

Tax update

Contents

| | |
|--|---|
| 15 June 2022 | 1 |
| 1. Private client | 1 |
| 1.1 Private residence relief allowed for period before construction | 1 |
| 1.2 Taxpayer loses appeal on share proportion for business asset disposal relief | 2 |
| 1.3 Appeal on deductions for CGT dismissed | 2 |
| 2. PAYE and employment | 2 |
| 2.1 Split contract arrangements held to be DOTAS notifiable | 2 |
| 3. Business tax | 3 |
| 3.1 UK controlled foreign company state aid appeal dismissed | 3 |
| 3.2 New super-deduction guidance | 3 |
| 3.3 Loan interest payable disallowed due to unallowable purpose | 3 |
| 4. And finally | 4 |
| 4.1 A bit of a rattle | 4 |

1. Private client

1.1 Private residence relief allowed for period before construction

The FTT has found for the taxpayers that 'period of ownership' for private residence relief (PRR) means the period of ownership of the dwelling being sold. The period during which they just owned the land, on which a house was subsequently built, was therefore not excluded from the relief.

The taxpayers bought a plot of land on which they built a house, moving in four days after the works were complete. The build took more than two years, and they sold the house after a year of residence. HMRC's interpretation of the legislation was that the period of ownership was the whole period they owned the land, and that PRR should only apply to the period they occupied the house.

The FTT found for the taxpayer that the 'period of ownership' was the time for which they owned the dwelling, not just the land. Although there is no clear definition in the legislation, the judge noted that this was the natural meaning. 'Dwelling house' in the legislation could not be interpreted to include land with no house. An extra-statutory concession on property undergoing renovations did not affect the reading of the legislation.

This is a somewhat surprising decision, given that in the past Courts have found that the period of ownership in this scenario starts when then the land is acquired, for example in *Henke*. It will be interesting to see the UT's thoughts on this matter, should this case be heard there.

Lee & Anor v HMRC [2022] UKFTT 175 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2022/TC08502.html

1.2 Taxpayer loses appeal on share proportion for business asset disposal relief

The FTT has denied business asset disposal relief (BADR), then known as entrepreneurs' relief, on a holding of just under 5% of shares in a company. Despite an internal understanding that the taxpayer held 5%, this was not reflected in his shareholding.

The taxpayer held A and B ordinary shares in a holding company. The B shares did not have voting rights. He held just under 5% of the A shares, but claimed BADR when the company was sold on the basis that he indirectly owned an additional fraction to make his shareholding up to 5%. He also received 5% of the proceeds on sale.

It has always been understood in the company that he owned 5%, though the number of shares in issue was such that his percentage of shares held was a tiny fraction less than 5%, and some paperwork referred to his 5% share. HMRC contended that he had no beneficial interest in any shares other than his, which fell under 5%, but he argued that the additional fraction was held on trust for him.

The FTT found for HMRC. There was not enough certainty of intention to create an express trust giving the taxpayer the additional percentage to take him up to 5%. Although his share had been referred to in rounded-up terms as 5%, this was shorthand, not a statement of exact fact. There was also no constructive trust, as there was no common intention among the shareholders that any of them held their shares on trust for the taxpayer. They each believed themselves to be the full owner of their own shares. There was no resulting trust, as again there was no intention to hold the shares on trust, and there was insufficient certainty of subject matter.

Kavanagh v HMRC [2022] UKFTT 173 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2022/TC08500.html

1.3 Appeal on deductions for CGT dismissed

The FTT has found that borrowing by a company was not expenditure on shares, so a shareholder who repaid loans could not deduct the expenses when calculating the chargeable gain.

The taxpayer sold some shares to a trust, in two tranches. The agreement was that they would be free of secured debt. He discharged the company's debts in consequence, and claimed this as an expense of the sale of shares.

The FTT agreed with HMRC that this was not a deductible expense, as it was not an incidental cost of sale. The agreement could have been structured to sell the shares at a lower price, with the debt in place. The expenditure did not change the state or nature of the shares, so it was also not enhancement expenditure.

Tedesco v HMRC [2022] UKFTT 171 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2022/TC08498.html

2. PAYE and employment

2.1 Split contract arrangements held to be DOTAS notifiable

The FTT has held that arrangements for splitting contracts into employment and consultancy were notifiable Disclosure of Tax Avoidance Schemes (DOTAS) arrangements.

Two associated companies offered a tax scheme. This involved splitting employment into a contract remunerating directors' fiduciary services and a second contract offering the services of the director under a consultancy arrangement with the promoter of the scheme or an associated entity. Under the latter arrangement the consultant was paid through loans, which were thought at the time to be taxable on receipt as loans and not remuneration. The loans were not expected to be recoverable during lifetime.

The case concerned the notifiability of the arrangements for DOTAS under the premium fee and standardised arrangements hallmarks. The arrangements were held to be so notifiable, but were held not to be grandfathered. Even though broadly similar arrangements had been previously promoted, the FTT found that there were material differences sufficient to mean that the grandfathering exception, whereby similar arrangements were known before 2006, did not apply.

AML TAX (UK) LIMITED (2) DENMEDICAL UK LIMITED v Revenue & Customs [2022] UKFTT 174 (TC) (04 May 2022)
www.bailii.org/uk/cases/UKFTT/TC/2022/TC08501.html

3. Business tax

3.1 UK controlled foreign company state aid appeal dismissed

The EU General Court has upheld the EC decision that the UK's controlled foreign company (CFC) rules did constitute illegal state aid. The case concerned the CFC rules in place in the UK between 2013 and 2018, specifically the group financing exemption.

In its original decision the EC found that the group financing exemption gave a selective advantage to some multinational companies when the financing income of a foreign group company was derived from decision-making functions in the UK. The EC ruled that the UK should recover tax from those companies that were unjustly advantaged by the exemption.

The UK Government and several affected businesses appealed the decision on a number of grounds. The EU General Court rejected all their arguments finding in favour of the EC.

[CURIA - Documents \(europa.eu\)](http://CURIA - Documents (europa.eu))

3.2 New super-deduction guidance

HMRC has issued new guidance on the capital allowances super-deduction and special rate first year allowance.

The guidance covers:

- checking eligibility for the super-deduction or special rate first year allowance;
- working out how much can be claimed on qualifying plant and machinery costs; and
- how to calculate the balancing charge when disposing of an asset on which the super-deduction or special rate first year allowance has been claimed.

www.gov.uk/guidance/check-if-you-can-claim-super-deduction-or-special-rate-first-year-allowances

3.3 Loan interest payable disallowed due to unallowable purpose

The FTT has found that the main purpose of a loan relationship to which the taxpayer was party was to obtain a UK tax advantage. The loan therefore had an unallowable purpose, and no deduction was allowed for the resulting interest expenses.

The taxpayer, a UK incorporated company, was a member of a multinational group with its ultimate parent company in the US. It was set up to acquire a US group worth \$1.1bn. The transaction involved a series of steps that sought to maximise group interest deductions whilst minimising taxable credit interest. Overall, the funding arrangements provided a deduction for third party interest in the US, and group interest in the UK with no taxable credits in the US, UK, or Cayman Islands where a finance company had also been set up. HMRC denied relief for over £40m of loan interest debits claimed by the taxpayer on the grounds that the loan had an unallowable purpose.

In reaching its decision, the FTT considered whether or not the main purpose of the loan arrangement was to obtain a tax advantage, and if it was, what proportion of the interest payment was attributable to that unallowable purpose. The FTT found that the presence of free-standing loan relationship deficits that were surrendered by way of group relief to UK members of the group, without any corresponding taxable receipts, did mean that the taxpayer had secured a tax advantage by being party to the loan relationship. Evidence, including reports and internal emails, showed the sole purpose of the funding arrangement was to obtain a UK tax advantage. The UK and Cayman Island companies had no employees or tangible assets, which further evidenced the lack of genuine commerciality in the loan agreements. As the main purpose for the taxpayer being party to the loan relationship was to obtain a UK tax advantage, no part of the loan had an allowable purpose and so it was correct that the interest payments be disallowed in full. The taxpayer's appeal was dismissed.

JTI Acquisition Company (2011) Limited vs HMRC [2022] UKFTT 166 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2022/166.html

4. And finally

4.1 A bit of a rattle

The *Lee* case this week (item 1.1 above) took us straight back *Through the Looking-Glass*. It reminded us of nothing so much as Tweedledee and Tweedledum agreeing to have their battle. For Tweedledum said Tweedledee had spoiled his nice new private residence relief. Tweedledee said we must pretend that owning land is owning a dwelling, but Tweedledum said we must pretend that we haven't owned the land. Whose complete fiction will prevail? Only in our beloved tax world do we find such absurdities. Alice might think them both obviously wrong, but we know one of them has to win and we all have to pretend the winner was right. Fiction indeed; but, sadly, with money at stake.

Tweedledee, though, also tells Alice that she is in someone else's dream. You can see his point. Sometimes, tax is just like that.

Lee & Anor v HMRC [2022] UKFTT 175 (TC)

www.bailii.org/uk/cases/UKFTT/TC/2022/TC08502.html

| Glossary | | | | |
|--|---|---|---|---------------------------------------|
| Organisations | | Courts | Taxes etc | |
| ATT – Association of Tax Technicians | ICAEW – The Institute of Chartered Accountants in England and Wales | CA – Court of Appeal | ATED – Annual Tax on Enveloped Dwellings | NIC – National Insurance Contribution |
| CIOT – Chartered Institute of Taxation | ICAS – The Institute of Chartered Accountants of Scotland | CJEU – Court of Justice of the European Union | CGT – Capital Gains Tax | PAYE – Pay As You Earn |
| EU – European Union | OECD – Organisation for Economic Co-operation and Development | FTT – First-tier Tribunal | CT – Corporation Tax | R&D – Research & Development |
| EC – European Commission | OTS – Office of Tax Simplification | HC – High Court | IHT – Inheritance Tax | SDLT – Stamp Duty Land Tax |
| HMRC – HM Revenue & Customs | RS – Revenue Scotland | SC – Supreme Court | IT – Income Tax | VAT – Value Added Tax |
| HMT – HM Treasury | | UT – Upper Tribunal | LBTT – Land and Buildings Transaction Tax | |

Evelyn.com

Offices: London, Belfast, Birmingham, Bristol, Dublin (City and Sandyford), Glasgow, Guildford, Jersey, Salisbury and Southampton.

Evelyn Partners LLP: Regulated by the Institute of Chartered Accountants in England and Wales for a range of investment business activities.

Tax legislation is that prevailing at the time, is subject to change without notice and depends on individual circumstances. Clients should always seek appropriate tax advice before making decisions. HMRC Tax Year 2022/23.

We have taken care to ensure the accuracy of this publication, which is based on material in the public domain at the time of issue. However, the publication is written in general terms for information purposes only and in no way constitutes specific advice. You are strongly recommended to seek specific advice before taking any action in relation to the matters referred to in this publication. No responsibility can be taken for any errors contained in the publication or for any loss arising from action taken or refrained from on the basis of this publication or its contents. © Evelyn Partners 2022.