[2020] UKUT 0119 (TCC)

Appeal number: UT/2019/0012

Tax treatment of certain payments under management training contract – whether FTT erred in conclusion termination payment trading revenue receipt (consideration for cancellation of the contract to provide training) rather than capital (compensation for loss of a secret process in proprietary performance management system) - House of Lords' decision in Evans Medical Supplies Ltd v Moriarty (H M Inspector of Taxes) ([1957] 37 TC 540) considered – no – whether FTT erred in conclusion other contractual payments gave rise to tax liability on appellant (as opposed, through a multi-party agreement, to other entities appellant owned) – no – appeal dismissed

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

KIERAN LOONEY;
KIERAN LOONEY & ASSOCIATES (a firm) **Appellants**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: JUDGE SWAMI RAGHAVAN
JUDGE ASHLEY GREENBANK

Sitting in public at The Royal Courts of Justice, Strand, London WC2 on 11 February 2020

Mr Nimal Fonseka of Senstone Limited, for the Appellant

Ben Elliott, counsel, instructed by the General Counsel and Solicitor to Her Majesty's Revenue & Customs for the Respondents

DECISION

Introduction

1. Mr Kieran Looney, both in his personal capacity and as the nominated partner of Kieran Looney & Associates ("KLA") appeals against the decision of the First-tier Tribunal (Tribunal Judge Rupert Jones and Tribunal Member Noel Barrett – "the FTT") released on 16 October 2018 (published as *Looney, Kiernan Looney & Associates (Partnership) v Revenue & Customs* [2018] UKFTT 0619 (TC)) ("the FTT Decision").

2. The matters giving rise to the appeals relate to a contract under which KLA agreed to provide management training to the senior management of Trafigura Beheer BV, a substantial commodities trading company. The appeal before the FTT concerned, amongst other matters, the tax treatment of certain payments made in relation to that contract being:

1) a payment of £1 million made on the early termination of the contract;

   The FTT rejected Mr Looney's case that the payment was capital (compensation for loss of a secret process in Mr Looney's proprietary performance management system) and upheld HMRC's analysis that the payment was consideration for the cancellation of the contract and therefore a trading revenue receipt ("the Termination Payment Issue").

2) payments under the contract totalling £3 million.

   The FTT rejected Mr Looney's case that the payments were not part of the income and turnover of KLA (as opposed to other entities Mr Looney owned – Kieran Looney and Co Limited (KLCL) and a Panamanian company (Nower Inc.)) ("the Income Recognition Issue").

3. The Upper Tribunal ("UT") granted permission to appeal in relation to the above issues. We have set out the grounds on which permission was granted in more detail below when we come on to discuss the grounds of appeal. The scope of what is before us in the UT encompasses two appeals: first an appeal against an HMRC decision amending KLA's partnership return (the partnership appeal) which concerns both the Termination Payment Issue and the Income Recognition Issue and second an appeal by Mr Looney against a closure notice but which was only in relation to the partnership profits. The results of the closure notice appeal therefore follow automatically from the outcome of the partnership appeal.

The background facts

4. The FTT's findings of fact are set out in the FTT Decision. We have summarized the key findings that are relevant for the purposes of this appeal below.

5. KLA carried on the trade of business coaching from 1 October 2003 until the partnership dissolved on 22 December 2009 (FTT [30]). The partners of KLA were Mr

Looney and Reality Coaching Limited. Mr Looney and his wife were shareholders and directors of that company (FTT [27] and [29]).

6. KLA entered into an agreement with Trafigura to provide management training for Trafigura's senior management on 14 January 2009 (the "KLA Proprietary Performance Management System Program" or the "KLA Program") (FTT [32]).

Contractual provisions

7. The terms of certain provisions of the contract were extracted in the FTT Decision (FTT [32]-[44]). We focus on the terms relevant to the issues before us.

8. The contract commenced on 14 January 2009 and it was agreed that it would continue for 36 months from that date (FTT [33]).

9. The terms and conditions which governed the fees charged under the contract were set out in Attachment 2. They provided for:

> (1) an annual fee of £3 million to be paid for each of the three years of the contract (Paragraph 3).
>
> (2) the payment of a non-refundable deposit of £2.4 million immediately on signing the contract and £600,000 on 1 August 2009 for "KLA Train the Trainer" (Paragraph 3) (FTT [37]).

10. The term of the agreement would cover the initial part of the curriculum and three years' subsequent use of materials on licence, after which the licence would be assigned to Trafigura for continued use; Trafigura could then continue to use the performance management system at no extra cost (Clause 1.3).

11. The KLA Program 'Materials' were to remain the absolute property of KLA during the term of the contract (Clause 1.5) (FTT [34]). The terms and conditions for the use of the Materials were contained in a further attachment (Attachment 3). Any Materials provided were to be used only by Trafigura during the course of the KLA Program or otherwise as expressly licensed by KLA (Paragraph 1.5 of Attachment 3) (FTT [42]). All Materials would remain the exclusive property of KLA (Paragraph 2.1), and all Materials had to be returned at the end of the Program or any subsequent licence period (paragraph 2.7) (FTT [43]).

12. Trafigura would be granted a lifetime licence provided that the entire KLA Program was completed and the early termination provision (Clause 1.10 – which we set out below) was not invoked (Paragraph 2.9).

13. The contract was non-assignable and was not to be varied except in writing by an authorised signatory of each party (Clause 1.12).

14. Clause 1.10 provided that the KLA Program would be discontinued on the service of a termination notice by Trafigura and the payment of the early termination fee. Upon the service of the notice and payment of the fee, the parties' obligations under the

contract would terminate (with the exception of certain provisions including those relating to confidentiality). Clause 1.10 was in the following terms:

> "Early termination may only occur on written notice on the basis set out in the Financials [*defined as the fees, payment terms, cancellation and other terms in Attachment 2*]. On Trafigura serving written termination notice and paying the early termination fee the Program will be discontinued and Trafigura and KLA will have no further obligations to the other in relation to payment or delivery of the Program respectively except that the confidentiality, Materials terms and other provisions of this agreement intended to apply after termination will continue to apply with full force and effect. If no written notice is served under and in accordance with the timescale set out in clause 2.5 Trafigura will pay the license fee for 2010 by 15th December 2009, and the license fee for 2011 by 15th December 2010."

15. Paragraph 5 of Attachment 2 headed "Early termination" specified:

> "Written notice must be received by KLA on or before 1st November 2009. Non-refundable deposit + £1,000,000 early termination fee to be paid to KLA within fourteen days of notification
>
> Otherwise 100%"

16. As we mention below, the scope of the early termination provisions was later litigated between KLA and Trafigura in proceedings before the High Court.

17. Trafigura made payments of £2,343,522.70 and £500,000 on 4 February 2009 and 5 August 2009 to the Swiss PFK bank account of Nower Inc, a Panamanian company of which Mr Looney was the director and shareholder and which Mr Looney had incorporated on 14 January 2009 at or around the time when KLA entered into the contract with Trafigura (FTT [72] and [77]). The balance of the £3 million had previously been paid by Trafigura directly to Mr Looney[1] (FTT [39]).

18. On 9 April 2009, Mr Looney incorporated Kieran Looney and Co Limited (KLCL) (FTT [51] and [73]).

19. KLA carried on the trade of business coaching until both it and Reality Coaching Ltd (the other partner in KLA) were dissolved on 22 December 2009 (FTT [28] and [30])[2].

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[1] Whether that balance referred to sums due under the deposit or the provision requiring a £3 million annual fee is unclear. The reference in FTT[39] to £500,000 being paid on 5 August 2009 (as opposed to the £600,000 due under the contract), and to the balance having been paid previously would appear to reflect at least in part that, as recorded in the High Court Proceedings Mr Looney took against Trafigura (reported at [2011] EWHC 125 (Ch) – (see paragraphs [9] and [15] of that decision), Mr Looney had agreed the contract should incorporate a coaching agreement he had entered into earlier with Trafigura's CFO for a fee of £100,000 and that he would refund payments he had received under that agreement to Trafigura.

[2] Although FTT [28] records that Mr Looney ceased as a partner on 22 September 2009, it is not clear to us how, if that was correct, and in the absence of any suggestion anyone else replaced him

20. Trafigura gave notice of early termination on 20 October 2009 and paid the £1 million early termination fee to KLA on 29 October 2009 (FTT [79]).

High Court Proceedings

21. In December 2009, Mr Looney brought a claim against Trafigura in relation to the termination of the contract on the basis that the termination clause had not been lawfully invoked.

22. The particulars of claim alleged Trafigura was in repudiatory breach of contract by terminating it without reasonable cause and claimed damages for the loss of earnings on the remainder of the contract. In respect of intellectual property rights, it was alleged Trafigura had drawn on the KLA Program to develop its own training programme called TrafiTalent (FTT [96]). In the particulars of claim, Mr Looney "reserved all of his rights concerning infringement of copyright and breach of confidentiality…in respect of the [KLA Program] pending clarification of the precise ambit of TrafiTalent" (FTT [49]).

23. Following a hearing which took place in December 2010, Newey J (as he then was) dismissed the claim for damages for breach of contract in a judgment handed down on 1 February 2011. He concluded Clause 1.10 did not restrict Trafigura to being able to terminate the contract only on "proper and reasonable grounds". The reasons given by Newey J (at [90] of the High Court's decision) included that there was a rational basis for the incorporation in the contract of a clause permitting Trafigura to terminate on notice without having to show it had good reason for termination. This had come out in the evidence of one of Trafigura's witnesses; in effect to avoid argument over whether "soft skills", which were difficult to quantify, had been delivered by having a transparent mechanism or break clause (FTT [48]).

24. The High Court also concluded that the KLA Program did not have any significant impact on the development of Trafigura's own performance management programme, TrafiTalent.

The FTT Decision

25. The FTT devoted [71] to [97] of its decision to setting out Mr Looney's submissions together with the evidence Mr Looney had given, explaining the evidence and submissions which the FTT rejected, and the findings of fact it accordingly made.

26. Regarding the Termination Payment Issue, the FTT recorded Mr Looney's claim that the compensation was received as a payment for the continued use of the secret processes used (or intellectual property) in his unique computerised management

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as partner, that the partnership could be said to continue until 22 December 2009 with only one partner (Reality Coaching Ltd). The only source we could find for the FTT's finding was in HMRC's skeleton argument before the FTT. It was not clear however what the evidential basis for that suggested fact was, whereas there was evidence before the FTT (Mr Looney's witness statement) regarding KLA continuing until 22 December 2009. Give that, and as it was not in contention that the partnership dissolved on 22 December 2009, we proceed on the basis KLA remained in existence with both Mr Looney and Reality Coaching Ltd. as partners until 22 December 2009.

performance system, which Trafigura used both during and after his period of engagement with them (FTT [90]). His evidence was that he had placed the compensation term in the Trafigura agreement to compensate for that use, that he realised once the system was in place it would be very difficult to ensure it was not used by Trafigura after the contract terminated, and that the £1 million sum (which vastly undercompensated him for the use of his proprietary product) was intended to be net of taxation (FTT [91]).

27. As regards the Income Recognition Issue, the FTT considered which of the entities associated with Mr Looney should be regarded as involved with the arrangements with Trafigura. Mr Looney's evidence was that once the Trafigura contract was signed with KLA "it dawned on him that the best way of operating the business was probably through a company". He set up Nower Inc. a company incorporated in Panama of which he was the sole director and shareholder for this purpose and opened a bank account for it in Switzerland to receive the payments from Trafigura (FTT [72] and [77]). Mr Looney recalled that his adviser, Mr Fonseka subsequently advised him to account for the monies from Trafigura in the UK through a UK company "to avoid any allegations of tax evasion by HMRC". He followed this advice and in April 2009 set up KLCL, a company incorporated in England and Wales (FTT [73] and [74]). Mr Looney stated he agreed with Trafigura to change the terms of the contract and, in effect, to novate the rights and obligations in the contract to Nower (FTT [75]). He claimed he could elect which entity should declare the income and that he recognised the income in KLCL (FTT [87]). HMRC, he submitted, was wrong to include these sums as partnership income (FTT [83]). He claimed the £1 million compensation payment was paid in error by Trafigura to his personal / KLA bank account and not to Nower (FTT [89]).

28. The FTT rejected Mr Looney's evidence both in relation to the termination payment, and also regarding his claim that the rights in the agreement were novated to Nower or any other entity such as KLCL. Accordingly, and as we have mentioned above, the FTT decided: on the Termination Payment Issue, that the payment was part of KLA's trading income and not compensation paid to acquire a secret process or intellectual property rights; and, on the Income Recognition Issue, that the payments were part of the income or profits of KLA (and not the income or profits of KLCL or Nower).

29. We have addressed the reasons for the FTT's conclusions and the reasons why it rejected Mr Looney's case later in this decision notice, when we discuss the grounds of appeal before us and the parties' submissions on those.

Grounds of Appeal

30. Permission to appeal was refused by the FTT and, on the papers, by the UT (Judge Richards). Following an oral hearing, the UT (Judge Richards) granted permission on two grounds.

Ground 1: the Termination Payment Issue

31. The first ground on which the UT granted permission to appeal was that:

> "The £1m termination payment that Trafigura made was capital in nature. The FTT was therefore wrong to conclude that it constituted taxable income."

Case-law on capital or revenue nature of compensation payments

32. There was no real dispute to the general approach to be taken in traversing this "well trodden territory" (as Moses LJ put it *Able (UK) Ltd v HMRC* [2007] EWCA Civ 1207).

33. HMRC referred us to an extract from the judgment of Arden LJ in *IRC v John Lewis Properties plc* [2002] EWCA Civ 1869 (at [13] and [14]), which although dissenting encapsulated the approach by reference to various authorities including the Sir Nicholas Browne-Wilkinson VC's judgment in *McClure (HMIT) v Petre* STC 749 at 754:

> "In my judgment it is equally established by authority that to decide whether a particular receipt is in the nature of income or in the nature of capital one has to look at all the circumstances of the particular case and apply judicial common sense in reaching a conclusion as to how the receipt is to be classified".

34. The issue is thus one of "fact and degree and above all judicial common sense in the circumstances of the case"[3]. Pausing here, this feature has implications for how quick an appellate court should be to interfere with the fact-finding tribunal's evaluation. This was highlighted by Lawrence Collins LJ's statement, to which HMRC referred us, in *Able*, that there was much to be said for the view that: "where the answer to a question is a matter of degree, taking account of all the circumstances, then an appellate court should show some circumspection before interfering with the decision at first instance". In a similar vein, Buxton LJ in *Able* while acknowledging (at [28] of his decision) that the issue was an issue of law, was of the view it was a special sort of issue as it had to be determined from a practical and business point of view.

35. When it comes to the approach to be taken to the correct characterisation of compensation, the relevant questions, as illustrated by the approach taken in *Able* (per Moses LJ at [5]) which concerned statutory compensation received by a landfill tipping site operator following a compulsory purchase order of part of the site, were:

> "Firstly, what was the compensation paid for? Secondly, would the sum which the trader ought to have received have been credited as income receipt of the trade (See Diplock LJ in *London and Thames Haven Oil Wharves Ltd v Attwooll (Inspector of Taxes)* [1967] Ch 772 at 815…"

36. While it is clear, following the principles above that the correct characterisation of a payment as capital or revenue will very much depend on the particular circumstances of the case, Mr Looney's case is that principles derived from the House of Lords case

[3] As referred at [21] of Lawrence Collins' judgment in *Able* to Lord Upjohn's statement in *Regent Oil Co Ltd v Strick (Inspector of Taxes)* [1966] AC 295 at 313

of *Evans Medical Supplies Ltd v Moriarty (H M Inspector of Taxes)* [1957] 37 TC 540[4] and the factual similarities of that case are of key relevance. In *Evans Medical*, the relevant payment related to acquisition of secret processes and was found to be capital in nature. Mr Looney submits, contrary to HMRC's position, that the FTT were wrong to distinguish the facts of that case as they did and wrongly applied the principles from the case.

37. In *Evans Medical*, the appellant company manufactured pharmaceutical products world-wide including in Burma where it carried on business through an agency. Under an agreement with the Burmese Government, the company undertook to disclose secret processes concerning the preparation, storage and packaging of pharmaceutical products and other information (drawings and designs for a new factory and machinery) in return for £100,000 "capital payment" and £20,000 per annum, which was accepted to be trading income, to operate and manage a factory. The company could continue to operate its agency in Burma and to use its processes for its own commercial purposes and the Burmese Government were under obligations not to disclose the processes to others without the company's consent. The issue was whether the £100,000 was a trading receipt. The Special Commissioners found the entire contract was for the provision of services so the £100,000 was trading income (as was the £20,000 annual fee). The High Court found the £100,000 was capital. The Court of Appeal unanimously held the payment was a trading receipt, except to the extent that it was attributable to the disclosure of the secret process, in which case it was a capital receipt. The House of Lords dismissed the Revenue's appeal; a majority, Viscount Simonds, and Lords Tucker and Denning, held it was not open to the Court of Appeal to apportion the sum and accordingly the entire payment was a capital receipt.

38. Viscount Simmonds rejected any argument the company had not sold or assigned any property confirming (at 578) that a secret process was something "which can be disposed of for value and that by imparting the secret to another its owner does something which could not fairly be described as "rendering a service". He did not think authority was needed for "so obvious a proposition" but that it could be found in *Handley Page v Butterworth* 19 TC 328. (Mr Looney's skeleton relied on an excerpt from that decision which appears in Lord Evershed MR's judgment in the Court of Appeal in *Evans Medical* at 561).

39. Viscount Simmonds then identified that the question remained, assuming the sum was for the sale and purchase of an asset, whether it was a capital asset and concluded the evidence was overwhelmingly that it was. The sum received was a capital sum. He continued:

> "…Of paramount, if not decisive, importance is the agreement itself. I need not repeat its recitals or its terms. The Company parted with something for which the Government was prepared to pay no less than £100,000. Its possession had secured for the Company a substantial share of the Burmese market: its loss will mean, in the words of the Commissioners, that "the Company's Burmese agency will become

[4] Also reported at 1958 1 WLR 66

> progressively less important", or, in other words, that the Company has parted with an asset which was the source, or one of the sources, of its profit. I venture to repeat the question stated by Bankes, L.J., in *British Dyestuffs Corporation (Blackley), Ltd. v. Commissioners of Inland Revenue*, 12 T.C. 586, at page 596:
>
> > ". . . looking at this matter, is the transaction in substance a parting by the Company with part of its property for a purchase price, or is it a method of trading by which it acquires this particular sum of money as part of the profits and gains of that trade? "
>
> I look accordingly at this transaction and, with all respect to those who take a different view, do not see how the question can be answered except by saying that the Company has parted with its property for a purchase price, and when I say " its property " I mean, as Bankes, L.J., meant, a capital asset."

40. As he went on to explain, it did not matter, as the Revenue were arguing, that divulging a secret process to another person, as opposed to the whole world, would not be regarded as parting with a capital asset:

> "…The whole value of the secret might conceivably not be lost at once to the original owner, but that its value must be greatly diminished is obvious: in the present case it is doubtful whether within a measurable time it will have any value at all, at any rate so far as the Burmese market is concerned."

41. Lord Tucker agreed with Viscount Simmonds. Lord Morton agreed with the Court of Appeal that the imparting of secret processes was a capital receipt but fell to be apportioned out of the £100,000 payment. Lord Keith (dissenting) held the company was trading in "know-how". While Lord Denning did not agree that "know-how" could be sold as a capital asset, he dismissed the appeal on the basis the payment could not be brought into the assessment because it was not received in the course of the company's existing trade.

The parties' submissions on the case law authorities

42. Mr Fonseka's case on behalf of Mr Looney, as elaborated in his skeleton, is that the FTT wrongly applied the propositions of law set out in *Evans*. The first excerpt he relies on is actually taken from *Handley Page* decision[5] (which was referred to in the Court of Appeal's decision in *Evans*[6]) to the effect that possession of secret process is a capital asset. The extract makes the point that profits derived from a person carrying out the secret process for himself or the royalties derived by granting a license for another to use it on terms securing that the process is not divulged to third parties would be taxed as income. But, if the secret process were sold or, as on the facts of *Evans*, the person surrenders a quasi-monopoly by making it public, the money the person receives in payment for either of those things is a capital receipt for the disposal of a capital asset.

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[5] (1935) 19 TC 328 per Lord Romer at page 359

[6] (1957) 37 TC 540 at page 561 and [1957] 1 WLR 288 per Lord Evershed MR at page 304

43. Mr Looney's skeleton further relies on *Evans* to support the proposition that a secret process, once communicated to another, is in jeopardy; if it gets into the wrong hands the grantor has no protection. He also refers to passages in *Evans* which make the point that even though the Burmese government pledged not to divulge the information they would possess it for ever (Upjohn J 552 quoted in Evershed MR at 559, and Romer LJ at 566). However, these passages, whilst helpful guidelines, were not, we think, laying down a general proposition. They were simply factors which were taken into account as part of all the circumstances of that case in arriving at a common sense conclusion on the categorisation of the payments in that case.

44. On the general principles which Mr Fonseka seeks to derive from *Evans Medical* and *Handley* Page, there is no argument however between the parties. HMRC accept that a secret process may amount to a capital asset, that the sale of a secret process (as opposed to its licence or use) can amount to a disposal of a capital asset, and that there can also be a disposal of a capital asset even where the disposer retains rights but the circumstances are such that on the facts, the value of the asset is greatly and permanently diminished. (In *Evans*, this arose from the fact the activities of the company's Burmese agency would become progressively less important – [39] above). Rather the dispute is as to whether the FTT erred in the application of such principles on the facts; in particular Mr Looney argues that the FTT was wrong to distinguish the facts of this case from those in *Evans* as, he says, the facts were in all material respects the same as in *Evans*.

The FTT's Decision regarding nature of the termination payment

45. The section of the FTT's Decision dealing with the termination payment was at [152] to [166] which began by setting out the relevant parts of the contract and the parts of the High Court's judgment on Clause 1.10. For the reasons summarised below, the FTT rejected Mr Looney's evidence (FTT [163]) and concluded the purpose of the payment was to compensate KLA for the lost opportunity to trade and profit from the remaining two years anticipated under the contract:

> (1) On the plain wording of Clause 1.10, the termination payment was not expressed to be compensatory for acquisition of intellectual property rights or secret process contained in KLA Program. Furthermore, numerous contract provisions excluded Trafigura from using, acquiring or licensing the intellectual property except where the contract ran its full three-year term (FTT [159] and [162]).
>
> (2) Mr Looney's particulars of claim in his High Court case did not suggest the payment was for compensation for the loss of the secret process - the particulars suggested Trafigura was in repudiatory breach and claimed damages for loss of earnings on remainder of contract. Such intellectual property breach as was mentioned was in relation to the unrelated allegation that Trafigura drew on KLA Program to develop its own programme (FTT [159]).

(3) Such purpose was consistent with the finding in the High Court decision that purpose of the Clause 1.10 was to compensate or provide consideration for the early termination of the contract (FTT [159]).

(4) After setting out the contract terms in *Evans* which provided for payment in return for the company agreeing to provide and make various information and "know-how" available to the Burmese Government, the FTT distinguished *Evans* on the basis the contract terms in that case "could not be further" than those provided under the termination clause. The transaction did not provide for KLA to part with a capital asset (the KLA Program or any other intellectual property or right to a secret process) for a purchase price but was a method of trading by which KLA acquired a particular sum of money as part of the profits and gains of its trade (FTT [165]).

The parties' submissions on the evidence before the FTT

46. Mr Looney submits the FTT erred in its analysis. The contract was silent on the reasons for the payment of the early termination fee and did not provide evidence either way on the issue. The FTT had to look behind the contract for the reasons for the payment. The only evidence before the FTT for the reasons behind Clause 1.10 was that given by Mr Looney in his witness statement that the compensation was received as a payment for the continued use of the secret processes. This was supplemented by his oral evidence that the clause was necessary as a disincentive for Trafigura to copy the processes which he had had to reveal to them in order to implement the programme. (We should note there was an inconsistency with this in how Mr Fonseka put his reply – he suggested Mr Looney was not concerned about Trafigura plagiarising his programme).

47. That oral evidence also suggested that the secret processes had a higher value than the sum payable under the early termination clause. The £1 million payment was only a fraction of the lost contract value and was more accurately to be described as a form of tax-free capital resource to be used to sustain the business. Mr Fonseka referred also to the fact the High Court claim was for £5 million damages representing the loss of fees over the next two years; it could not represent compensation for loss of earnings under the contract because the amount was too low. The significance of the loss of the intellectual property rights was evident from the subsequent lack of demand for work from Mr Looney and the drop in his income as could be seen from his subsequent tax returns.

48. HMRC's case, in summary, was first that the contract was not neutral. It did not suggest that any intellectual property rights had been transferred to Trafigura. The terms of the contract were clear that KLA retained full ownership of the intellectual property rights in the KLA Program and the Materials. The purpose of the payment was to compensate KLA for the early termination of the contract. Second, Mr Looney's evidence, which only went to his subjective understanding of what the payment was for, was rejected (because of the terms of the contract, business common sense, and his behaviour regarding the High Court proceedings, and as corroborated by the High Court's findings). From all of those matters the FTT clearly formed the view Mr

Looney's evidence was self-serving. There was nothing close to a successful *Edwards v Bairstow*[7] challenge to show the evidence should be restated in the way Mr Looney's case implied.

Discussion

49. Under s11 Tribunal Courts and Enforcement Act 2007 appeals to the UT are limited to points of law and thus to the question of whether the FTT made an error of law in its decision which needs to be corrected.

50. The FTT had before it the contract under which the payment was made, Mr Looney's evidence and findings made in a High Court judgment (but in proceedings involving different parties) and details of the particulars of claim Mr Looney had filed in that case. While it does not appear from the FTT's decision that it was referred to many of the authorities to which we were referred regarding the general approach to be taken to questions of whether a payment was capital or revenue, given, as identified above, that these cases direct the tribunal to look at all the facts and circumstances of the particular case and apply judicial common sense, which in this case would entail looking at contract under which payment was made and the wider circumstances we cannot see any material error in the FTT's approach.

51. The starting point was the contract. There is nothing in those provisions which suggests the FTT erred in its analysis. It correctly observed there was nothing in Clause 1.10 which suggested that the payment was made in respect of intellectual property rights or secret processes, and that other provisions excluded use and licensing of the KLA Program except where the full three years were seen out. There was nothing on the face of the agreement which transferred intellectual property rights or secret processes to Trafigura.

52. Mr Looney's evidence was really a disguised submission and at best subjective evidence as to what he thought the contractual provision concerned. But, whatever limited value that would have in the analysis, the FTT was entitled to reject it for the reasons it did. It was not consistent with the drafting of Clause 1.10 under which the payment was made or the wider provisions of the contract mentioned above. It was also not consistent with how Mr Looney had argued his case regarding the termination fee as disclosed in his particulars of claim before the High Court and it did not take into account the fact that the only claim regarding a breach of intellectual property rights in the High Court proceedings was the unrelated allegation of the use of the KLA Program to develop TrafiTalent.

53. As regards the significance of the High Court findings we pressed Mr Elliott, counsel for HMRC, on the relevance of its judgment, given it concerned different parties. He readily acknowledged the findings could not be binding on the FTT, but we agree the FTT did not regard them as such. Rather and as Mr Elliott put it, the FTT

[7] [1956] AC 14

"drew comfort" from the High Court's findings as they served to corroborate the FTT's analysis of the nature of the payment.

54. There was accordingly nothing in the surrounding circumstances which were before the FTT which indicated the payment was as Mr Looney was arguing. (While Mr Elliott took us to other excerpts from the FTT's decision concerning matters which are not under appeal before us where the FTT had rejected Mr Looney's evidence, we do not agree these provided further support for the FTT's rejection of his evidence. It is clear to us the FTT was not approaching Mr Looney's evidence in that manner, rather it was testing it against the other evidence before it in relation to particular issues– the fact it rejected his evidence in one area did not provide a reason for rejecting it in other areas.)

55. We also consider the FTT was correct to conclude *Evans Medical* did not advance Mr Looney's case. While the FTT distinguished the case on the basis of the wording and effect of the contractual provisions - in *Evans* the secret process was clearly transferred under the agreement whereas in Mr Looney's case the agreement did not effect the transfer of any intellectual property rights - the more significant reason why the principle in that case did not apply was because there was no evidence before the FTT of permanent diminishment of the relevant intellectual property. Mr Looney's case, in essence, is that irrespective of the contractual provisions once the secret process was disclosed the reality was that it then became of little value. It thus echoes what Viscount Simonds in the House of Lords in *Evans Medical* noted regarding the Burmese market being progressively less important to the appellant company and Romer LJ's analysis in the Court of Appeal's decision ((1957) 37 TC 540 at page 566) which looked beyond the letter of the contractual provisions to the reality on the facts of that case. (Romer LJ rejected, as unrealistic, the Revenue's submission that the value of the secret processes was not impaired as there was nothing under the agreement to prevent the company exploiting its knowledge for its own commercial purposes and the Burmese Government had promised not to further divulge the information).

56. However, Mr Looney's difficulty is that his claim that value in his intellectual property/secret process was lost is not one which was supported on the facts that were before the FTT. As HMRC point out, there was no evidence before the FTT on the point on which to make a finding that the value of any intellectual property rights had been diminished as a result of the agreement with Trafigura. There was no evidence that Trafigura divulged any intellectual property to others or took advantage of the intellectual property itself in breach of the agreement or that the value of the intellectual property was otherwise diminished. That there was no breach of the agreement was consistent with the findings of the High Court in so far as those were relevant. While Mr Fonseka submitted, in the hearing before us, that there was a drop in demand for Mr Looney's services, as he said could be seen from Mr Looney's subsequent income tax returns, there appears to have been no evidence to that effect upon which the FTT could make such findings of fact, or for that matter before us. Further, as HMRC say, any drop in demand for Mr Looney's services could be due to any number of factors aside from loss of his secret process or intellectual property.

57. As to Mr Fonseka's point about the amount payable under the clause being too low, there is nothing in the amount which appears at odds with its characterisation by the

FTT; it reflects that when a contract is terminated early, costs that might otherwise be incurred in fully performing the contract both in terms of time and resource are not incurred. Also, as HMRC say if the clause was not a clause dealing with termination it would be strange that there was then no provision in the contract regarding loss of earnings through cancellation.

58. Standing back, we ask ourselves: did the FTT err in its task of looking at the circumstances and applying judicial common sense? We consider it did not make any such error and that there is no basis for interfering with the FTT's conclusion regarding the characterisation of the termination payment. It was quite clearly open to it to reach the conclusion it did on the materials that were before it (the contract, the subjective evidence of Mr Looney which it rejected anyway, but even if it had not would only have been of very limited weight, and the consistency of its view with findings in the High Court). We also bear in mind the injunctions in the case-law (see [34] above) that we should be slow to interfere with a first-instance tribunal's evaluation. That provides all the more reason to reject the argument that the FTT erred in law in its conclusion regarding the characterisation of the £1 million payment. HMRC put forward various other reasons why the FTT would have been entitled to reach the conclusion it did but given our conclusion above we do not need to consider those.

Ground 2: the Income Recognition Issue

59. The second ground on which the UT granted permission to appeal was as follows:

> "The FTT should have concluded from the evidence it was shown that there was a multi-party arrangement involving all or any of (i) Mr Looney; (ii) Nower Inc; (iii) KLCL and (iv) KLA to the effect that sums Trafigura paid under the contract were to be enjoyed by KLCL. Moreover, the FTT should have concluded that this arrangement had the effect that this arrangement meant that neither Mr Looney nor KLA was subject to tax on sums Trafigura paid and, instead, KLCL was liable to tax on those sums."

60. In granting permission in the UT, Judge Richards made it clear that no permission to adduce new evidence was being given and the ground would have to stand or fall by reference to the evidence which was before the FTT.

The FTT Decision

61. To put the relevant parts of the FTT's decision in context, it must be recalled that the argument put to the FTT was that the rights in the contract had been assigned or novated to Nower or to another entity such as KLCL. The FTT's findings and reasoning were accordingly principally addressed at this issue. The FTT summarised the evidence Mr Looney gave regarding the circumstances in which Nower and KLCL were set up including his reasons for setting them up when he did (FTT [71] onwards). Noting there was nothing in writing to evidence the alleged variation (as required by the Clause 1.12) or regarding Trafigura's reasons for so agreeing, or as to who had agreed it, the FTT rejected his evidence that he or KLA assigned, transferred or novated rights of KLA to Nower or any other entity such as KLCL (FTT [78]). It concluded HMRC had been

right to include payments of money under the contract (£3 million and £1million) as income of the KLA (FTT [84]).

62. In its reasoning (FTT [135] to [151]) which referred back to its earlier rejection of Mr Looney's evidence the FTT started by noting the agreement was made between KLA and Trafigura (FTT [136]). It noted that KLCL was not a contracting party, that it was not in existence when the contract was formed in January 2009 and that by the time it was incorporated in April 2009 the majority of the money paid pursuant to the contract (£2.3 million) had already been paid by Trafigura (FTT [144] and [145]). It was satisfied the sums paid by Trafigura to Nower and KLA bank accounts were attributable and due to the KLA and no other entity (FTT [146]).

The parties' submissions

63. Before us in the UT, Mr Looney no longer maintains that there was any novation, transfer or assignment. His challenge was reformulated in the following way. He maintains he was entitled to transfer monies (income and expenses) between the various entities he owned using cross management charges. There was no written agreement, but there did not need to be as Mr Looney owned the relevant entities (and HMRC do not make any point on the lack of a written agreement). His case is that the FTT ought to have inferred from the following sequence of events that there was a multi-party agreement: Mr Looney, on behalf of KLA, signed an agreement with Trafigura; he then asked Trafigura to send money to Nower Inc.; he then incorporated KLCL and wound-up KLA; and KLCL accounted for the relevant monies in its VAT return.

64. HMRC do not dispute that the relevant parties could in principle have made a multi-party agreement, but submit that there is no evidence any such agreement was entered into. Crucially for the agreement to have the tax consequences Mr Looney was seeking (showing the liability was not that of KLA) it would have to be shown 1) that the entity transferring or paying charges had an expense in its accounts 2) that the expense was wholly and exclusively for purposes of the trade (under s 34 Income Tax (Trading and Other Income) Act 2005).

Discussion

65. We can deal with this ground in short order. We agree with HMRC. There is insufficient evidence from which the multi-party agreement, with the tax effect contended for, might be inferred. As explained above the FTT clearly rejected Mr Looney's evidence. Even if that rejection was limited to rejecting his rationale for setting up Nower Inc and KLCL when he did, a tribunal faced with the remaining bare facts as to when the various entities were set up would be more than entitled to reject the submission that it thereby followed that a multi-party agreement had been formed.

66. The other evidence before the FTT also did not support the inference of a multi-party agreement.

(1) There was no mention of the relevant sums as an expense in the partnership accounts of KLA as filed originally, and even in those which were then subsequently amended (see FTT [31] and [64]),

(2) The statement in Mr Looney's statement of case in the FTT proceedings that the money was accounted for in KLCL to which Mr Fonseka drew our attention in his reply, was not contested by HMRC. However, it was not in dispute that KLCL accounted for the money in that way. Whether it was correct to do so was clearly in dispute. The fact KLCL treated the money as it did does not necessitate any finding that the money so accounted for was received pursuant to a multi-party agreement between the entities with which Mr Looney was involved.

67. As we have mentioned, Mr Fonseka directed us to the VAT returns of KLCL as evidence of a multi-party agreement between the parties. Even if these entries could support the inference of an agreement between some of the parties – which we do not accept – there was no evidence on this point before the FTT. The grounds on which Mr Looney and KLA have permission to appeal expressly excluded the introduction of new evidence in support of this ground.

68. For these reasons, in our view, there was no error of law in the FTT failing to find that there was a multi-party agreement with the effect contended for and this ground of appeal must be rejected.

69. We do not therefore need to deal with the issue that HMRC sought permission to raise in their respondent's notice, as to whether, in any event, the transfers were wholly and exclusively for the purposes of the trade.

70. While Mr Looney sought to raise before us a number of further alleged errors: that the contract with Trafigura was not with KLA but with Mr Looney personally, that the FTT ignored that its decision would result in double taxation given HMRC's taxation of sums in KLCL, and that the UT should in any event allow Mr Looney to claim capital allowances in relation to the expenditure incurred on his know how, none of those were issues in relation to which permission was granted and indeed some, such as the capital allowances point, were specifically refused. We do not therefore deal with these points except to record that HMRC confirmed before us, as they did before Judge Richards at the oral renewal of permission hearing before him, that they did not seek to collect tax on the same sums from both Mr Looney and KLCL.

Decision

71. For the reasons above neither ground shows the FTT erred in law. We therefore dismiss the appeal.

Swami Raghavan
Judge of the Upper Tribunal

Ashley Greenbank
Judge of the Upper Tribunal

Release date: 22 April 2020