

Personal tax update (Lecture P1271 – 23.18 minutes)

Compensation allowance as earnings

Summary – Payment made to compensate an employee for the withdrawal of an ICT allowance was taxable as employment income.

Patrick McAllister was employed by the Commission of the Northern Ireland Assembly as an application development analyst managing a team of software developers. In addition to his salary, he was entitled to an ICT allowance of £5,640 per annum. This allowance was set out in a letter from the Commission to Patrick McAllister's Trade Union, and stated:

“...the purpose of the ICT allowance is to recognise the skills and competencies that are required of and exercised by staff in the ICT discipline and to reflect the need to have ICT skills available in order to meet service requirements outside normal office hours if required... . The ICT allowance is payable exclusively to staff who occupy posts that are within the ICT discipline and require the post holder to exercise particular ICT skills and competencies.”

Following a pay and grading review it was decided that there was no justification for paying an additional allowance for having ICT skills. Those receiving the allowance were predominantly men. Women, on the same grade in other disciplines were not receiving an allowance and the Commission was concerned about the possibility of equal pay claims being made.

Patrick McAllister received a lump sum payment of £44,860 in return for giving up his contractual right to the ICT allowance contained in his contract of employment. There was no commitment to remain employed by the Commission for any period of time beyond the date of the payment and there was no requirement to refund any of the payment if he left.

Patrick McAllister argued that the payment was an ex-gratia payment, with the first £30,000 being tax free. The payment was not made in return for any services past, present or future but rather it was paid so that the employer could avoid equal pay vulnerabilities. The only condition for the payment was the surrender of the ICT allowance.

HMRC argued that this sum was taxable earnings under s.62 ITEPA 2003 as an emolument of his employment.

Decision

The First Tier Tribunal found in favour of HMRC, concluding that the payment made derived from employment.

The payment was made to compensate for the loss of an allowance that had previously formed part of Patrick McAllister's salary. The payment was taxable as employment income, as it was paid solely for a change in the terms and conditions of his employment.

Patrick McAllister v HMRC (TC08181)

Termination payment and RTI

Summary – The taxpayer had taken reasonable care when completing his online tax return and a 'hypothetical officer' should have considered Real-Time Information to identify the tax discrepancy that existed.

Alan Loughrey had always paid income tax under PAYE and had never been required by HMRC to file a tax return.

In 2013 he was made redundant and, believing that too much tax had been deducted from his pay in 2013/14, he filed a tax return for that year using figures from his P45. No longer able to access his electronic payslips, he included a £30,000 deduction against his termination payment that he was entitled to. Based on this return, HMRC processed a £14,000 tax refund. However, unknown to him, Alan Loughrey's employer had already deducted the £30,000 from the P45 taxable pay figure, meaning the exemption had been claimed twice.

On reviewing the return using the real time information (RTI) held on HMRC's computer systems, HMRC identified this discrepancy and HMRC raised a discovery assessment in April 2018 to correct the matter. HMRC argued that the hypothetical officer would not have been aware of the insufficiency of tax from a review of the information on the tax return

Alan Loughrey appealed. He did not dispute HMRC's calculation, but rather he challenged whether HMRC had satisfied the requirements to be able to make a valid discovery.

Decision

The First Tier Tribunal found that when submitting his online tax return, Alan Loughrey had followed HMRC's instructions and deducted £30,000 from the P45 figure for the tax-free redundancy payment. He had not acted carelessly as the online guidance did not indicate that amounts for which the £30,000 exemption had already been given should be treated any differently. There was no suggestion in that guidance that he should seek further advice from either HMRC or a qualified professional.

HMRC should have been aware of the discrepancy, as it was aware of the existence of the real time information on his pay figure from his employer. This information would make it obvious to a hypothetical officer that there was an insufficiency of tax in respect of employment income. After all, it was HMRC's computer systems that initially flagged the discrepancy on the tax return using the RTI data to begin with and further, HMRC had used the RTI information when reviewing the correctness of the tax return.

The appeal was allowed.

Alan Loughrey v HMRC (TC08198)

Market value of shares gifted to charity

Summary – The Tribunal determined the market value of the shares gifted as being the highest price a reasonably prudent purchaser would pay for them.

These appeals are lead cases involving the valuation of shares in a company called Baa Bar Group Plc that were gifted to charity.

Neil McArthur invested in Baa Bar Group Plc in anticipation that it would purchase a business, with the shares in Baa Bar Group Plc then be floated on a stock exchange.

Thomas Bloxham began a business, Baa Bar Ltd, which he sold to Baa Bar Group Plc for some £12m cash, deferred consideration of £250,000 and shares in Baa Bar Group Plc.

Baa Bar Group Plc was floated on the Channel Islands Stock Exchange and since then, both taxpayers gifted shares to charity and claimed income tax relief based on the market value of the shares at the time of the gifts.

Following an enquiry, HMRC issued closure notices stating that the market value of the gifts was lower than the relief claimed.

The taxpayers appealed.

Decision

The First Tier Tribunal concluded that the market value was the highest price a reasonably prudent purchaser would pay, not the highest price a range of reasonably prudent purchasers might pay.

To arrive at the price that such a prudent purchaser would pay, the Tribunal acknowledged that expert valuers would come up with different estimates as demonstrated by the difference in values put forward by expert witnesses as follows:

	<u>Taxpayers'</u> <u>value</u>	<u>HMRC's</u> <u>value</u>
19 Feb 2007	108	8
13 Aug 2008	41	16
16 Oct 2009	56	16.5

The Tribunal noted that there was a significant divergence on valuation, due to the different views of the experts as to the information available to the hypothetical purchaser, different weight given to the various methodologies considered and different assumptions used in applying those methodologies. The Tribunal concluded that in reaching their decision, it was important to consider various valuations methods, taking into account the information available about the business, its current position as well as the company's future prospects.

In conclusion, the valuations were closer to those provided by HMRC's expert witness than the taxpayer's expert witness.

Neil McArthur and Thomas Bloxham (TC08186)

Information on foreign income and gains

Summary – Sch.36 Notices were 'reasonably required' but the Tribunal concluded that it did not have the jurisdiction to decide whether the taxpayer was UK domiciled at this stage.

Robert Perlman was born in Curaçao and had lived in the UK since at least 1967. Arguing that he was not UK domiciled, he claimed the remittance basis of tax.

HMRC opened enquires into his Self Assessment tax returns for the years 2014/15 to 2016/17 and in July 2019, notified him that they had decided he had a domicile of choice in the UK and so had not been entitled to claim the remittance basis.

They asked informally for information and document about his worldwide income and gains, so they could make consequential amendments to his tax returns and close the enquiries. However, Robert Perlman refused to provide that information, and so HMRC issued him with Notices under Sch. 36 Finance Act 2008.

Robert Perlman appealed the Notices on the ground that the information was not “reasonably required” because he was not domiciled in the UK. He argued that the information would only be reasonably required if HMRC had first proved he was not so domiciled. He requested that the domicile issue be decided as part of the appeal.

HMRC argued that the Tribunal did not have the jurisdiction to decide whether Robert Perlman was domiciled as part of an appeal against a Sch 36 Notice, and even if it did have that jurisdiction, it should decline to exercise it.

Decision

The First Tier Tribunal concluded that this appeal was against the issue of a Schedule 36 Notice, part of the ‘preliminary investigative stage’ of the enquiry. It is independent of any tax investigation. This appeal was limited to deciding whether the information requested was ‘reasonably required’ in order to check Robert Perlman’s tax position.

Referring to the case *Kotton v HMRC* and others, the Tribunal concluded that “reasonably required” meant that it was only necessary that there be a “rational connection” between the enquiry and the information required by the Notice. The Tribunal found that the Notices were reasonably required.

The Tribunal found that the determination of Robert Perlman’s domicile was beyond the jurisdiction of the appeal. With no right for the losing party to appeal a Sch. 36 Notice, if the Tribunal did have jurisdiction to decide Robert Perlman’s domicile status at this stage, the losing party would have no right to appeal the decision, and that would be ‘a surprising outcome’.

The Tribunal went on to say that ‘the lack of an appeal right following Sch. 36 hearings is entirely consistent with the limited and preliminary role played by Sch 36 within the statutory framework.’

Alternatively, the First Tier Tribunal found that if it did have jurisdiction, it should not exercise it in these circumstances. The Tribunal stated that:

‘Given that a domicile dispute often involves many days of contested witness evidence, it would not be in the interests of justice for the Tribunal to exercise that occasional jurisdiction in Mr Perlman’s appeal against the Notices.’

The appeal was dismissed.

Robert Perlman v HRC (TC08168)

Bonuses to LLP members

Summary – Bonus payments made to five LLP members were remuneration relating to former employment and so liable to income tax and Class 1 NIC.

Charles Tyrwhitt LLP is a limited liability partnership operating as a clothing retailer. In 2008, the partnership set up a bonus scheme for its directors and other senior management known as the Long-term Incentive Plan. Under the plan, once certain conditions had been met, eligible employees became entitled to bonuses, calculated by reference to the LLP’s profits over a period

when the individual had been an employee. To be eligible, individuals must still be employed or not have left as a 'bad leaver'.

Under the original terms, becoming an LLP member could have meant that the individual was classed as a bad leaver and so would lose their entitlement. Consequently, the terms were changed so that eligibility was based on being either an employee or a member. A new clause was included that stated that the partnership would pay the relevant tax and NIC, depending on whether the individual was an employee or a member at the time of payment.

Five individuals were admitted to the plan when they were employees but later became LLP members, receiving bonuses under the scheme at that time:

- Charles Tyrwhitt LLP claimed that the payments were made to the individuals in their capacity as LLP members, and so should be treated as a share of the LLP profits, subject to income tax and Class 4 NIC;
- HMRC argued that the payments should be taxed as deferred employment income, subject to income tax and Class 1 primary and secondary NIC.

The First Tier Tribunal agreed with HMRC, confirming that the scheme was for the benefit of employees and the bonus payments were in respect of their employment. The bonus was received because the individuals had been eligible employees and not because they were members of the partnership.

Charles Tyrwhitt LLP appealed to the Upper Tribunal.

Decision

The Upper Tribunal concluded that the individuals had two different roles with the partnership — initially as employee and then later as a member of the LLP.

No evidence was provided to confirm that the partnership had agreed with its members that the bonus payments would represent part of their profit. The changes that had been made to the scheme merely ensured that the employees would not lose their right to the bonus on becoming members of the LLP.

The Upper Tribunal agreed with the First Tier Tribunal. The individuals received the bonus payments in their capacity as former employees. The bonus payments were contingent on the employees' contractual requirements being met and so should be taxed as employment income, even though the individuals received them after the employment had ceased.

The payments were derived from their employment and the appeal was dismissed.

Charles Tyrwhitt LLP v HMRC [2021] UKUT 0165 (TCC)

Multiple dwellings relief and historic use

Summary – The Upper Tribunal confirmed the First Tier Tribunal's decision that Multiple Dwellings Relief was not available for the purchase of a house with an annexe that may or may not have been used as separate properties in the past.

On 27 April 2016 the taxpayers bought a detached property with an annexe, a garage and a summer house for £575,000. They made a claim to reduce the SDLT due on the property by £10,000 on the basis that the acquisition qualified for multiple dwellings relief.

The annexe contained a sitting room, kitchen/utility room, bedroom and shower room. The annexe could be accessed either from outside via its own doors or by using a corridor which was connected to the main house. The annexe did not have its own separate postal address, council tax or utility supply. There was also a restrictive covenant over the land to prevent more than one bungalow being built on it.

HMRC opened an enquiry into the SDLT return and in August 2018 issued a closure notice amending the return denying the multiple dwellings relief.

On appeal, the First Tier Tribunal agreed with HMRC finding that, although the property had the facilities for the occupant to sleep, eat and wash in the property, it lacked the privacy and security required to be treated as a separate dwelling.

Keith Fiander and Samantha Brower appealed to the Upper Tribunal on the grounds that the First Tier Tribunal had failed to take into account oral evidence given by Samantha Bower and that it had erred in law in reaching the conclusions that it did. The couple claimed that from her evidence, it was clear that when they viewed the property for sale and at completion, that the two buildings had initially been physically separated and only later joined by a brick corridor with two internal doors between the main house and the annexe. HMRC did not recall this evidence.

Decision

There was no written or recorded evidence supporting her claim and so the First Tier Tribunal's findings of fact could not be displaced and her oral evidence was considered inadmissible.

However, even if the evidence had been admissible, it would not have affected the outcome as what mattered for SDLT was the use of the buildings at completion, and not their use in the past.

The Upper Tribunal concluded that the First Tier Tribunal were correct and there had been no error in law.

The case was dismissed.

Keith Fiander and Samantha Brower v HMRC [2021] UKUT 0156 (TCC)

Enquiry notice validity

Summary –HMRC sending an enquiry notice to the wrong address did not render the enquiry invalid as the taxpayer's advisers acknowledged and acted on the enquiry.

Under ss.9A and 15 TMA 1970, HMRC must give notice of an enquiry into a taxpayer's tax return by sending it addressed to the taxpayer's usual or last known place of residence, or their place of business or employment.

In early 2005, HMRC received two documents showing Mr Tinkler's address as Station Road:

1. Form 64-8 on the appointment of BDO Stoy Hayward (BDO) as his agent;

2. Mr Tinkler's 2003/04 Self Assessment Tax Return.

As a result, HMRC amended the address that was held on their system to show the Station Road address rather than the address at Heybridge Lane where Mr Tinkler had previously been living in a rented house.

For reasons that were not stated, on 1 July 2005, HMRC incorrectly changed the address back to Heybridge Lane and that same day, sent two letters:

1. A notice of enquiry into Mr Tinkler's 2003/04 Return to Heybridge Lane;
2. A letter to Mr Tinkler's accountants and tax advisers, BDO Stoy Hayward (BDO), informing them of the enquiry and raising a number of questions about his tax affairs. It included a copy of the notice that had been sent to Heybridge Lane.

BDO replied to HMRC by letter on 6 July 2005, confirming that BDO would respond to the questions raised in relation to capital gains by 22 August 2005 as requested by HMRC. BDO also referred to a "gilt strip loss" which had mistakenly not been included in the Return. If taken into account, BDO asserted that Mr Tinkler had suffered an income tax loss for 2003/04 of some £2.5m but it pointed out that it could not amend the Return "as the Return is now the subject of a section 9A TMA 1970 enquiry". A repayment of tax overpaid by Mr Tinkler was nevertheless sought which BDO stated amounted to £605,319.58 (plus £30,265.98 in overpaid surcharge). HMRC responded by letter dated 12 July 2005, noting the gilt strip loss claimed but saying that "no repayment will be made until after the enquiry has been concluded".

Correspondence continued between HMRC and BDO, during which time HMRC were informed that Mr Tinkler no longer used the Heybridge Lane address and on 1 November 2005, HMRC corrected the address recorded in their system to Station Road.

HMRC finally issued a closure notice in August 2012, denying the losses and stating that Mr Tinkler owed just over £700,000 in tax.

At this time, Mr Tinkler argued that the closure notice was invalid because the initial notice of enquiry had been sent to Heybridge Lane, which was neither his usual or last known place of residence, nor his place of business or employment.

HMRC argued that as Mr Tinkler and his agent had corresponded with HMRC on the shared assumption that the enquiry was validly opened, he was estopped from challenging that assumption.

The First Tier Tribunal and Upper Tribunal dismissed Mr Tinkler's appeal but the Court of Appeal allowed it.

HMRC appealed to the Supreme Court.

Decision

The Supreme Court considered the principles governing estoppel by convention in *CRC v Bendchollar* [2009] STC 2342 and concluded that by replying and engaging with HMRC's enquiry process, BDO had confirmed that they were acting on the shared assumption that the enquiry had been validly opened.

Had HMRC not relied on the common assumption, and objections to the enquiry notice were raised at the start, HMRC could have issued an alternative notice with the new address. Waiting over nine years to raise the issue was not acceptable.

Lord Burrows concluded by saying:

“Standing back from the detail, what Mr Tinkler and his advisers have done is to take at a late stage what can fairly be described, on the facts of this case, as a technical point (that the notice of enquiry was sent to the wrong address) even though that has not caused Mr Tinkler any prejudice. It is entirely satisfactory that, by reference to estoppel by convention, the law has the means to avoid such a technical point succeeding.”

HMRC's appeal was allowed.

Tinkler v HMRC [2021] UKSC 39