

Business tax update (Lecture B1456 – 24.34 minutes)

SEISS, CJRS or nothing?

Summary – As a director who performed work during the pandemic, the taxpayer was not entitled to COVID related payments of any kind.

Until 5 February 2019, Sofia Lorenzo operated as a self-employed, semi-permanent, makeup and beauty therapist. From that date the business was incorporated, with her becoming an employee, sole director and shareholder.

During COVID she applied for and received coronavirus support payments under the Self-Employed Income Support Scheme (SEISS).

HMRC raised assessments to reclaim the payments made because, as an employee, she had no entitlement under the SEISS as she was not self-employed.

Despite later accepting that she was not eligible for the sums received, she appealed HMRC's assessment on the basis that:

- she had received payments under SEISS because of an innocent mistake; and
- as an employee, she should have been entitled to receive payments funded through the Coronavirus Job Retention Scheme (CJRS);
- her CJRS payments would have been greater than the amounts paid under SEISS.

She sought to have her SEIS payments treated as if they had been valid payments under CJRS. However, the witness statement and skeletons identified that it was not clear that the company would have been entitled to make CJRS claims and so there was a factual and legal dispute which needed to be determined.

Decision

The First Tier Tribunal found that, had a claim been made under the CJRS, for a number of reasons it would have been invalid. The reasons included that during the pandemic:

- the company did not pay her a salary;
- she had performed some duties during the furlough period, beyond the directors' duties permitted under the CJRS rules.

The appeal was dismissed.

Sofia Lorenzo v HMRC (TC09227)

Entitlement to SEISS and bounce back loan

Summary – As the taxpayer was no longer trading on a self-employed basis, he was not entitled to claim under the Self Employment Income Support Scheme.

Ali Sadiq Jaafar traded as a self-employed minicab driver for a number of years before ceasing on 30 September 2019, a date confirmed in his Self Assessment return as well as separately by his agent in writing.

On 12 September 2018 he became the sole director and shareholder of a newly incorporated company, Fly Services Limited, which filed dormant accounts for the year to 30 September 2019 and micro company accounts for subsequent periods.

Ali Sadiq Jaafar applied for and received three payments under the Self Employment Income Support Scheme (SEISS) in June, September and December 2020. He argued that he had in fact continued to trade on a self-employed basis in the 2020/21 tax year.

HMRC accepted that being a company director did not prevent him resuming self-employment but stated that no evidence was provided supporting his claim that he did so in 2019/20 or later years. His 2020/21 return only showed the support payments and expenses and nothing was reported in 2021/22.

Consequently, HMRC contended that Ali Sadiq Jaafar was not entitled to claim under the SEISS as he did not meet the requirements which were that he must have:

- carried on a trade, the business of which had been adversely affected by Coronavirus; and
- intended to continue to carry on a trade in the tax year 2020/21.

Consequently, HMRC raised assessments to recover the three payments previously made.

Ali Sadiq Jaafar appealed.

Decision

The First Tier Tribunal acknowledged that Ali Sadiq Jaafar had provided copies of his TfL private hire driver's licences with expiry dates 8 December 2020 and 17 January 2024, and the V5C and MOT certificates for a Mercedes Benz car in his name as well as copies of his car insurance. However, the Tribunal did not accept that these were sufficient to show that he was self-employed in the period in question:

- he would have needed the same licences to be able to drive as an employee;
- the fact that he had owned the car in his own name, rather than transferring it to the company, did not mean that he must have been self-employed; and
- his car insurance showed that he was insured to drive the car for social, domestic and pleasure purposes only;
- his company, Fly Services Limited, had applied for and been granted a bounce back loan, the terms of which required that the company had to be trading as a limited company. This was not consistent with his claim that he had continued in self-employment and had not traded through the company.

While his bank statements did show 'some small payments from Ontime Chauffeurs', the First Tier Tribunal found that there was no documentation to indicate in what capacity these had been received.

In conclusion, the First Tier Tribunal found that Ali Sadiq Jaafar had ceased self-employment on 30 September 2019 and had no intention to 'continue to carry on' as self-employed in 2020/21. Consequently, he was not entitled to support payments.

The appeal was dismissed

Ali Sadiq Jaafar v HMRC (TC09279)

CIS determinations challenged

Summary – The First Tier Tribunal dismissed the company's appeal against determinations relating to its failure to make deduction at source under the CIS legislation. The appeal against late filing penalties were also dismissed.

The Oaks (Gatley) Limited was set up to carry out a one-off residential development project. As part of that project the company paid various construction service providers, failing to make deductions at source as required by the CIS rules.

Despite accepting that it had failed to make the deductions, the company appealed against HMRC's determinations issued to recover the tax relating to one sub-contractor, Dreamspace, arguing that HMRC had not followed its own Regulations when raising the determinations.

Regulation 9 states that an HMRC officer may direct that a contractor is not liable to pay any shortfall between the amounts it should have deducted under CIS and the amounts actually deducted if the sub-contractor brings into account the payments made to it. On appeal, the company included a letter from Dreamspace confirming that it had brought all amounts received from *Oaks (Gatley) Limited* into account in calculating its corporation tax liabilities. Consequently, there was no net loss of tax to HMRC.

Decision

The First Tier Tribunal found that it had jurisdiction to consider whether CIS deductions were due as well as the quantum of such deductions.

The Tribunal acknowledged that HMRC's Compliance Operational Guidance manual does indicate that officers should consider the overall tax/regulation 9 position before moving forward with a regulation 13 determination.

COG909400 makes it clear that:

"you must always consider all the information you hold in respect of possible claims [for relief under regulation 9] prior to the issue of regulation 13(2) determinations".

Although the company asserted that there was no tax loss, the Tribunal stated that there was no material evidence supplied to support that assertion.

The Tribunal stated:

"Saying that HMRC could work out the sub-contractors' UTRs for themselves and find the required information is not sufficient."

The Tribunal went on to say:

“In the circumstances, if public law arguments could have been introduced, we would have held, on the basis of the evidence before us, that HMRC did not depart from the process they outlined in the Manual or, if they did, they did not do so in a way which is conspicuously unfair to (the company).”

The appeals were dismissed.

The Oaks (Gatley) Limited v HMRC (TC09233)

Mis-selling of interest rate hedging products

Summary – The redress payments put the taxpayers back in the position they would have been in but for the mis-selling in relation to their property rental business. These payments were revenue in nature and taxable as part of the property rental business.

Simon and Edward Hackett were brothers who ran a property business.

In 2006, they bought interest rate hedging products from HSBC and RBS to help manage fluctuations in interest rates on loans.

It was later agreed that some of these products had been mis-sold and the Financial Conduct Authority set up a compensation scheme to put customers back in the position they would have been in had the mis-sale not taken place.

Simon and Edward Hackett received compensation but did not include these sums in their Self Assessment tax returns as trading receipts.

Following an enquiry, HMRC issued closure notices assessing them to tax on the payments.

The Hackett brothers appealed, arguing that the payments were for the cost of lost opportunities of being able to enter into different hedging products and, as a result were not part of the profits of the property business. This meant that, under s.271 ITTOIA 2005, the payments were not liable to income tax and the interest was not chargeable under s.369.

Decision

The First Tier Tribunal did not agree, finding that the compensation was for business expenditure on the mis-sold interest rate hedging products. The brothers were not put in a better position but were put back in the position they would have been had it not been for the mis-sold products. Both the compensation and interest were liable to tax. The appeal was dismissed

Simon and Edward Hackett v HMRC (TC09267)

Adapted from the case summary in Taxation (8 August 2024)

R&D claim for sub-contractor costs

Summary – Although creation of a director’s loan constituted payment, there was a lack of evidence to support the claim that this was qualifying R&D.

Tills Plus Limited developed technology for the hospitality industry and in this case, a virtual hospitality manager using Artificial Intelligence and Big Data.

The company wanted to develop a new product or suite of products, the funding for which was to come from the sole director's father-in-law, who was resident in Iran.

Due to international sanctions, it was extremely difficult to move money out of Iran. Consequently, the company looked for a partner in Iran to carry out the necessary development work, choosing a company called iWond as they had the necessary expertise and had the best English language capabilities.

The agreement between iWond and Tills Plus Limited did not set out any specific fees for the work but simply provided that Tills Plus Limited would be invoiced every three months.

Due to the difficulties in moving money in and out of Iran, it was agreed that iWond's invoices would be paid direct by the father-in-law from his bank account in Iran, who would make a loan to the UK director who would in turn make a loan, recorded on a director's loan account, to Tills Plus Limited. The loans were interest free and repayable on demand but was only put in writing once HMRC's enquiries had begun.

Tills Plus Limited submitted claims for research and development expenditure, including subcontractor costs, for the years 2018 and 2019.

- For 2018, a tax credit payment of just over £390,000 was claimed and paid by HMRC;
- For 2019, a tax credit payment of a little over £275,000 was claimed but HMRC did not pay this

Following an enquiry, HMRC concluded that both claims should be disallowed and sought to recover the £390,000 already paid. S.1133(1) CTA 2009 defined a "sub-contractor payment" as "a payment made by a company to another person (the 'sub-contractor') in respect of research and development contracted out by the company to that person". HMRC argued that the sums claimed had not been paid as to be eligible, the invoices needed to be paid from the company's bank account to the subcontractor company in Iran.

Tills Plus Limited appealed.

Decision

The First Tier Tribunal considered whether the expenditure:

- had actually been 'paid';
- was qualifying R&D expenditure.

On the payment issue:

- The company argued that it would be very odd if a payment did not satisfy the requirements of the legislation simply on the basis that there was no physical payment by the company to the sub-contractor;
- HMRC argued that there was a difference between payment by credit card and a payment using borrowing where the actual payment to the sub-contractor was made by the lender rather than the borrowing company.

The Tribunal concluded that it could not have been Parliament's intention that the availability of relief should depend on fine distinctions as to the way in which a payment was made to a sub-contractor. The First Tier Tribunal agreed with the taxpayer, who could see no avoidance or abuse taking place where the debt was settled by the loan arrangement. The Tribunal concluded that what was required was that an obligation to the sub-contractor was discharged at the cost or expense of the company, which is what happened here:

- iWond's invoices were addressed to Tills Plus Limited and were therefore an obligation of Tills Plus;
- The invoices were physically paid by the father-in-law but this was treated by agreement as a loan from him to the director and then a loan by the director to Tills Plus Limited.

This meant the obligation to iWond represented by the invoice was discharged and was replaced by an obligation for Tills Plus Limited to repay the resulting loan, so at the cost or expense of Tills Plus Limited.

It did not matter that it was not a commercial loan, with no interest and no fixed date for repayment. The Tribunal did not consider that the reasons why payment was made in a particular way was relevant to the issue of statutory interpretation.

Unfortunately for the company, the First Tier Tribunal went on to conclude that there was insufficient evidence to show the company had carried out qualifying R&D. One report being relied on was found to contain an expert's opinion/ assertion but he was unavailable to give evidence to support the claims or be cross-examined. The Tribunal stated that it was possible that the work could constitute qualifying R&D but evidence was lacking and 'without further evidence, we cannot say that what was being done would be acknowledged by a competent professional working in the field as a genuine and non-trivial improvement'. With the company failing to provide a satisfactory explanation of the advance in technology being sought, the claim failed.

Tills Plus Limited v HMRC (TC09235)

Reallocation of Special Capital

Summary - Allocations by a corporate member of a mixed member partnership to individual members constituted miscellaneous income.

An investment management business, GSA, transferred its high-frequency foreign currency trading team to the HFFX LLP, a mixed partnership LLP whose members were:

- Individual members of the trading team who became self-employed LLP partners;
- GSA Member Ltd, a company that was independent of the individual members.

HFFX LLP's business was to second members of the team to GSA Capital Partners LLP, GSA's primary trading entity.

Individual LLP member received payouts from the profits they earned for GSA, but a substantial proportion was deferred via a "Capital Allocation Plan".

Under this plan:

- 50% of the pay-out that the team would otherwise have received was allocated to GSA Member Ltd, who invested these sums in funds managed by GSA;
- On the first, second and third anniversaries of the allocation, the corporate member sold a third of the investments, contributing the net proceeds back to HFFX LLP as "Special Capital";
- The corporate member then decided to reallocate the Special Capital to individual members, who were able to withdraw it.

The scheme was designed with the intention that:

- the corporate member would be taxed at corporation tax rates on the amounts allocated to it (rather than the higher income tax rates to which individual members would be subject if the profits were allocated to them);
- the subsequent reallocation of Special Capital would not give rise to tax for the individual members.

HMRC disagreed, stating that the reallocated special capital was taxable as miscellaneous income under s.687 ITTOIA 2005.

The First Tier Tribunal and Upper Tribunal found in favour of HMRC.

The individual members appealed. It was not disputed that the amounts were income in the hands of the individual members. The central issue was whether that income had a source. The members argued that the corporate member's discretion to reallocate Special Capital was purely voluntary, which meant that it did not constitute a source of taxable income.

Decision

The Court of Appeal agreed with HMRC that the case was 'materially indistinguishable' from *BlueCrest Capital Management LP and others v CRC* [2024] STC 92, in which the court decided the miscellaneous income issue in HMRC's favour.

The deciding factor was that the individual members had legal '*rights under the Partnership Deed*' for the corporate member to reallocate Special Capital to the individual members.

This was enough to make such receipts taxable as miscellaneous income under s.687. The receipts were not a 'pure gift'.

The taxpayers' appeal was dismissed.

HMRC v HFFX LLP [2024] EWCA Civ 813

Apple State Aid case

Summary - The Court of Justice of the European Union (CJEU) has overturned the General Court's 2020 ruling in the Apple State Aid case. The decision reinstates the European Commission's 2016 ruling that Ireland provided illegal State Aid to Apple and therefore confirms that the company should repay €13bn in taxes to Ireland.

Explaining the background to the judgment, Heather Self, tax consultant at Blick Rothenberg, said: 'Ten years ago, in June 2014, the EU Commission announced an investigation into rulings issued by Irish tax authorities on the calculation of the taxable profits allocated to the Irish branches of two

companies, Apple Sales International (ASI) and Apple Operations Europe (AOE). ASI and AOE were incorporated, but not tax resident, in Ireland. In both cases, the Irish branches declared low profits, claiming that the profits relating to intellectual property were attributable to the head office and not taxable in Ireland. However, due to the interaction of Irish and US tax rules at the time, the profits were not taxed anywhere.

'In a decision in 2016, the Commission said that the rulings allowed profits from 1991 to 2014 to be calculated in a way “that did not correspond to economic reality” and said that this was State Aid. They ordered Ireland to recover €13bn from Apple. Both Ireland and Apple appealed, and in 2020 the General Court annulled the Commission's decision, holding that the Commission had not sufficiently established that ASI and AOE enjoyed a selective advantage. The Commission appealed to the Court of Justice (ECJ).

Self said: 'On 10 September 2024, the CJEU has now issued its final ruling. The decision of the General Court has been overturned, and the Commission's original decision has been upheld. In particular, the CJEU held that the Commission was correct to compare the activities of the Irish branches with the head offices of ASI and AOE, and not to take into account the activities of other group companies such as Apple Inc.

'This is an important decision, even though it deals with events from some years ago and the Irish rules on tax residence have now been updated. In particular, the US warned in 2016 that the EU risked damaging international agreements on tax reform if it continued to act as a “supra-national tax authority”. The CJEU's decision that Europe should collect tax of this magnitude from Apple may push the US towards finally implementing the OECD's proposed reforms – or could have the opposite effect of causing Pillar One to collapse altogether,' Self added.

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