Tax update

September 2017

In this month's update we report on HMRC's new guidance on asset-based penalties for offshore inaccuracies; the GAAR Advisory Panel's first published opinion on tax planning involving gold bullion and Spotlight 39 on measures designed to avoid the 2019 EBT loan charge. We also comment on three recent cases on HMRC's failure to comply with the Tribunal Rules; obtaining a closure notice direction from the Tribunal forcing HMRC to close its enquiries and a successful appeal against a discovery assessment.

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New guidance from HMRC on asset-based penalties for offshore inaccuracies

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Eastern Power – Tribunal orders HMRC to close its enquiries despite outstanding information notices

In *Eastern Power Networks Plc and others v HMRC*, the FTT directed HMRC to issue closure notices even though there were a number of outstanding information notices. more›

Any comments or queries

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About this update

The Tax update is published on the first Thursday of every month, and is written by members of RPC's Tax Disputes team.

We also publish a VAT update on the final Thursday of every month, and a weekly blog, RPC's Tax Take.

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Gray – FTT allows appeal against discovery assessment as PAYE had been correctly accounted for

In *Gray v HMRC*, the FTT allowed the taxpayer's appeal against a discovery assessment in relation to a termination payment as there was no additional tax to assess in the relevant year and in any event the assessment was out of time. more›

News items

New guidance from HMRC on asset-based penalties for offshore inaccuracies

On 17 July 2017, HMRC published new sections in its Compliance Handbook on asset-based penalties for offshore inaccuracies and failures.

The guidance provides a summary of the legislation and considers the circumstances in which the penalties will apply. Various examples, illustrating the application of the rules and identifying assets within the scope of "asset-based income tax", are also included.

The guidance can be found here.

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GAAR Advisory Panel considers tax planning involving gold bullion and an EBT not to be "a reasonable course of action"

On 3 August 2017, the General Anti Abuse Rule Advisory Panel published an opinion on planning using gold bullion and an employee benefit trust. The Panel is of the view that the planning is not a reasonable course of action in relation to the relevant tax provisions.

The Panel opined that the steps involved in the planning were contrived, were inconsistent with the policy objectives of the legislation and were not reasonable.

The Panel's opinion can be found here.

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HMRC Spotlight on disguised remuneration loan charge

On 10 August 2017, HMRC published Spotlight 39, called "Disguised remuneration: re-describing loans".

Spotlight 39 refers to arrangements under which taxpayers declare that sums received under loan agreements from a disguised remuneration arrangement are not loans because they hold the money in a fiduciary capacity.

These arrangements are intended to circumvent the new charge that will apply to loans made to employees and the self-employed that are outstanding on 5 April 2019, under rules contained in Finance (No. 2) Bill 2017. HMRC is of the view that it is not possible to reclassify something in this manner and that such arrangements do not work.

Spotlight 39 can be found here.

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Case reports

BPP – Supreme Court confirms Tribunal was correct to strike out HMRC's case for failure to comply with rules and directions

In *BPP Holdings Ltd v HMRC*[1], the Supreme Court has confirmed that the First-tier Tribunal (FTT) was justified in directing that HMRC be barred from taking further part in the proceedings for failure to adhere to the FTT's rules and directions.

Background

The underlying case concerned the VAT treatment of supplies of books to the students of the taxpayer's law school. The Supreme Court's decision concerned non-compliance by HMRC of directions issued by the FTT. Those directions related to the provision of information that was requested by the taxpayer from HMRC in relation to the appeal. It is a fundamental aspect to all forms of litigation in England and Wales that litigants, particularly public bodies, disclose all relevant material to the claim/appeal, even if that material assists the opposing party.

Nevertheless, HMRC declined to provide the information and, thereafter, the taxpayer applied to the FTT for a direction compelling HMRC to supply the information. The FTT granted the taxpayer's application and issued an 'unless' order.

HMRC provided some of the requested information, however, the taxpayer's case was that it had still materially failed to comply with its request and the FTT's direction. On application from the taxpayer, the FTT issued a direction under Rule 8 of the Tribunal Rules barring HMRC from further participation in the proceedings.

The central question was whether the FTT Rules ought to be complied with in a manner similar to the Civil Procedure Rules 1998 (CPR), or whether the Tribunal Rules anticipated a lesser standard of compliance. The FTT considered that no such lesser standard should be applied to HMRC.

The FTT considered the approach to compliance as discussed in *Mitchell v News Group Newspapers Ltd*[2] and *Denton v TH White Ltd*[3] and noted that HMRC had failed to explain its non-compliance, and that the delay had caused prejudice to the taxpayer. HMRC appealed to the Upper Tribunal who allowed its appeal. The taxpayer appealed to the Court of Appeal.

HMRC argued that a CPR-style approach should not be applied in tax appeals before the tax tribunals. The Court of Appeal rejected this argument, and in allowing the taxpayer's appeal noted that HMRC regularly relies on the CPR by analogy in cases where it suits its arguments, remarking "the irony in that circumstance is not lost on this court".

HMRC appealed to the Supreme Court.

Supreme Court's judgment

HMRC's appeal was dismissed.

The principle question for the Supreme Court was whether it would be correct for it, as an appellate court, to interfere with the decision of the FTT. In other words, was the FTT entitled to make the debarring order.

1. [2017] UKSC 55.
2. [2013] EWCA Civ 1537.
3. [2014] EWCA Civ 906.

It was argued by HMRC that the FTT's reliance on the Court of Appeal's reasoning in *Mitchell* was not appropriate as the position had been modified by the Court of Appeal's later decision in *Denton*. The Supreme Court noted that the FTT judge had not directly applied the CPR, or the authorities giving guidance thereon, but had applied their principles by analogy. There was no indication that the FTT had misunderstood the *Mitchell* guidance and the fact that the FTT did not consider *Denton*, was not a valid reason for upsetting its decision. The Court of Appeal in *Denton* described the *Mitchell* approach as "remaining substantially sound", and the refinements contained in *Denton* were largely clarifications.

The Court was of the view that although, strictly, the approach to compliance with rules and directions made under the CPR (as discussed in *Mitchell* and *Denton*) does not apply to proceedings being conducted before the tax tribunals, it is unrealistic and undesirable for tribunals not to pay close regard to the principles enunciated in those cases.

HMRC also argued that the FTT should have accepted the relevance of, and taken into account, the fact that the debarring direction prevented HMRC from discharging its public duty to collect tax and could lead to the public interest being harmed in that VAT which should be paid may not be recovered. The Supreme Court gave short shift to this argument. It was of the view that it would set a dangerous precedent if the judge had been required to adopt such an approach as this would discourage public bodies from living up to the litigation standards expected of individuals and private bodies. The Supreme Court commented that it is arguable that the courts should expect higher standards from public bodies, such as HMRC, when conducting litigation.

Comment

This judgment is helpful and confirms that:

- the FTT can rely on the guidance provided in *Mitchell* and *Denton*
- HMRC does not have a special status and must comply with the Tribunal Rules and any directions issued by the FTT, and
- the FTT is within its rights to debar HMRC from further participation in proceedings when it has not complied with such Rules and directions.

A copy of the judgment can be found here.

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Eastern Power – Tribunal orders HMRC to close its enquiries despite outstanding information notices

In *Eastern Power Networks Plc and others v HMRC*[4], the FTT directed HMRC to issue closure notices even though there were a number of outstanding information notices.

Background

The four applicants, Eastern Power Networks Plc, London Power Networks Plc, Southern Eastern Power Networks Plc and UK Power Networks (Transport) Ltd (the Applicants), were trading subsidiaries of a shell company, UK Power Networks Holdings Limited (UK Power). HMRC opened enquiries into the Applicants' Corporation Tax returns for the periods ended 31 December 2011 to 2013, inclusive. In those returns the Applicants had claimed consortium

relief under section 133(2), Corporation Tax Act 2010 (CTA 2010).

When first incorporated, UK Power had three shareholders, Devin International Ltd (Devin), Eagle Insight International Ltd (Eagle), CKI Number 1 Ltd (CKI 1), who owned the company in equal shares. The three shareholders had some connection with the Hutchison Whampoa group, and were part of a consortium.

Hutchinson 3G UK Holdings Ltd owned Hutchinson 3G UK Ltd (Hutchison 3G), and both companies were also members of the Hutchison Whampoa group.

The surrendering company was Hutchinson 3G, who had sustained substantial losses when developing the 3G network in the UK. The "link company", for the purposes of section 133(2) was CKI1. CKI1 was owned by CKI2, which was itself owned by CKI3. Devin was owned by an energy company, Hong Kong Electric Holdings (HEH), in which CKI1 also had an interest.

The consortium subsequently acquired the power transmission business of EDF, and underwent a restructure. The articles of UK Power were amended to the effect that: the CKI companies held 74.6% of the voting rights; the voting threshold to pass shareholder resolutions was increased to 75%; and CKI3 entered into an agreement with HEH under which it contracted not to exercise its votes in UK Power without the prior written consent of HEH (the Voting Agreement). At this point the consortium comprised CKI1, CKI2 and CKI3, each of which was now also a link company.

As part of its enquiries, HMRC issued information notices to UK Power and CKI3 in November 2015 and August 2016, under Schedule 36, Finance Act 2008.

HMRC was of the view that it needed the information requested in the information notices in order to establish whether the purpose of the restructuring was to obtain a tax advantage by exploiting the consortium relief rules and to verify the quantum of the relief claimed.

The Applicants argued that the information requested was not necessary in order to determine the issues between themselves and HMRC and applied to the FTT for a direction, pursuant to paragraph 33, Schedule 18, Finance Act 1998 (FA 1998), that HMRC issue closure notices in relation to the enquiries.

FTT's decision

The FTT granted the application and directed that HMRC issue a closure notice within 30 days of the date of the FTT's decision.

The FTT rejected HMRC's submission that the mere existence of outstanding information notices prevented the issue of a closure notice. The closure notice procedure provides protection for a taxpayer seeking finality in his tax affairs. Parliament could not have intended that this could be automatically negated by HMRC simply issuing an information notice.

Consent given by the applicants in relation to the information notices did not amount to an admission that the information sought was reasonably required. The consent was given under sufferance, and had been designed to allow the applicants to challenge the notices at a hearing before the FTT. If they had not given their consent, HMRC would have sought approval from the FTT to issue the notices, in which case the Applicants would have been limited to making representations as there is no right of appeal against such notices.

4. [2017] UKFTT 494 (TC).

The FTT was of the view that questions in the notices relating to the Voting Agreement did not constitute reasonable grounds for not closing the enquiries. Whether the Voting Agreement deprived CKI3 of its voting power was a question of law (section 144(3)(d), CTA 2010). The proper place to determine that issue was at a substantive appeal hearing.

Finally, the FTT held that the request for information in relation to the purpose of the restructuring in relation to section 146B did not constitute reasonable grounds for not issuing a closure notice. This was because the purpose test in section 146B was only relevant if certain criteria were met. The CKI companies could not be prevented from exercising control over the Applicants on consideration of either the Voting Agreement or the increase in the voting threshold to 75%. The criteria were therefore not met and the purpose test did not apply.

Comment
This decision is a timely reminder of the utility of a well formulated closure notice application to the FTT.

It is not uncommon for HMRC to seek to continue with its enquiries notwithstanding the fact that it has been supplied with sufficient information and documentation to enable it to form a view on the underlying facts and close its enquiries. In such circumstances, taxpayers should give serious consideration to making an application to the FTT for a direction, pursuant to paragraph 33, Schedule 18, FA 1998, that HMRC issue closure notices in relation to such enquiries.

Taxpayers will welcome the confirmation from the FTT that it will order HMRC to issue a closure notice in appropriate circumstances even though HMRC has issued an information notice which has not been complied with.

A copy of the decision can be found here.

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Gray – FTT allows appeal against discovery assessment as PAYE had been correctly accounted for

In *Gray v HMRC*[5], the FTT allowed the taxpayer's appeal against a discovery assessment in relation to a termination payment as there was no additional tax to assess in the relevant year and in any event the assessment was out of time.

Background
Mr Gray (the taxpayer) had a contract of employment with ITV Services Limited (ITV). This contract was terminated on 31 March 2008.

On 9 April 2008, ITV paid the taxpayer £221,136 in settlement of any claims he had, or might have, against it (the Termination Payment). The first £30,000 of the Termination Payment was made without deduction of income tax or NICs pursuant to section 406, Income Tax (Earnings and Pensions) Act 2003, and the remainder was subject to an appropriate deduction for income tax at the basic rate and NICs.

The taxpayer did not notify HMRC of his higher rate tax liability.

5. [2017] UKFTT 0275.

In December 2013, HMRC issued a discovery assessment in respect of the 2008/09 tax year, pursuant to section 29, Taxes Management Act 1970 (TMA). The taxpayer contended that this was the wrong tax year and in August 2015, HMRC discharged the 2008/09 assessment and issued a new one for 2007/08 (the Assessment).

The taxpayer appealed the Assessment on the basis that the Assessment was outside the time limits permitted by section 34, TMA.

HMRC contended that the taxpayer should have given HMRC notice of receipt of the Termination Payment (under section 7, TMA) and that in failing to do so he was careless or negligent (the statutory language applicable at the time) which enabled HMRC to issue an assessment outside the normal time limits.

The taxpayer contended that he had received the Termination Payment after tax had been deducted by ITV and he was not careless or negligent in relying upon this fact.

FTT's decision
The FTT allowed the taxpayer's appeal.

The FTT undertook a detailed analysis of section 7, TMA, and the Income Tax (Pay as You Earn) Regulations 2003 (the PAYE Regulations).

In respect of section 7, HMRC contended that because ITV had deducted tax at the basic rate only, the taxpayer's income could not have been said to have been taken into account in accordance with the PAYE Regulations.

In the FTT's view, the income was assessable in 2008/09 and ITV had correctly accounted for PAYE in that year in accordance with the PAYE Regulations. Thus, not only was there no additional tax to assess in 2007/08, but the assessment for that year was out of time because the taxpayer was not required to notify any other source of income, under section 7, for that year.

Comment
The FTT acknowledged in its decision that the statutory provisions relating to the taxation of termination payments are complicated. It is to be hoped that the Government's proposed reforms in this area, which are expected to come into effect in April 2018, will help simplify this complex area of the law.

A copy of the decision can be found here.

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