority of the amount raised under SEIS was, as part of the arrangements, paid to or for the benefit of a relevant person or relevant persons.

The company's appeal was dismissed.

No unconditional contract

Summary – With 'insufficient certainty as to the terms of the purported agreement prior to 3 December 2014', the taxpayer had failed to establish that any contract was made between her and her close company for the disposal of the goodwill before that date.

Frances Delaney owned and ran two nursery schools from church premises under personal licences. Her business gained reputation and grew. In order to protect herself from personal liability and with the aim of ultimately selling her business, she was advised to transfer her business to a limited company.

In 2012, with her two church licences due to expire in 2014, she began to renegotiate with the church diocese and as part of those negotiations the possibility of a transfer of the business to a limited company was discussed. In order to facilitate incorporation, the existing personal licences would need to be replaced with the granting of leases to the new company.

Miss Delaney's Nursery Schools Limited (MDNSL) was incorporated in November 2013, with Frances Delaney as sole director and shareholder.

Correspondence with the churches confirmed that she was "looking to operate (her business) under a corporate structure in the future" but no business sale agreement was ever drafted.

In November 2013 Frances Delaney started to investigate alternative premises, which were found and terms agreed in December 2013. However, the landlord withdrew in January 2014. Under the circumstances, Frances Delaney continued negotiations with the church and the personal licences which were renewed as an interim measure for the period through to 31 August 2014.

Negotiations were re-opened with the alternative landlord, with more suitable premises offered. Planning permission was needed for change of use from residential use and if granted, the property then needed to be inspected and registered with OFSTED.

An underlease was agreed on 9 September 2014, with MDNSL responsible for applying for "Planning Consent". If such Planning Consent was not granted the company was entitled to give one month's notice of termination of the lease.

Planning consent was granted on 11 December 2014 and the company began to make the changes necessary in order to run a nursery school from the property. Frances Delaney, in her capacity as director, decided not to make the application for OFSTED registration as a new provider of nursery school education until completion of the building works, enabling the entity and property registrations to be made and considered at the same time. The appointed head teacher spent the period from January to September 2015 overseeing the works to the new property and the preparation and submission of the OFSTED applications. The company and the property were both duly registered in July 2015.

Frances Delaney claimed entrepreneurs' relief on the gain on disposal of her nursery business, including goodwill, to her close company.

However, HMRC issued a closure notice stating that entrepreneurs' relief was not available on the disposal of goodwill, as there was no unconditional contract for disposal in place prior to 3 December 2014.

Frances Delaney appealed arguing that the unconditional contract for the disposal was made in September 2014.

Decision

The First Tier Tribunal confirmed that prior to 3 December 2014 a taxpayer who disposed of a business, including goodwill, to a limited company to which they were connected was entitled to claim entrepreneurs' relief. However, following a change in law, entrepreneurs' relief is denied on any such disposal occurring after 3 December 2014 (s. 169L TCGA1992). So, the issue to decide was whether there was an unconditional contract for the disposal of the business in place before 3 December 2014.

The First Tier Tribunal stated that the extended personal licences and the break clause in the lease enabled the Frances Delaney to keep all her options open for the running of the business until she had certainty that she could transfer the business to company who would then be able to operate it.

The First Tier Tribunal found that by 3 December 2014 the company had been incorporated, it had entered into a lease agreement and it had employed a head teacher. However, these were preparatory steps only and by 3 December 2014 there was no written contract or definite intention that Frances Delaney would incorporate her nursery business as both Planning consent and OFSTED registration were outstanding. Further, the Tribunal stated that:

“most significantly there was, at that point, no agreed mechanism by reference to which the consideration payable for the transfer would be determined and thereby there was a lack of certainty that MDNSL would acquire and at what price (or how such price would be determined).”

The appeal was dismissed.

Frances Delaney v HMRC (TC09101)

Tax liability when bankrupt

Summary – The gain arising on the exercise of a property option was taxable on the taxpayer as he had remained the beneficial owner throughout, despite the property being vested in his trustee in bankruptcy for a number of years.

On 31 July 1997, Edward Newfield inherited a property, valued at £55,000, from his mother.

Two and a half years later, having been declared bankrupt, beneficial ownership of the property vested in his trustee in bankruptcy. After three years, in February 2003, he was discharged from bankruptcy.

Bankruptcy related restrictions remained in the property until 2016, when they were removed.

On 4 May 2016, Edward Newfield granted an £1 option to a company, Choiceplace Properties Limited, to buy the property for £215,000 and in September 2016 the option was exercised.

Edward Newfield did not declare a capital gain on his Self Assessment tax return as he argued that he was only liable to CGT while he was the beneficial owner of the property. Given that he had only reacquired ownership of the property a short period before its disposal date, there was no increase in value.

HMRC disagreed and, following an enquiry, sought to charge tax on the gain with proceeds on exercise being the £215,000 paid plus the £1 paid for the option at grant. The cost of acquiring the asset was an allowable deduction.

The issue in this case was who was liable to the capital gains tax?

Decision

The First Tier Tribunal stated that it was not clear when, following his discharge from bankruptcy, the property reverted in Edward Newfield. However, this was not relevant for capital gains tax purposes as s.66(1) TCGA 1992 clearly covered the matter. It stated:

“In relation to assets held by a person as trustee or assignee in bankruptcy or under a deed of arrangement this Act shall apply as if the assets were vested in, and the acts of the trustee or assignee in relation to the assets were the acts of, the bankrupt or debtor (acquisitions from or disposals to him by the bankrupt or debtor being disregarded accordingly), and tax in respect of any chargeable gains which accrue to any such trustee or assignee shall be assessable on and recoverable from him.”

For CGT purposes, bankruptcy does not affect the ownership of assets as the bankrupt is to be treated as holding the relevant assets throughout the period when ownership of the assets is vested in the trustee in bankruptcy.

The appeal was dismissed.

Edward Newfield v HMRC (TC09058)

Converted barn and paddock

Summary – A converted barn bought with a paddock was found to be entirely residential property, meaning that the SDLT mixed-use rates did not apply.

On 20 December 2021 Jessica Harjono & Yusdi Santoso bought a property consisting of a converted barn with three acres of land. Roughly half of the land was a fenced paddock with gates to the garden and also to the main access road.

The paddock was subject to a grazing agreement that was in place at completion and the taxpayers believed this to be a commercial arrangement. Consequently, an SDLT return was submitted and tax paid on the basis that the property was mixed use, with the lower rates of tax being paid.

Following an enquiry, HMRC concluded that the grazing agreement was not in place at the effective date and even if it was, it was a barter of convenience, and the paddock was still part of the grounds of the dwelling. HMRC issued a closure notice on the basis that the higher residential rates applied and sought to collect an additional £113,250 of SDLT.

The taxpayers appealed.

Decision

The First Tier Tribunal concluded that the grazing agreement was in place at completion but, having taken all the facts and circumstances into account, it still constituted part of the grounds.

The Tribunal referred to the word commercial as being a “weasel” word stating:

"In mixed-use situations it is increasingly being asserted that any letting of part of a property for a market rent is commercial and, as if by magic, the land leaves the residential pot and turns up in the mixed-use pot. As the cases show, this simplistic analysis is being rejected by the courts."

The Tribunal went on to say:

"What is of greater significance in these sorts of situations is the use to which the land is ultimately put and whether that use is inconsistent with the householders' use of the dwelling as such."

The three-acre plot that included the paddock was "consistent and proportionate to the size and nature of the house and garden", with access to the paddock from the garden. The paddock was a selling point for the house and gardens.

It was part of the "wonderful outside space for families and friends to enjoy". Despite the land registry showing two titles, the property was bought in a single transaction, with the paddock having been used since 2009 as part of the house and garden.

The appeal was dismissed.

Jessica Harjono and Yusdi Santoso v HMRC (TC09107)