[2024] UKUT 00266 (TCC)

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

Applicants: (1) Wired Orthodontics Limited **(2) Ian Hutchinson** **(3) Susan Bessant**	**Tribunal Ref: UT/2023/000119**
Respondents: The Commissioners for His Majesty's Revenue and Customs	

APPLICATION FOR PERMISSION TO APPEAL

Oral hearing: 20 June 2024

DECISION NOTICE

JUDGE THOMAS SCOTT

1. This was an oral hearing to consider the application of the Applicants (the "Application") for permission to appeal against the decision of the First-tier Tribunal (Tax Chamber) (the "FTT") released on 6 January 2023 ("the Decision"). The Applicants had requested that their application be dealt with at an oral hearing, to be held remotely, so this decision has not been preceded by any written decision of this Tribunal regarding permission to appeal.

2. The FTT refused permission to appeal in a decision dated 31 October 2023 (the "PTA Decision").

3. The hearing was attended by Mr Andrew Thornhill KC as representative of the Applicants and Mr Adam Tolley KC as representative of HMRC. I had directed that HMRC had permission to make any written submissions in advance of the hearing. Mr Thornhill

filed a skeleton argument and Mr Tolley filed written submissions in advance of the hearing. I heard oral submissions from both counsel.

When can an appeal be made?

4. An appeal to this Tribunal can be made only on a point of law: section 11 of the Tribunals, Courts and Enforcement Act 2007. It must be shown that it is arguable that the FTT made an error of law in reaching its decision. "Arguable" means that the argument stands a realistic as opposed to fanciful prospect of success.

The Decision

5. References below in the form FTT[x] are to paragraphs of the Decision.

6. The issues which were before the FTT are set out at FTT[1]-[3]:

> 1. Wired Orthodontics Limited ("the Company") established an employee benefits trust ("the Trust") to which it undertook to contribute £300,000 within the next 10 years. The Company then entered into agreements with a company called Asset Hound Ltd ("Asset Hound") for the purchase of £300,000 worth of gold bullion for Ms Bessant and Mr Hutchinson ("the Directors"), who were its shareholders and directors as well as employees of it. The gold was immediately sold and the Directors satisfied the Company's obligation to Asset Hound to pay for the gold by the use of the proceeds of its sale. In so doing a corresponding credit was created on their directors' loan accounts which they later drew upon by payments in cash to them. At the same time as the purchase of the gold the Directors agreed to assume the obligation entered into by the Company to pay £300,000 to the Trust. We refer to the transactions taken together as "the Scheme".
>
> 2. HMRC say that the Directors received money or money's worth as a reward for the provision of the services which constituted "earnings" in relation to their employment with the Company, notwithstanding their obligation to pay sums to the Trust. As a result HMRC say that:
>
> (1) Either:
>
> (a) the Company was obliged to account for PAYE income tax and NICs on the earnings; and
> (b) the Directors, having failed to make good the income tax in question to the Company are liable to a further income tax charge under s222 Income Tax (Earnings and Pensions) Act 2003 ("ITEPA");
>
> Or:
>
> (c) the Company is liable to tax on the value of the benefit (the gold) conferred on the Directors pursuant to s464A Corporation Tax Act 2010 ("CTA 2010");

(2) the Company is not entitled to a corporation tax deduction for the relevant expenses in the relevant accounting periods because:
(a) the expenses were not recognised in accordance with generally accepted accounting practice ("GAAP");
(b) the expenses were not incurred wholly exclusively for the purposes of the Company's trade; and/or
(c) any deduction for the expenses was deferred pursuant to section 1290 and/or s1288 Corporation Tax Act 2009 ("CTA 2009").

3. Finally, HMRC say that if their assertions regarding the taxation of the Directors and the Company are not correct, the general anti-abuse rule ("GAAR") applies such that the tax advantages arising from the arrangements should be counteracted.

7. The FTT did not determine the GAAR position. In relation to the other issues it decided that:

(1) The Company made payments of earnings for income tax and NICs purposes (the "earnings" decision).

(2) Section 222 ITEPA 2003 (readily convertible assets) applied to the Scheme (the "section 222" decision).

(3) The payments by the Company were not deductible for corporation tax purposes because they were not made wholly and exclusively for the purposes of the Company's trade (the "deductibility" decision).

Grounds of appeal

8. Mr Thornhill stated in his skeleton argument, and confirmed in the hearing, that certain of the grounds for which permission was sought in the Application were no longer pursued by the Applicants.

9. The grounds for which permission is now sought are as follows:

(1) **Grounds 1 and 2**: These grounds relate to the **earnings** decision. They are as follows:

Ground 1: The Decision attaches no weight to the directors' obligation to pay the Trust. It is dismissed on the basis that the obligation did not arise under a loan (paragraph 196 of the Decision). There is no acceptance of the Respondents' contention (paragraph 160) that there was no intention to pay the Trust, nor could there be. The Trust was paid early, admittedly to avoid the loan charge (paragraph 143), but clearly there would have been no loan charge liability if the arrangement was that the debt would never be paid. It is accepted that the obligation was not under a loan. However, the same reasons apply to the obligation to pay the Trust as apply in the case of a loan (cp the decision in *Dextra Accessories Ltd v Macdonald (Inspector of Taxes)* cited in *Rangers* [2017] STC 1556 at paragraph 57. The decision should have treated the obligation to pay as negativing earnings. While Lord Hodge disagreed with the conclusion in *Dextra*, it was not in regard to loans not being earnings. The

decision also questions whether a loan could be regarded as a reward. There is no reason, it is submitted, why not.

Ground 2: It is submitted that the Tribunal misinterpreted the decision of the Supreme Court in *Rangers* (paragraph 198) and was led by this misinterpretation to the conclusion that the directors received earnings. The Supreme Court did not decide that loans were earnings. They decided that the footballer employees had arranged for their earnings to be paid to trusts which happened to loan the amounts to them. The payment of earnings occurred when the trusts were paid, not when the loans were made. This is clearly established by the concluding words of paragraph 66 of Lord Hodge's speech *(RFC 2012 (in liquidation) (formerly the Rangers Football Club Plc) v Advocate General for Scotland* [2017] STC 1556 at page 1578).

(2) **Ground 3**: This relates to the **section 222** decision. It is as follows:

If, contrary to Grounds 1 and 2, there were earnings at the outset, the Tribunal erred by holding s.222 ITEPA applied. As submitted by the Respondents (paragraph 159 of the Decision) it was pre-ordained that the gold would be sold, the cash used to pay for the gold and proceeds credited to the directors' loan accounts. They received and could only receive cash. The readily convertible asset provisions are needed where the employee receives the asset and sells it for cash which he keeps. The directors did not keep the cash. They received credits to their loan accounts. The company could have reduced the credits by paying PAYE if there were earnings.

(3) **Ground 4**: This relates to the **deductibility** decision. It is as follows:

On deductibility the Tribunal erred by misinterpreting the decision of the Upper Tax Tribunal in *Scotts Atlantic Management Ltd v HMRC* [2015] STC 1321. The finding in the third bullet point at paragraph 61 on page 1336 was critical to the decision. Furthermore, the correctness of that decision has been called into question by the Court of Appeal in *Hoey v HMRC* [2022] STC 902 paragraph 194.

10. In his oral submissions. Mr Thornhill modified and supplemented these grounds, and I will deal below with the additional points which he raised orally.

Grounds 1 and 2 :Earnings

11. Grounds 1 and 2 are based on a number of assertions about the FTT's reasoning in concluding that "earnings" were received under section 62 ITEPA, which Mr Thornhill says were arguable errors of law. I now consider each of those assertions:

(1) It is said that the FTT attached no weight to the directors' obligation to pay the Trust, dismissing it at FTT[196] on the basis that it did not arise under a loan. That characterisation of the FTT's reasoning is inaccurate. At [196] and [197], the FTT explained why it accepted HMRC's argument, and rejected the taxpayers'

argument, stating that there was no actual loan—which is accepted by Mr Thornhill—and that on the facts the obligation to the Trust did not have the effect argued for by Mr Thornhill. This assertion does not identify any arguable error of law.

(2) It is said that *Dextra*, *Rangers* and principle mean that the arrangements should be taxed in the same way as a loan. The Applicants' arguments on this issue were considered by the TTT and rejected, with full reasons. Continued disagreement with the FTT does not serve to identify any arguable error of law.

(3) It is said that the FTT misinterpreted the decision of the Supreme Court in *Rangers* (paragraph 198) and was led by this misinterpretation to the conclusion that the directors received earnings. As the FTT said in its PTA Decision (paragraph 13), it relied on *Rangers* primarily to support a purposive construction of the legislation. The FTT's reasoning was not based on a mistaken interpretation of *Rangers* but on all the factors and conclusions set out at FTT[193]-[201]. Mr Thornhill said in particular that a sentence in FTT[198] showed that the FTT had misunderstood *Rangers*. However, when the FTT said at that paragraph that "the Supreme Court decided that the actual loans made to the employees in that case were taxable earnings where the payments were made by the employer to the employee remuneration trust", Mr Thornhill's reading, that the FTT thought the loans were earnings, ignores the second part of that sentence. It also ignores the fact that, read fairly and in the round, the FTT correctly directed itself as to the law on earnings and properly understood *Rangers*. This assertion does not identify any arguable error of law.

(4) In HMRC's written submissions, Mr Tolley argued that it was well established that earnings do not cease to be taxable simply because an employee is obliged to, or agrees to, apply the earnings in a particular way, citing as authority *Rangers* and *Smyth v Stretton* (1904) 5 TC 36. Mr Thornhill took issue with that argument. However, this is not a rehearing and the issue before me is whether the FTT arguably erred in law in reaching its decision. While the FTT referred to Mr Tolley's argument on this point at FTT[17(3)] and FTT[159], in reaching its conclusion it does not refer to *Smyth*. This was not, therefore, an arguable error of law in the FTT's decision on this issue.

12. Mr Thornhill stressed that in this case there was no pre-existing or antecedent right to earnings which was being redirected: the situation was therefore materially different from *Rangers*. He said that (1) an employee paid full market value for the gold, so there were no earnings when the gold was received, and (2) when a credit was made to the director's loan account, any drawing on that account was subject to an obligation to fund the Trust, so by analogy with a loan that obligation negatived any receipt of earnings. There was "nothing magic about a loan". He said that the FTT was wrong to rely in reaching its decision on the presence of recycling, because there was no certainty, and no finding, as to what amounts would be credited, and in what proportions to whom. It was not possible to say at the outset that the money would travel in a circle.

13. Mr Tolley said that Grounds 1 and 2 were unsound because they mischaracterised the FTT's decision. In relation to the FTT's finding re recycling, the absence of any findings as to amounts and allocation was irrelevant; the point of substance was that "what went in

would come out". Mr Thornhill's arguments as to why earnings did not arise were inconsistent with the FTT's findings of fact as to the operation of the scheme, and so was his argument that there was no "antecedent right" to earnings.

14. I do not consider that any of the points made by Mr Thornhill during the hearing before me (in addition to those on his skeleton argument and the Application) identify any error of law in the FTT's decision on the earnings issue which is arguable, in the sense of having a realistic as opposed to fanciful prospect of success.

15. Mr Thornhill no longer seeks permission to appeal against the FTT's findings regarding recycling, and I agree with Mr Tolley that it is not arguable that the FTT erred in relying on those findings because it did not make related findings as to precisely which individual would receive what amount and when. The FTT was fully aware that those details were not settled at the outset of the scheme: see, in particular, its findings at FTT[135] and [136]. The relevance of the recycling feature to the FTT's decision on the earnings issue was as described by the FTT; its rejection of Mr Thornhill's argument that the arrangements should be treated in the same way as a loan was "reinforced" by recycling (FTT[197]) and it formed an element of its reasoning as to why the receipt of the gold gave rise to earnings (FTT[200] and [201]). Neither of those conclusions entailed any arguable error of law because the precise basis of allocation was not known at the outset.

16. As I have explained above, it is not arguable that the FTT's decision relied on an analogy with the facts in *Rangers*.

17. The argument that the FTT erred in not appreciating that there was no antecedent right to earnings is, in my view, largely an attempt to reargue the issue, but in any event it is not consistent with the FTT's findings of fact and conclusions, in particular at FTT[195] and [200].

18. I do not consider that Grounds 1 and 2 raise any arguable error of law. I refuse permission to appeal on those grounds.

Ground 3: Section 222

19. Mr Thornhill explained that if the FTT was correct that earnings arose when the gold was received, the Applicants accepted that section 222 would apply. However, if there were no earnings at all, or if the earnings arose when credits were made to the directors' loan accounts, then permission to appeal was sought to challenge the conclusion that section 222 would apply.

20. Since I have refused permission to appeal in relation to the earnings issue, Ground 3 relates only to whether the earnings arose when the gold was received.

21. Mr Thornhill argued that the use of gold in the scheme was all part of a plan to take advantage of the disguised remuneration provisions, and since that plan had failed "the complexities of the gold were irrelevant and unnecessary at the end of the day". He also repeated his argument that the directors never had an entitlement to the gold, as they paid market price for it, and it was "pre-ordained" that they would sell it and pay the purchase

price, the Company having no funds to pay for the gold. The directors could only ever receive cash, via the loan account credits.

22. I consider that in view of the FTT's findings of fact, which are not challenged, this ground is unarguable. At FTT[193(2)], the FTT stated that "the Directors received £300,000 worth of gold. The documents were at pains to show that the beneficial ownership of the gold vested in the Directors". At FTT[195] the FTT found as follows:

> We are clear that the provision of the gold to the Directors was the provision of money or money's worth to them. The Directors were able to convert their momentary ownership of the gold into loan account credits which they subsequently drew as cash. There was no contractual requirement as between the Company and the Directors that when they became entitled to the gold they should use the proceeds of sale of it to satisfy Asset Hound's invoice. Instead, the Directors received the gold and the documents sought to make clear that they had beneficial ownership of it even if in fact that ownership was momentary because they had already decided to sell it.

23. At FTT[203], the FTT agreed with HMRC's submission that the rules dealing with readily convertible assets were "precisely aimed at covering situations in which there is, in substance, a payment of earnings in cash". I agree.

24. Ground 3 is unarguable and I refuse permission to appeal for this ground.

Ground 4: Deductibility

25. The FTT's decision on the deductibility issue was at FTT[185]-[191], where it set out the relevant principles, and FTT[205]-[221]. The FTT identified two issues, namely whether the expense of £300,000 was correctly recognised in the Company's accounts in accordance with GAAP, as required by section 46(1) Corporation Tax Act 2009 ("CTA 2009"), and whether the expense was incurred wholly and exclusively for the purposes of the Company's trade, as required by section 54 CTA 2009. Both requirements needed to be satisfied.

26. The FTT recorded that although the expert witnesses for each party disagreed, they agreed that if in fact there was no intention that the Directors should satisfy the obligation to pay sums into the Trust, the expenses would be correctly recognised for GAAP: FTT[207]. The FTT decided that because it had concluded that in fact it was most likely that the moneys would be recycled to the Directors, there was in substance no intention to this effect, so that no asset should be recognised under GAAP in the Company's accounts in relation to the Trust. As a result, the deduction was made in accordance with GAAP.

27. In relation to the "wholly and exclusively" requirement, The FTT identified the issue as whether, in incurring the relevant expenses, there was a duality of purpose which meant that the test was not met: FTT[211]. The burden of proof was on the Appellants. The FTT found that the scheme transactions were "highly contrived in order to seek to achieve the combination of tax free income for the Directors and a tax deduction for the Company" (FTT[214]) and that "the transactions were designed with the aim of circumventing [the disguised remuneration legislation] by, amongst other things, the very unusual step of the

Directors ostensibly undertaking to fund the Trust themselves" (FTT[216]). The FTT concluded as follows:

> 217. These consequences were "so inevitably and inextricably involved" in the payment of the £300,000 and were not "merely incidental" (as per *Rangers*) that they must be taken to be a purpose for which the payment was made.
>
> 218. Therefore, looking at the transactions and our findings overall, we conclude that a primary purpose of the Scheme was to provide tax-free cash to the Directors in circumstances where a corporation tax deduction could also be sought. There was a clear purpose to implement a pre-arranged scheme in order to achieve those results. The purpose of the transactions was not simply to reward the employees. That could have been achieved in various, much simpler ways.
>
> 219. As a result we are satisfied that there was a duality of purpose when the Company paid the £300,000 for the gold in the context of the Scheme overall. The securing of a corporation tax deduction was a freestanding purpose of the Company in entering into the Scheme transactions.
>
> 220. We recognise that in the ordinary course the payment of taxable earnings to employees would give rise to deductible expenses for an employer. Mr Thornhill submitted that this must be the result here. However, there is no legislative or other rule identified by Mr Thornhill causing that corporation tax treatment to follow the taxability of the earnings and we are satisfied that no such result is required in law.

28. Ground 4 seeks permission to appeal the FTT's decision on the "wholly and exclusively" issue on the basis of two arguments. First, it is said that "either *Scotts Atlantic*[1] has been misinterpreted or it was wrongly decided". Second, it is said that the decision was wrong in the light of the decision of the Court of Appeal in *Hoey v HMRC* [2022] EWCA Civ 656 ("*Hoey*").

29. Similar versions of both of these arguments were recently considered and rejected in *AD Bly Groundworks and Civil Engineering Limited v HMRC* [2024] UKUT 00104 (TCC) ("*AD Bly*"), by an Upper Tribunal of which I was part. Permission to appeal that decision to the Court of Appeal was refused by this Tribunal on 22 May 2024. Mr Thornhill suggested that a reason for "keeping these arguments alive" was that permission to appeal had been sought the Applicants from the Court of Appeal. The Court of Appeal Case Tracker was last updated on 22 July 2024 and does not contain any reference to such an application, but, in any event, I do not accept that any such application would provide a good reason to grant permission in this case. Mr Tolley pointed out that an application for postponement of the application for permission on this ground could have been made, but was not, and Mr Thornhill clarified in the hearing no such application was sought. Ground 4 falls to be considered by reference to the facts of this case (not those in *AD Bly*), and by reference to the law as it currently stands.

30. Dealing first with *Scotts Atlantic*, the FTT set out Mr Thornhill's submissions to the FTT on that authority at FTT[149] and [189]. As was explained in *AD Bly*, the argument that

[1] *Scotts Atlantic Management Ltd v HMRC* [2015] UKUT 66 (TCC).

Scotts Atlantic established that the "wholly and exclusively" test is only failed by reference to a tax deduction purpose where that purpose is "all-pervading object" wrongly relies on the FTT's approach to that issue in *Scotts Atlantic*, which was criticised by the Upper Tribunal in the passage set out in the Decision at FTT[190]. The assertion that, alternatively, "*Scotts Atlantic* was wrongly decided" is not arguable insofar as it relates to the summary in that case of the well-established authorities on duality of purpose. Whether or not it was wrongly decided on the facts is nothing to the point in relation to the Application.

31. The decision in *Hoey* was released two months before the FTT hearing in this case, but it does not appear to have been referred to or relied on by Mr Thornhill: paragraph 18 of the PTA Decision. Assuming for the purposes of the Application that the new argument is admitted, I do not consider it is arguable that, by failing to take *Hoey* into account, the FTT erred in law in reaching its decision on deductibility.

32. The relevance and effect of *Hoey* as a matter of law on the deductibility issue is set out in *AD Bly* at [39]-[51]. It is not arguable that a decision that earnings arose for tax purposes mandates a decision that the payment was deductible; it all depends on the facts. Mr Thornhill suggested that there was nothing artificial or excessive about the remuneration in this case, but I do not accept that: the scheme was, as the FTT found, highly contrived and could scarcely have been more artificial, and did not cease to be so because it did not work. Nor do I accept Mr Thornhill's suggestion that, because the scheme did not work, one should effectively ignore the contrived steps of the scheme and treat the payment as "normal" remuneration. The issue in relation to the "wholly and exclusivity" test was not contrivance *per se* but duality of purpose. It is not arguable that because a purpose of tax reduction was found to exist it should be ignored because in the event that purpose was not achieved.

33. I do not consider Ground 4 to be arguable and refuse permission for it.

Decision

34. For the reasons given, permission to appeal is refused.

Signed: **Date:29 August 2024** **Judge Thomas Scott**
Issued to the parties on: 29 August 2024