



## FIELD COURT TAX CHAMBERS

### **Expenses: the wholly and exclusively test<sup>1</sup>**

#### *Examining the subconscious*

Everybody knows that to obtain an income tax deduction for an item of expenditure, it has to be incurred wholly and exclusively for the purposes of the trade (ITTOIA 2005 s 34). These words (in their present and earlier incarnations) have given rise to an enormous amount of argument (and cases) and will continue to do so.

A problem with such claims is often the concept of duality of purpose. If the expenditure has more than one purpose, none of it is allowable. (Although for some reason, if the expenditure is incurred by a company, an apportionment is allowed under CTA 2009 s 54(2)).

The classic case on the subject is *Mallalieu v Drummond* [1983] 57 TC 330 where a barrister claimed the cost of her court clothing as a business expense. The House of Lords said this was not incurred wholly and exclusively for the purposes of her profession because one of her objects was to serve her needs as a human being. The fact that the clothes were only for the purposes of wearing in court and would never have been used for any private purpose, was not enough to displace the duality of purpose.

The test is not the use made of the clothing but the purpose for which they were purchased. She only had one purpose in mind – that was her professional purpose because she would not have been allowed to appear in court in other clothing. Still not good enough. The House of Lords said that she must have had a subconscious purpose of meeting her needs as a human being, and that subconscious purpose was enough to disallow the expenditure.

This is the law, and it remains the law, despite the fact that it has caused decades of disappointment to taxpayers who simply cannot understand why they are not allowed a deduction for what is quite obviously a genuine business expense.

This makes life rather difficult. If when redecorating my office, I decide that I would like the walls painted white because I prefer white to any other colour, why is that not disqualified from relief? Similarly, if I buy a computer for my office with a huge screen because I (perhaps subconsciously) want to feel important, my personal purpose clearly disqualifies the expenditure from relief. Indeed, it is virtually (if not completely) impossible to imagine incurring any expenditure which does not have some element of personal purpose. You turn the office heating on because you want to be warm. That is a basic human need – and so it goes on. But no challenge is known to have been made for these things.

In the recent case of *Rogers v HMRC* [2021] UKFTT 458 (TC), a partner in a partnership was facing a criminal charge and sought a deduction from the partnership profits for the legal costs of his defence. Why am I even mentioning this? Spoiler alert.

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<sup>1</sup> This article was first published in the InBrief section of Tax Journal published by LexisNexis on 27<sup>th</sup> May 2022.

There can be no doubt, and there was plenty of evidence, that if Mr Rogers had been convicted of this crime, it would have been very damaging to the business. Everybody agreed, but that is not the point. The point is whether Mr Rogers had a conscious (or subconscious) personal purpose for the expenditure on his defence. HMRC said he did. They said that the costs of his defence were incurred to avoid a criminal conviction, and to defend his personal reputation as well as being for the benefit of the trade.

The First-tier Tribunal (FTT) was extremely sympathetic. The FTT acknowledged that a conviction would have had an effect on the personal reputation of Mr Rogers but it was important to distinguish whether this was a reason for the expenditure or was just a lucky incidental effect. It concluded that Mr Rogers was not concerned about his personal reputation or anything other than the business when he incurred the legal fees.

The FTT expressly disregarded the fact that the criminal charge facing Mr Rogers carried a prison sentence. You might have thought that was something which would have rather concentrated his mind. The FTT said that the nature of the alleged crime was that it was unlikely that he would go to prison. Oh yes. How many defendants have been told that? Personally, I would find it absolutely impossible to put out of my mind (let alone my subconscious) that if I were convicted I could go to prison. I don't think I would be very comforted by somebody saying it is unlikely, so don't even think about it.

Mr Rogers represented himself before the FTT and clearly did a cracking job in persuading the FTT to his point of view. It would be a pity if HMRC were to appeal successfully and expose him to a liability for costs.

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