

## Personal tax (Lecture P1471 – 16.31 minutes)

### Loan account was employment income

*Summary - £4,500,000 left on a loan account following incorporation should have been taxed as income rather than a gain eligible for entrepreneurs' relief.*

This case concerned Rupert Grint, the actor who played Ron Weasley in the Harry Potter films.

Based on advice from Clay & Associates LLP, he was advised to incorporate a company with the LLP confirming in writing:

“The motivation for incorporating Rupert’s business is that as a self-employed person he is currently subject to income tax at 50% plus NIC at 2% on nearly all his earnings, particularly the bonuses and residuals that will continue to flow from the Harry Potter films. We can shelter this income from a 52% tax rate by operating the business through a limited company. Income received by the company will only be subject to Corporation Tax at a maximum rate of 26%.”

Consequently, Clay 10 Limited was incorporated. Rupert Grint was the sole shareholder and his father, who managed his son’s affairs, was the company’s sole director. Rupert Grint’s acting services were provided through the company.

Rupert Grint had rights, under contracts with third parties, to be paid in respect of films in which he had already acted, as well as the prospect of generating earnings in the future. These rights, as well as records and goodwill, were transferred to Clay 10 Limited on 13 October 2011 with consideration left on a loan account for Rupert Grint’s benefit and comprised:

- £4,086,814 as consideration for income from Harry Potter contracts accruing to Rupert Grint as a result of his acting services, which were still to be paid; and
- £4,500,000 as consideration for contractual rights and goodwill relating to likely residuals and bonuses to be paid over the next six years

For the tax year 2011/12 Rupert Grint reported the £4,086,814 as income, while the £4,500,000 was reported as a capital gain, eligible for entrepreneurs’ relief. Rupert Grint withdrew sums from Clay 10 Limited over the following years on the basis they were a repayment of the £4,500,000 loan.

In January 2014, HMRC opened an enquiry into his 2011/12 tax return, issuing a closure notice in July 2019 stating that his tax return had been amended by treating the capital amount of £4,500,000 as income arising under s 778 ITA 2007.” Credit was given for the capital gains tax already paid.

Rupert Grint appealed.

## *Decision*

The First Tier Tribunal highlighted that s.773 ITA 2007 provides an overview of the relevant provisions in this case and sets out a condition for their application as follows:

“773 Overview of Chapter

(1) This Chapter imposes a charge to income tax—

- a) on individuals to whom income is treated as arising under section 778 (income arising where capital amount other than derivative property or right obtained), and
- b) on individuals to whom income is treated as arising under section 779 (income arising where derivative property or right obtained).

(2) Income is treated as arising under those sections only if—

- a) transactions are effected or arrangements made to exploit the earning capacity of an individual in an occupation, and
- b) *the main object or one of the main objects of the transactions or arrangements is the avoidance or reduction of liability to income tax.*”

The First Tier Tribunal emphasised point (2)(b) which was Rupert Grint’s main argument. He claimed that as “avoidance or reduction of income tax was not one of the main objects of the transfer of rights and goodwill to Clay”, the test was not met.

The First Tier Tribunal accepted that one of the reasons for incorporation may well have been to provide limited liability protection. Further, it is possible that incorporation may have provided some administrative convenience.

However, the Tribunal were convinced that these were the main reasons for incorporation. The First tier Tribunal found that the main objects of the arrangements was to ensure that Rupert Grint would not be subject to income tax, as clearly stated by the advisers. The judge stated that one of the main objects in implementing these arrangements was to ensure that Rupert Grint would not be subject to income tax on £4,500,000 relating to his receipts from his work as an actor and any related matters.

The Tribunal concluded that the £4,500,000 sum “derived substantially the whole of its value from the activities” of Rupert Grint and was taxable as income.

*Mr Rupert Grint v HMRC (TC09337)*

## **Failing to deduct and pay PAYE**

*Summary – The taxpayer did not know that the company had wilfully failed to pay income tax and primary NIC contributions on sums paid to him.*

Carbon Managed Services Limited provided support services to a legal company, CPL Group Limited. Both companies were owned by Flourish Holdings Ltd.

Michael Burne was the majority shareholder and director of Carbon Managed Services Limited and CEO of the parent company.

Carbon Managed Services Limited and its parent company were placed into administration on 12 December 2019, with the former put into compulsory liquidation on 30 January 2020.

On 5 March 2021, a compliance check was opened and as part of that work information was requested relating to Michael Burne's PAYE tax and primary class 1 NIC for the period 6 April 2019 to 5 April 2020.

HMRC concluded Michael Burne had been paid an income from his employer shortly before going into administration but no tax or NIC had been deducted from the payments that he received. HMRC believed that Michael Burne knew about this failure to operate PAYE correctly.

On 1 March 2022, a Direction was made, under Regulation 72(5) Condition B of PAYE Regulations 2003, that the company was not liable to pay the outstanding PAYE amounts in respect of the tax year 2019/20. This Direction meant that Michael Burne became liable to pay the amounts due and HMRC sought to collect the amounts payable.

Following a review, the income tax payable was amended slightly but the unpaid NIC was upheld.

Michael Burne appealed to the First Tier Tribunal.

The main issue to determine was whether there was a wilful failure by Michael Burne to make deductions of PAYE tax and pay NIC from payments received by him from the company for the tax year 2019/20 and whether he knew this.

#### *Decision*

Michael Burne was able to produce evidence that, on the balance of probability, showed that he had acted on the advice of others, was not aware of an underpayment and did not knowingly accept payments with the knowledge that the PAYE process had not been followed.

The First Tier Tribunal noted that the company has a good history of meeting its PAYE obligations under RTI and Michael Burn:

- had no advanced knowledge that his company was going to be placed in creditors' administration on 12 December 2019;
- once in creditors' administration, Michael Burn had no standing in the company, or authority to act as a director to direct or control what the company did; such actions rested with the lender's appointed administrator.
- consequently, the RTI return processed on 19 December 2019 could not have been processed or authorised by Michael Burn, in anticipation of the company being placed in administration.

The appeal was allowed.

*Michael Burne v HMRC (TC09326)*

#### **Employee acting as a tax agent**

*Summary – Undeclared income discovered as part of a criminal investigation should have been reported as income arising as a result of the taxpayer acting as a tax agent for clients.*

Issac Frempong claimed that he had always been taxable as an employee through the PAYE system. From 2010/11, he claimed employment related expenses through Self Assessment, submitting his 2010/11 Self Assessment return on 30 May 2011. On 27 January 2012, HMRC opened an enquiry into that tax return. On 12 June 2012, he submitted his Self Assessment return for 2011/12 and on 28 June 2012, HMRC opened an enquiry into that tax return.

In July 2014, HMRC commenced a criminal investigation and the enquiries were put on hold. When interviewed, he provided a pre-prepared statement, in which:

- He denied the allegations that he was a tax agent;
- He stated he had assisted a number of friends and family to use his computer to complete their tax returns, because they did not own a computer;
- He admitted that he assisted these people in completing the relevant forms to claim mileage expenses based on what they told him;
- He stated he believed the claims were legitimate;
- He stated he did not deliberately assist anyone to give false information to HMRC and he did not charge any fee for his assistance; and
- He did not act dishonestly and believed the information that he provided was correct.

In 2016, HMRC issued closure notices, making adjustments to the relevant tax returns, disallowing the employment expenses claimed.

Although the criminal investigation was later closed, evidence gathered during that investigation led HMRC to discover numerous bank deposits totalling in excess of £300,000, a list of individual Self Assessment logins and a spreadsheet detailing payments made by 'clients'.

HMRC issued discovery assessments covering four tax years for the income that had not been declared and Isaac Frempong appealed, disputing the 'Other Income' figures included in the assessments.

### *Decision*

With a university degree in finance and accountancy, the First Tier Tribunal found that Isaac Frempong would have been well aware that when filing his own tax returns that he had significant bank account deposits, which were not being declared for tax. The Tribunal stated that these were not "trivial amounts" described by the taxpayer as "thank you" gestures for the occasional assistance that he claimed that he given to family and friends.

The First Tier Tribunal found that Isaac Frempong was "operating a sophisticated and large operation as a tax agent or tax adviser to numerous individuals, and that he was providing his services for a fee or commission."

This was supported by material seized from the taxpayer's premises including:

- more than 150 individual SA online user identity numbers, almost all with associated passwords;

- web logs obtained from seized devices showing he had registered at least 85 individual users for self-assessment online services, accessed the accounts for at least 105 individual users, and submitted at least 161 income tax returns or claims for repayment of income tax for various taxpayers;
- a spreadsheet listing the names of some 86 individuals under to a column headed “client”, and another column headed “commission” and the sums due.

The First Tier Tribunal found that Isaac Frempong had acted deliberately to mislead HMRC by not declaring the income and the appeal was dismissed.

*Isaac Aboagye Frempong vs HMRC [2024] TC09347*

### **Accountant's ‘Compensation’**

*Summary – The contingent advisory fee was found to be employment income that was liable to income tax and NICs.*

Mr Mellor qualified as a Chartered Accountant in 1997 and immediately went to work for Mr Wall, who was the owner and director of Opal Group, which included a company called Opal Property Group Ltd.

By 2013, Mr Mellor was a director of all companies in the Opal Group, including Opal Property Group Ltd but he was not a shareholder.

The company had entered into an ‘Interest Rate Hedging Product’ which, in 2013, resulted in Opal Property Group Ltd going into administration. Within days, Mr Mellor incorporated Equity Advisory Limited and became director of that company. The company’s single share was owned by Juvanesco Ltd, a company owned jointly by Mr Mellor and his wife.

Opal Property Group Ltd claimed against the bank for mis-selling the hedging product, with Mr Wall owning the interest and rights to that claim.

In 2017, Mr Wall and Equity Advisory Limited entered into an agreement relating to that claim. whereby the company, Equity Advisory Limited would act as consultant in return for a “contingent advisory fee’ payable for both preparing and presenting the claim against the bank. This fee was to be calculated as a percentage of the net proceeds ultimately received at the outcome of the claim. Mr Mellor would undertake the actual work involved. Separately, Equity Advisory Limited and Mr Mellor signed an agreement, effectively transferring the advisory fee to Mr Mellor. Mr Mellor had not told Mr Wall about this and had not shown him a copy.

In September 2017, with the settlement finally agreed between Mr Wall and the bank, the contingent advisory fee of £4,367,496 was paid to Mr Mellor.

Mr Mellor reported this sum on his Self Assessment return as a capital payment, exempt from taxation and included a 26-page white space disclosure that included the rationale for treating it as non-taxable. He argued that the real reason for the payment was that it reflected his lost career resulting from the administration, as he was now professionally unemployable. The sum received was a capital sum, exempt from taxation under s.51(2) TCGA 1992 as this was a sum “obtained by way of compensation or damages for any wrong or injury suffered by an individual in his person or in his profession or vocation”.

HMRC disagreed, arguing that the payment was not linked in any way to the wrongdoing by the bank but rather, it was employment income. HMRC sought to recover PAYE (£1,954,387) and NICs (£693,747) from Equity Advisory Limited. Further, Mr Mellor was personally liable for income tax of £1,960,708.

Equity Advisory Limited and Mr Mellor appealed.

### *Decision*

The First Tier Tribunal stated that if a payment is chargeable to income tax, then it is not capital. Consequently, the appropriate starting point was whether the payment was chargeable to income tax or not. This involved consideration of its source.

The Tribunal found that the payment was made by Mr Wall pursuant to the provisions of the Consultancy Agreement. Equity Advisory Limited, and not Mr Mellor in his personal capacity, was providing the services to Mr Wall under that agreement. The Tribunal stated that “This remains the position even though, as is clear, Equity Advisory Limited was providing its services to Mr Wall through the human agency of Mr Mellor.” In the First Tier Tribunal’s view, looked at in the round, the payment source was Mr Mellor’s employment with Equity Advisory Limited. The payment was Mr Mellor’s remuneration for his services to Equity Advisory Limited; or “as a reward to Mr Mellor for his services as a director of Equity Advisory Limited.”

The Tribunal went on to say that:

“For the sake of completeness, we simply note that if Mr Mellor’s position ....was that the payment was to “compensate”[him] ‘for the destruction of his career’, that this seems to be an acceptance that the Payment would have fallen within the provisions of ITEPA sections 401-406 (which deal with payments on termination of employment)”

Consequently, the payment to Mr Mellor was a:

- payment “from” his employment with Equity Advisory Limited for income purposes;
- remuneration or profit “derived from” an employment for NICs purposes.

The appeal was dismissed.

*Equity Advisory Limited and Craig Allan Mellor v HMRC (TC09334)*

### **Ten years too late**

*Summary – The taxpayer’s appeal was submitted ten years too late and was rejected for being out of time.*

Believing that Paul Needham had not declared property income, HMRC issued notice to file letters and paper Self Assessment returns covering 2005/06 to 2009/10, which he claimed he never received.

As these returns were not filed, HMRC issued determinations that were not paid and so on 11 November 2011, HMRC issued the late payment surcharges, which he also claims he never received.

In April 2012, HMRC had also issued him with a notice to file a self-assessment tax return for 2011/12, which he filed, but not until 19 October 2019. Having been filed late, HMRC issued late

filing, six-month, daily and 12-month penalties. When Paul Needham and his accountant tried to engage with HMRC to establish why the return notices had been issued, they claim HMRC failed to provide an explanation.

Finally, in August 2023, Paul Needham appealed against the late filing penalties, determinations, surcharges, and interest, totalling just under £12,000.

The appeal was obviously late and so this case concerned whether the First Tier Tribunal would allow the appeal out of time.

### *Decision*

The First Tier Tribunal considered each of the three points established in *Martland v HMRC* (2018) UKT178 and concluded that:

1. An appeal ten years after the penalties were issued was a long time;
2. Although Paul Needham claimed that the reason for the delay was because HMRC had failed to provide him with the explanations that he needed, this was not a valid reason for submitting the appeal ten years later.
3. On the balance of probabilities, despite HMRC's lack of assistance, it was likely that Paul Needham was aware of his right to appeal for some time before he actually appealed.

The appeal against surcharges and late penalties was dismissed. Further, as there is no right of appeal or other statutory provision against interest and determinations, the First Tier Tribunal had no jurisdiction to hear and determine these issues, this part of the appeal was struck out.

*Paul Needham v HMRC (TC09342)*

### **Information notice**

*Summary – Information and documents requested by HMRC were reasonably required in order to check the taxpayer's tax position.*

HMRC were, and are still, concerned that Mary Simpkins had entered into arrangements with Olympus Consulting Ltd, her employer, to avoid income tax on her earnings.

In February 2023, HMRC wrote to her requesting information and documentation relating to her employment arrangements, but she failed to supply the information requested.

Consequently, HMRC formerly requested the information by issuing an information notice. The information requested included details of the terms of employment and how earnings were to be paid, payments received in connection with the employment, intermediaries through which she provided services, contracts, and copies of payslips and bank statements.

Mary Simpkins challenged the notice, arguing that:

- documents for the current tax year should not be requested as that year was not subject to an enquiry;

- the documents were not reasonably required particularly regarding the current tax year and as there was no "sensible or reasonable possibility of HMRC imposing any liability to pay tax";
- some documents should be obtained from her employer;

### *Decision*

The First Tier Tribunal stated that:

"It is the Appellant who is liable for the payment of income tax and class 1 national insurance contributions on any sums she earns from her employment. Such tax is usually collected by way of deductions made by an employee's employer under Pay As You Earn, the employer paying over the tax deducted to HMRC. However, the primary liability to account for and pay the correct amount of income tax rests with the Appellant."

Consequently, under schedule 36 FA 2008, if Mary Simpkins' employment arrangements resulted in an underpayment of income tax in any year "past, present or future" HMRC are entitled to "check" that "tax position". The Tribunal stated that it did not matter whether there was an open enquiry or that the information and documents were requested for a current tax year.

Having carefully considered each item of information and documentation requested, the First Tier Tribunal concluded that they were reasonably required in order to check whether Mary Simpkins had received payments on which no tax had been deducted, and whether tax should have been so deducted. The information required was not unduly onerous to produce as all of the documents requested were of a type that should have been retained and/or could have been requested from her employer. The items were all within her possession or power.

Finally, the Tribunal considered whether a third-party notice to her employer should have been issued for some of the information. The Tribunal stated that whilst the deductions made from employment income were made by the employer and, in accordance with Sch. 36, HMRC were also entitled to check her employer's tax position in this regard, that did not negate the fact that HMRC were also entitled to check the Mary Simpkins' tax position. Accordingly, the information notice was found to be appropriate.

*Mary Simpkins v HMRC (TC09320)*