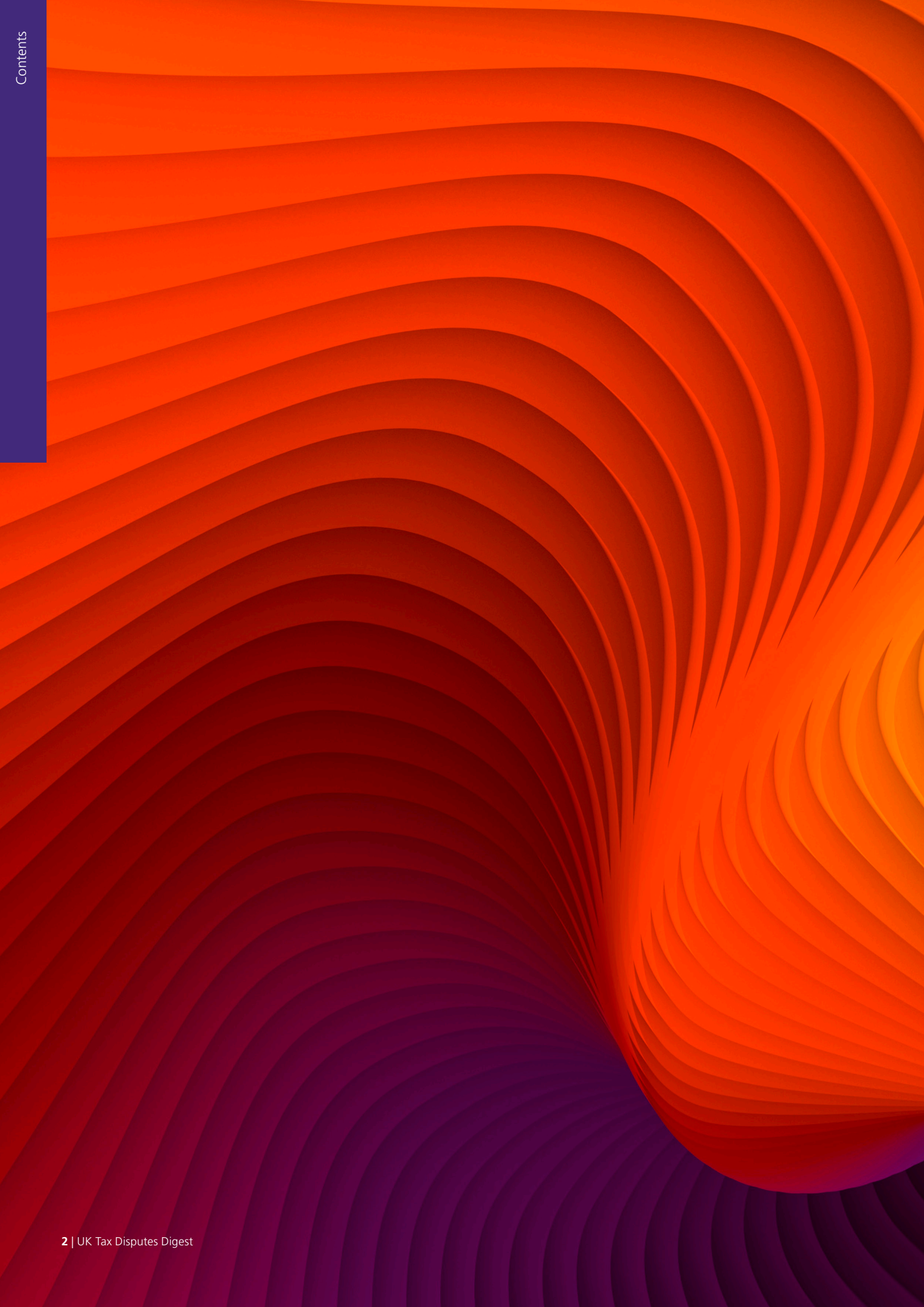
UK Tax Disputes Digest

Summer 2023



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Introduction

Welcome to the Summer 2023 edition of our UK Tax Disputes Digest: a high-level summary of key developments in contentious tax over the last few months for heads of tax, finance directors, general counsel and other in-house professionals.

In previous editions, we have discussed the pressure on HMRC following the end of the pandemic to recover money through closing the tax gap. Over the last quarter, we have seen a continued increase in HMRC investigations across various areas. Both individual and corporate taxpayers would be well-advised to check their tax position as soon as possible to prepare for any potential HMRC investigation into their tax affairs.

In this edition, we look at just a few of the latest developments, including recently published HMRC guidance on the "unallowable purpose" rule, a consultation aimed at curbing tax avoidance by umbrella companies, a new Code of Practice 9, a report by the Public Accounts Committee which adds further pressure on HMRC, and the latest series of HMRC nudge campaigns (including a new campaign aimed at UK residents identified as part of the "Pandora Papers" leak).

We also cover a number of notable tax cases and other interesting procedural decisions, including a recent victory for SSE in the Supreme Court on which the CMS Tax Disputes and Investigations team was instructed.

We are also delighted to have become a contributing author to the Chambers and Partners Tax Controversy 2023 Global Practice Guide, with the first ever UK chapter. Please click here to read the chapter setting out the essential background on tax disputes in the UK, as well as a summary of the latest trends and developments.

About the team

With 15 partners in our London office, the CMS tax team is one of the largest in the City and advises high-profile clients across a wide range of sectors and all areas of tax. As part of that general tax practice (and the CMS global network with tax capability in over 70 offices), our tax team regularly helps both individuals and corporates with all aspects of tax dispute prevention, management and resolution.

The CMS disputes team is one of the UK's leading contentious practices with some 500 disputes lawyers in the UK alone. We regularly appear before all courts and have more sector and practice expertise among our disputes lawyers than any other firm. We are one of only a few firms to routinely appear in The Lawyer's annual reports on leading cases both for first instance and appeal cases.

The firm's contentious tax practice pools the resources of the CMS tax and disputes teams, including dedicated tax disputes specialists.

For more information on our team and the type of work we undertake, please see here.

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In focus: "tunnels" and "aqueducts" – SSE wins Supreme Court case on capital allowances

In *HMRC v SSE Generation Ltd* [2023] UKSC 17, the Supreme Court confirmed that SSE Generation Limited ("**SSE**") was entitled to claim capital allowances in respect of the construction of a hydro-electric power station, bringing to an end a long-running dispute with HMRC. The CMS Tax Disputes and Investigations team was pleased to have advised SSE on this case. Counsel for SSE were Jonathan Peacock KC and Michael Ripley.

Background

Capital expenditure is not generally deductible from income for the purpose of calculating trading profits subject to corporation tax. However, the Capital Allowances Act 2001 ("**CAA 2001**") provides for capital allowances to be claimed in relation to certain categories of expenditure, including on plant and machinery. Subject to specific exclusions set out in Chapter 3, Part 2 CAA 2001, the general rule is that a company will be entitled to claim capital allowances where it has incurred capital expenditure on the provision of plant and machinery for the purposes of a "qualifying activity" (which includes the company's trade).

This particular case concerned the extent to which SSE was entitled to claim capital allowances on expenditure incurred when constructing the hydro-electric power station at Glendoe, Fort Augustus in Scotland (the "**Glendoe Scheme**"). The Glendoe Scheme is a state-of-the-art facility first opened by HM The Queen in 2009 and the only large-scale hydro-electric station of its type built in the UK in the last 50 years. Similar to other hydro-electric power stations, the Glendoe Scheme generates electricity by taking water at high pressure from a dammed area in order to drive a water turbine, which in turn engages a generator (with the used water then discharged into Loch Ness). The unique aspect of the Glendoe Scheme is that many of its assets are underground, thereby optimising water pressure but also minimising the environmental impact.

HMRC disputed a substantial proportion of the allowances claimed by SSE in respect of the Glendoe Scheme on the basis that, in their view, the relevant assets should be disqualified from relief by virtue of Chapter 3, Part 2 CAA 2001. Broadly, those provisions include exclusions from plant and machinery allowances for the following main categories of expenditure:

1. expenditure on the provision of a building, including the items set out in "List A" (section 21 CAA 2001);
2. expenditure on the provision of a structure or other asset within "List B" (section 22(1)(a) CAA 2001); and
3. expenditure on works involving the alteration of land (section 22(1)(b) CAA 2001).

Before the Supreme Court, the critical provision was Item 1 of List B, section 22 (emphasis added):

*A **tunnel**, bridge, viaduct, **aqueduct**, embankment or cutting.*

If, as HMRC argued, the disputed items were a "tunnel" or an "aqueduct" for these purposes, the associated expenditure (approximately £200 million) would be disqualified from capital allowances. To the extent that the disputed items were so disqualified, SSE relied upon the saving provisions in List C, section 23 CAA 2001.

The lower courts

Meaning of "tunnel"

The First-tier Tribunal (Tax Chamber) ("**FTT**") held that SSE was entitled to claim allowances for some of the disputed items, but upheld HMRC's view on others. The FTT considered that the words in List B are not "specialist terms" but instead have "ordinary English meanings". In ascertaining those meanings, the FTT

held that it was "legitimate to consider the way in which they have been grouped in the legislation, the assumption being that structures and assets which are specifically grouped together are likely to share some basic common theme" ([38]). In relation to Item 1 of List B, the FTT concluded that the relevant theme was one of structures related to transportation infrastructure, and that the ordinary meaning of the word "tunnel" in this context was a "passage bored through ground which permits people or forms of transport to pass to and fro". On that basis, the FTT held that none of the disputed items was a "tunnel".

HMRC lodged an appeal before the Upper Tribunal (Tax and Chancery Chamber) ("**UT**") in respect of some of the items which the FTT had found did give rise to capital allowances. The UT dismissed HMRC's appeal, while disagreeing with the FTT's analysis in certain respects and remade the decision largely in SSE's favour. In respect of the meaning of "tunnel", the UT considered that the ordinary meaning was "any form of subterranean passage" ([90]) but that the statutory context requires that the term should be given a narrower meaning than its ordinary dictionary definition.

The Court of Appeal agreed with the FTT on the ordinary meaning of the word "tunnel" and that the context was one involving a transportation theme.

Meaning of "aqueduct"

The FTT noted that the term "aqueduct" has two potentially relevant definitions under the Oxford English Dictionary:

(a) "an artificial channel for the conveyance of water from place to place; a conduit; esp. an elevated structure of masonry used for this purpose"; and
(b) "The similar structure by which a canal is carried over a river, etc." (which has a more obvious transportation association).

The FTT held that, in the statutory context, the former meaning was correct – and that the transportation of water itself was enough to be consistent with the "transportation" theme of Item 1, List B (rather than requiring the water to be the means of transportation of other things, as in the case of a canal).

The UT disagreed, deciding that "aqueduct" should be given its other dictionary meaning, and therefore limited to a bridge or viaduct-like structure which carries a canal (rather than merely conveying water to a destination). On that basis, the UT concluded that none of the disputed items was an "aqueduct" for relevant purposes.

On appeal by HMRC, the Court of Appeal expressed some difficulty in reaching its decision on the basis that the definition adopted by the UT would "exclude many spectacular and elegant structures that have been left to us from ancient times and are commonly thought of and referred to as aqueducts". However, the Court held that the principle of *noscitur a sociis* should apply to limit the ordinary meaning to a particular type of aqueduct with a transportation theme.

Supreme Court's decision

The Supreme Court unanimously dismissed HMRC's appeal, holding that the disputed items were neither a "tunnel" nor an "aqueduct" within the meaning of List B. On that basis, it did not need to consider SSE's cross appeal based on the saving provisions in List C, section 23 CAA 2001.

In relation to "tunnel", the Supreme Court held that the Court of Appeal (and tribunals) had been correct to consider the statutory context. The Supreme Court agreed with SSE that, in the drafting of List B, a choice had been made to group the relevant structures in separate lists and that it was reasonable to conclude that those grouping choices were made for a thematic reason. That theme linking Item 1 of List B was that of structures related to the construction of transportation routes or ways, such that a "tunnel" in this context is a "subterranean passage through an obstacle for a way (such as a railway, road, or canal) to pass through". HMRC's approach, on the other hand, gave no effect to that statutory context and did not offer any explanation for the groupings made in List B.

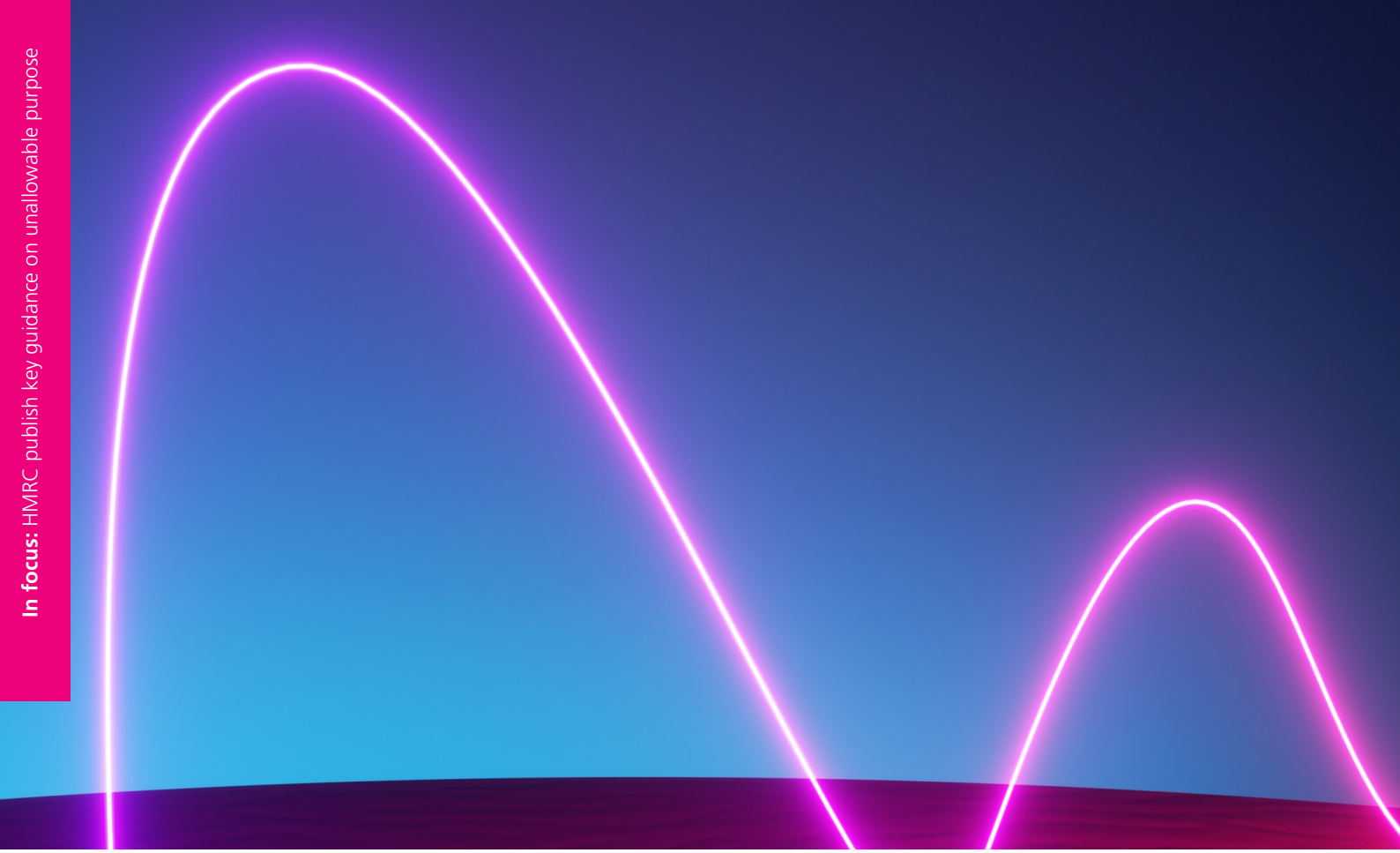
On that same thematic basis, the Supreme Court held that "aqueduct" means a "bridge-like structure for carrying water, which includes but is not limited to carrying a canal". According to the Supreme Court, this was the common ordinary meaning and the general transportation theme did not compel the more limited meaning of a bridge-like structure carrying a canal which was given to it by the UT and Court of Appeal (thereby addressing one of HMRC's arguments, which was that the Court of Appeal's definition was arguably limited to historic structures).

Comment

The Supreme Court's decision reinforces the importance of context when determining the meaning of words used in statute, and is therefore of potential significance for both tax and non-tax cases.

This long-running dispute was essentially brought about as a result of the unique design of the Glendoe Scheme. Had the disputed elements of the Glendoe Scheme been built above ground (i.e., at the expense of engineering ingenuity and environmental concerns), they would have likely qualified for capital allowances on HMRC's case. Aside from the material amounts of tax at stake, therefore, the Supreme Court's decision brings welcome clarity for SSE and other similar businesses when considering the viability of further infrastructure projects to develop renewable power in the UK.

In focus: "tunnels" and "aqueducts" – SSE wins Supreme Court case on capital allowances



In focus: HMRC publish key guidance on unallowable purpose

HMRC's recently published guidance on the "unallowable purpose" rule in section 441 of the Corporation Tax Act 2009 ("**CTA 2009**") gives a key insight into HMRC's latest thinking on this increasingly contentious area of tax law, with particular impact for acquisition financing and intra-group debt reorganisations.

Whilst clarification may be useful in some circumstances, and the guidance is broadly pragmatic in tone as regards some of the more straightforward scenarios, the guidance is silent on some key points, pending the outcome of ongoing litigation.

Background

The effect of section 441 CTA 2009 is that a company must not bring into account so much of a loan relationship debit as is attributable to an "unallowable purpose".

A company has an "unallowable purpose" if, "at times" during a relevant accounting period, the company is a party to a loan relationship (or enters into a "related transaction" by reference to a loan relationship) for purposes which include a purpose which is not amongst the company's "business or other commercial purposes". This would include circumstances where the company is party to a loan relationship with a "tax avoidance" purpose, unless that purpose is not the main purpose or one of the main purposes for which the company is party to a loan relationship (or enters into a related transaction by reference to a loan relationship).

Although the unallowable purpose rule is certainly not new (its predecessor having been enacted in 1996), it is an area of renewed focus. Unallowable purpose has, in recent times, been a key area of activity for HMRC, as evidenced by the volume of recent litigation in this area (in respect of which HMRC have had a significant degree of success).

At the time of writing, the decision of the UT in *JTI Acquisition* is keenly awaited. The Court of Appeal is expected to hear the taxpayers' appeals in the *Blackrock* and *Kwik-Fit* cases in the spring of 2024.

The guidance is therefore perhaps best seen as a snapshot of HMRC's current view, but one which may be quickly superseded by further developments in ongoing litigation.

Status of HMRC guidance

As a practical matter, HMRC's published guidance is useful as a means of establishing their current view in a particular context and therefore the practical likelihood of HMRC challenge. In broad terms, the guidance is likely to be of some reassurance to taxpayers in some of the more uncomplicated scenarios, for example those involving straightforward debt financing of an acquisition of a UK company by a UK acquiror. Further, it provides a broad steer that certain scenarios are likely to be the subject of HMRC challenge, for example the routing of debt relating to a non-UK acquisition through a UK finance company solely to access tax capacity in the UK. Given that the ongoing litigation referenced above has given rise to particular uncertainties, especially as regards acquisition finance, there will be circumstances in which this insight into HMRC's likely approach is useful.

One issue to consider is that a taxpayer may be subject to a disclosure obligation under the Uncertain Tax Treatment rules if it departs from HMRC's known position. It will therefore be important for taxpayers to carefully consider any positions being/to be adopted for potential inconsistencies with HMRC's new guidance in order to determine whether a disclosure obligation may exist.

If a taxpayer finds the guidance to be of comfort that its position is consistent with HMRC's stated view, it is nevertheless worth considering what would happen if HMRC were subsequently to act in a way which the taxpayer believed to be inconsistent with the guidance. In certain circumstances, taxpayers might be able to bring challenges through judicial review on the basis of having a "legitimate expectation".

Overview of "unallowable purpose" guidance

Prior to the publication of the guidance, in light of recent litigation, it had become difficult in certain contexts to establish the extent to which financing arrangements (structured with tax efficiency in mind) would be subject to challenge. It is therefore welcome that the new guidance (i) acknowledges that tax considerations may sway decision-making in circumstances where the non-tax reasons for choosing between debt or equity funding are finely balanced and (ii) accepts that the unallowable purpose rule will not inevitably apply in those circumstances. However, there will be circumstances where it may apply and HMRC give examples of various different scenarios, which are considered further below.

Another welcome aspect of the guidance is that it sets out HMRC's views on some key themes arising from the ongoing litigation. For example, the guidance discusses the relevance of a wider "group purpose", concluding that it is likely, as a matter of fact, that the directors of a company will take into account their knowledge of the group's purposes in their decision making.

The guidance also includes HMRC's view on the possibility of a company's purpose in being party to a loan relationship changing over time, for example where an unallowable purpose arises at some point after the company enters into the loan relationship, however fleetingly.

A key area which HMRC do not seek to resolve in the guidance pending the outcome of the ongoing litigation, is the method by which debits should be regarded as attributable on a just and reasonable apportionment to the unallowable purpose, in circumstances where there is both an allowable purpose and an unallowable purpose. This therefore remains a key area of uncertainty and likely contention.

HMRC's guidance also sets out the factors that will be examined in order to assess the full factual context and therefore determine the taxpayer's purpose - these require careful reading, particularly in the context of cross-border financing arrangements.

HMRC's examples

The guidance first gives some examples of scenarios in which HMRC accept that there is no disallowance, either because it is accepted that there is no unallowable purpose or that no debits should be attributable to the unallowable purpose. These examples include finely-balanced decisions as between debt or equity funding of business investments "straightforwardly linked to the UK", where the potential availability of a UK tax deduction for interest is a deciding factor in choosing to finance the acquisition by debt.

In perhaps the most revealing aspect of the guidance, HMRC go on to give some examples of situations in which they will normally start with the view that the unallowable purpose rule will apply and that debits will be attributable to one or more unallowable purpose:

— where external debt is being routed through a UK finance company, because there is tax capacity in the UK (but not in the other relevant jurisdictions), being acquisition finance for a non-UK subsidiary to buy shares in a non-UK company;

— where intra-group debt is created in the UK (where there is tax capacity) in circumstances where the corresponding interest receivable will not be taxable in the hands of the non-UK parent and where the debt funds an intra-group acquisition of shares which has no real commercial justification;

— where new intra-group loans (with no real commercial justification) are created in order to access trapped losses;

— where a UK entity borrows to pay a dividend to its parent, resident in a low-tax jurisdiction. Parent then lends the funds to a non-UK subsidiary, which uses the funds to make an acquisition. The aim of the structure is to give rise to two deductions within the group, as opposed to only one deduction if the non-UK subsidiary simply took out external finance for the acquisition; and

— other more specific examples (i.e., borrowing for the purposes of mutual trading, borrowing and lending for the personal purposes of a director, and lending to a company solely because of a family connection).

Residual uncertainty

HMRC's guidance indicates that no further clarification will be given in response to particular taxpayer enquiries. HMRC's apparent refusal to give confirmation as regards specific facts and transactions, combined with the residual uncertainties arising from HMRC's guidance and from ongoing litigation – in particular as regards the method by which debits should be attributed as between allowable and unallowable purposes, respectively – means that significant uncertainties remain.

Conclusion

Whilst HMRC's guidance provides some useful clarification and a generally systematic insight into HMRC's view on some particular themes arising from the ongoing litigation, it is clear that this remains a key area of HMRC activity. Further disputes in this area are highly likely.

Taxpayers should consider their tax positions carefully in light of this new guidance, including in circumstances where there may be a disclosure obligation under the Uncertain Tax Treatment rules.

In focus: why tax should be part of your ESG strategy

With a growing public perception of tax avoidance as a moral issue, tax disputes have the potential to cause significant reputational harm. At the same time, tax is also expected to be a key tool in helping to drive sustainable behaviours and the transition to net zero. In light of recent global tax initiatives and with taxpayers facing unprecedented levels of scrutiny, it has never been more important for all businesses to make tax a fundamental part of their broader ESG strategy.

Environmental considerations and tax

Potential tax implications should be front of mind when considering a business's environmental impact. For example, a business which seeks to lower its carbon footprint by localising supply chains may find that this has consequences not only for its indirect tax liabilities (e.g., import taxes) but also for its existing functional analysis under transfer pricing rules (amongst other potential tax issues).

Businesses should also be aware of the potential impact of legislative changes which may be implemented to help drive environmental behaviours. In the short to medium term, this might include taking advantage of tax reliefs or exemptions made available for "green" or sustainable behaviour.

In the longer term, the transition to net zero is expected to have significant fiscal implications. As the economies of the UK and other jurisdictions decarbonise, traditional tax revenues from fossil fuel-related activities will inevitably decline. Businesses may, therefore, want to plan for the jurisdictions in which they operate moving towards a "polluter pays" model focused on alternative sources of revenue derived from carbon emissions, water usage, plastic creation/usage and otherwise. For example, the UK's Plastic Packaging Tax, in force from 1 April 2022, applies to plastic packaging manufactured in, or imported into, the UK that does not contain at least 30% recycled plastic. Even those not strictly liable to pay the tax may find that they are paying higher prices as costs are passed through to consumers. Affected businesses may see prices rise despite an exemption for certain medicinal products which is limited to "immediate" packaging and, in any case, the packaging would still count towards a manufacturer or importer's 10-tonne registration threshold. Businesses will need to be alert to these types of development, both current and future, in each jurisdiction in which they operate and adapt accordingly.

Social considerations and tax

Tax avoidance is increasingly viewed as not just as an economic issue, but as a moral one too with tax becoming a fundamental part of the ESG agenda. In light of current economic circumstances, businesses need to be more vigilant than ever to any tax issue that might cause unwelcome publicity or significant reputational damage.

For example, certain multinational groups may derive a large part of their value from intellectual property ("**IP**"), often with IP rights held in one jurisdiction but licensed or developed elsewhere, which has led to the creation of IP "hubs" (i.e., the concentration of profits from the exploitation of IP in low tax jurisdictions). International developments and domestic legislation (such as the UK's Diverted Profits Tax) are already targeting these types of structures that erode the tax base of those jurisdictions in which the relevant work on research and development is taking place. Multinational groups that hold valuable IP portfolios should review their current tax planning arrangements to assess not just the risk of challenge by tax authorities but also the potential perception by stakeholders and the public.

Governance and tax

The global tax landscape has radically changed in recent years. In the face of public pressure to crack down on perceived tax avoidance, in particular by multinationals, tax authorities are becoming increasingly proactive. Moreover, international initiatives have seen unprecedented levels of transparency and cooperation between tax authorities.

For example, country-by-country reporting was designed as part of the OECD Base Erosion and Profit Shifting (BEPS) project to provide tax authorities with an overall picture of the global profit and tax position of multinational groups operating in their jurisdictions. Notwithstanding these developments, there are increasingly calls for information on country-by-country reporting to be made more publicly available. In 2019, the Global Reporting Initiative issued the first global standard for public country-by-country reporting and the EU has also approved a new directive requiring member states to introduce legislation by June 2023 for public country-by-country reporting for certain large companies.

As a result of social attitudes to tax (and particularly in light of greater transparency), businesses will, of course, need to ensure that they are compliant with the tax rules of any jurisdiction in which they operate, reviewing tax policies and responsibilities where appropriate. There is the potential for all businesses to embrace the developments towards greater tax transparency and accountability in order to showcase their ESG credentials, reassuring investors that a sustainable and responsible approach is being taken in relation to the tax affairs of the business.

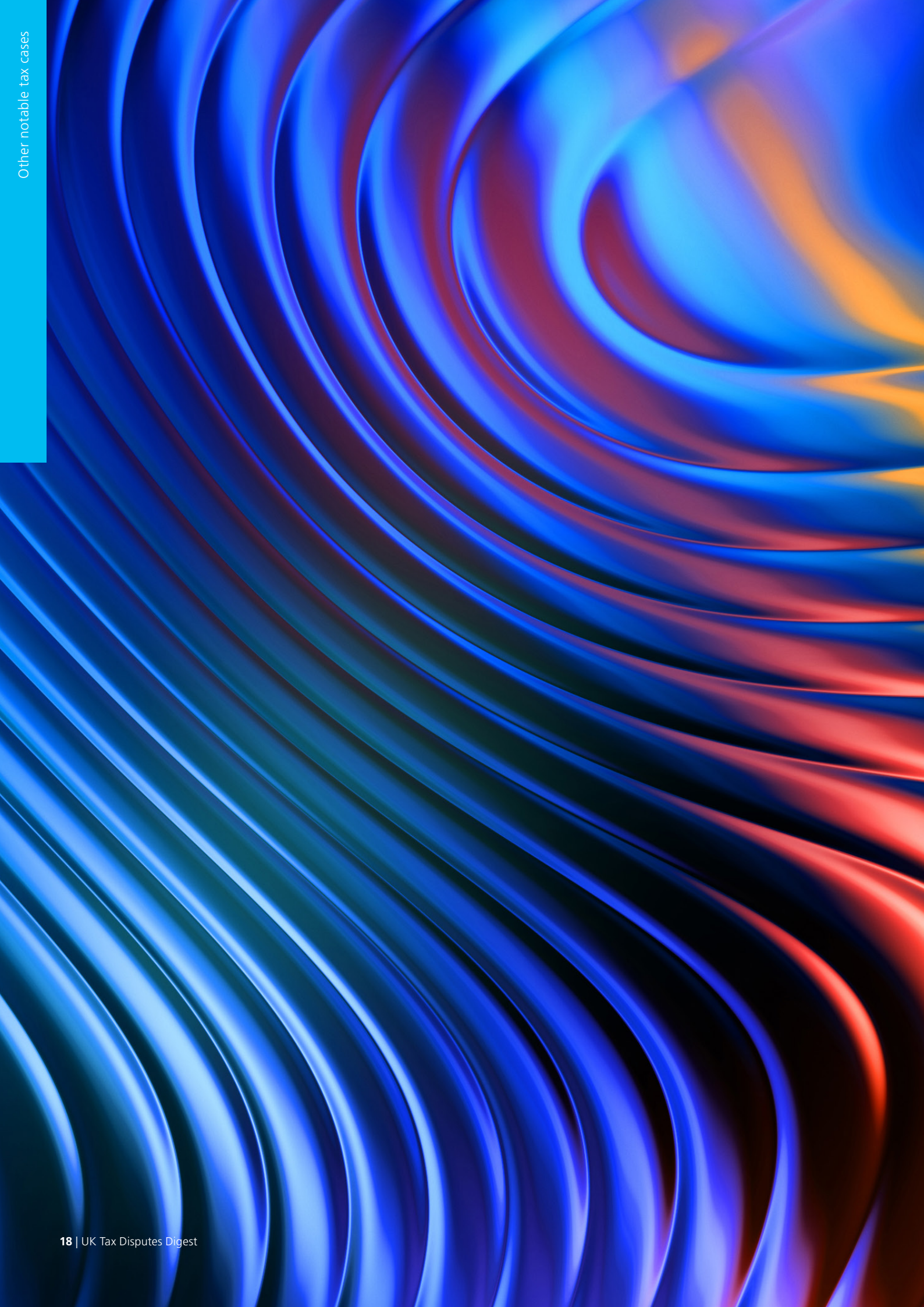
Action points

— Ensure that all potential tax consequences are considered before implementing any decisions in relation to the broader ESG strategy.

— Monitor potential environmental policy and legislative changes that may impact the use of any environmental reliefs or affect business models more broadly to ensure that these are factored into ESG strategy.

— Review existing tax structures, policies and responsibilities to ensure that the risk profile for tax is aligned to the broader ESG strategy and that tax compliance is made a priority. Complex or potentially aggressive structures should be assessed not just for the potential risk of challenge by tax authorities but also the potential perception by stakeholders.

— Consider greater levels of tax transparency and reporting to communicate ESG credentials to stakeholders.



Other notable tax cases

Mark Mitchell & Paul Bell v HMRC [2023] EWCA Civ 261

This Court of Appeal decision dealt with the disclosure of confidential documents, in particular where the interests of the co-appellants interests were "not aligned". HMRC opened an investigation under Code of Practice 9 into the tax affairs of Mr Mitchell and his companies, as a result of which the companies were assessed for VAT and issued deliberate penalties. The companies subsequently went into liquidation, and HMRC issued personal liability notices against Mr Mitchell and Mr Bell on the basis that they were shadow directors. Each individual was of the view that the other ran the companies. The issue before the Court was whether HMRC could disclose to Mr Bell certain documents obtained in the course of the Code of Practice 9 investigation into Mr Mitchell. The Court of Appeal concluded that HMRC did have the power to disclose those documents, pointing to exceptions to HMRC's taxpayer confidentiality obligations contained in the Commissions for Revenue and Customs Act 2005 ("**CRCA**"). In an interesting comment on the increasingly relevant issue of the jurisdiction of the tax tribunals to hear public law arguments, the Court of Appeal stated that, while the FTT does have jurisdiction to determine issues of case management under the FTT rules, any challenge to the exercise of HMRC's powers under the CRCA must be by way of judicial review.

Moulsdale t/a Moulsdale Properties v HMRC [2023] UKSC 12

This Supreme Court decision was concerned with the complexity and circularity of the disapplication of the option to tax rules. The taxpayer sold a property to an unconnected third party, subject to a continuing lease. Despite the fact that the property had been opted to tax, the taxpayer did not charge VAT on the sale, relying on the anti-avoidance provisions in schedule 10 to the Value Added Tax Act 1994 ("**VATA**").

In the simplest terms, whether the option was disapplied turned on whether or not the individual (as seller) was "a developer of the land" for the purposes of paragraph 12(1)(a) of schedule 10 VATA; whether or not he was a "developer" depended, under the legislation, on whether he intended or expected the purchaser to incur VAT on the property. This led to a "conundrum" that, if he did charge VAT on the price of the property, he would have been a "developer", and if he did not, then he was not and did not have to charge VAT. The Supreme Court preferred HMRC's construction of the relevant disapplication provisions, deciding that the provisions must be interpreted with reference to the grantor's (here, the seller's) intention or expectation regarding incurring VAT on some other cost, different from the payment for the property itself (i.e., different from the transaction to which the disapplication provisions applied). To interpret the legislation otherwise would have defeated the purpose of the provisions, which is to ensure that exempt businesses cannot recover input tax.

R (Airline Placement Limited) v HMRC [2023] EWHC 1191 (Admin)

This High Court decision follows a long line of judicial review cases dealing with whether a taxpayer has a "legitimate expectation" that HMRC will act consistently with a statement they have made in a non-statutory clearance. Two key principles were re-affirmed in this case. First, HMRC accepted that statements made in a non-statutory clearance can give rise to a "legitimate expectation", such that taxpayers can rely on those clearances. Second, and of as much importance to taxpayers, is that such "legitimate expectation" will not arise where a non-statutory clearance has been sought on a basis which is materially inaccurate and misleading, and which lacks "full and frank disclosure". This is a reminder to taxpayers of their responsibilities in the process of seeking a clearance, if they want HMRC to effectively be bound by their response.

Hugh Murphy & Anor. v HMRC [2023] EWCA Civ 497

This Court of Appeal decision dealt with another judicial review case concerning statements made by HMRC, this time in the form of an extra-statutory concession ("**ESC**"). The substantive issue was whether a concessionary treatment that was provided by ESC B18 was subject to a certain limitation (HMRC argued that it was – and the applicant successfully argued that it was not). Of more general application to most taxpayers are the comments made in the decision on the interpretation of ESCs. The judgment is a reminder that the meaning of an ESC is to be assessed by reference to how it would "reasonably have been understood by an ordinarily sophisticated taxpayer". In reaching such meaning, the judge looked in detail at the language, history and even the layout of the ESC in question (including with reference to paragraph breaks). Ultimately, and of significance to taxpayers and advisers interpreting ESCs, the judge found that, in this case, it was not right to have regard to the previous iterations of the ESC, determining that an "ordinarily sophisticated taxpayer" would not expect to have to research the

historical versions, nor were they readily accessible online. Additionally, whether or not a settled practice of HMRC has an effect of the interpretation of an ESC is decided by whether an ordinarily sophisticated taxpayer could have been alerted to that practice, for example by published guidance or practitioner commentary.

Altrad Services Limited & Anor. v HMRC [2023] EWCA Civ 474

In this case, the issue before the Court of Appeal was whether HMRC were raising a new ground of appeal that they had not placed before the FTT or the UT and, if so, whether they should allow HMRC to now argue that new ground. Having determined that HMRC were indeed raising a new argument, the Court had to determine whether granting permission would be materially prejudicial to the taxpayers, either because the taxpayers would want to rely on factual evidence to deal with the point (which could not now be placed before an appellate court) or because the hearing would have been conducted differently if the point had been raised before the FTT. The Court of Appeal held that the taxpayers would not be so prejudiced, and that the prejudice of not having been able to call witnesses to give evidence in their favour on the new ground would be mitigated by the courts assuming that that the evidence fell in the taxpayers' favour. The Court of Appeal also found for HMRC in relation to the requirement that the point was "one of pure law" (as opposed to fact).

Deepak Bhatia v Christopher Purkiss [2023] EWHC 775 (Ch)

This is an insolvency case with a tax angle. The specific decisions before the High Court were whether the appellant's level of knowledge of the involvement of a company (of which he was an erstwhile director) in missing trader VAT fraud amounted to a fraudulent breach of his duty under section 212 of the Insolvency Act 1986 and to fraudulent trading under section 213 of that Act. If so, the director would be liable to contribute to the company's assets. The decision is of particular interest for its discussion of what is meant by "actual knowledge". In particular, the judge emphasised that the director need only be aware of the fraud to be liable – there was no requirement that they know every detail, and that knowledge included "blind eye knowledge" (i.e., deliberately shutting one's eyes because of a conscious fear that enquiring will confirm suspicion of wrongdoing). The judge found the appellant did therefore have actual knowledge of the fraud, and so dismissed the appeal.

Stephane Etroy & Anor. v Speechly Bircham LLP [2023] EWHC 386 (Ch)

This High Court case concerned whether a claim in respect of negligent tax advice brought against a firm of private client solicitors was time-barred. The starting point is that, under section 2 of the Limitation Act 1980 ("**LA 1980**"), a negligence claim must be brought within six years from the date on which the cause of action accrued. However, if that limit has passed, a claim may be brought within the period of three years from the date on which the claimant had the knowledge required for bringing an action for damages in relation to that claim (section 14 LA 1980). In that context "knowledge required" means both "the material facts about the damage in respect of which damages are claimed" and "the other facts relevant to the current action" (including that the damage was attributable to the negligent behaviour). Here, the judge accepted the claimant's argument that they obtained the "knowledge required" at a later date than their former solicitors alleged, and so were not time-barred in bringing the claim.

Of particular significance for taxpayers and their advisers is the judge's comments that negligence cases which call for "specialised technical expertise" (as here) are ones where "the claimant may know a basic fact, but not know what to an expert, they add up to". To set time running, the claimant must know the "essence of the act of omission to which his damage is attributable" – and therefore, "until the client is aware of the damage, it is unlikely he will have knowledge of attributability". For tax advice negligence cases, it can be a considerable period of time until a taxpayer is aware of the damage, given HMRC's time limits for making a discovery assessment – or, as here, the time period which might elapse before hiring tax advisers to look into a structure again many years later.

McClean v Thornhill [2023] EWCA Civ 466

The Court of Appeal considered whether a senior tax barrister, who had advised the promoters of a film finance tax scheme, owed a duty of care to the individual investors in the scheme and, if so, whether that duty had been breached. The Court applied the two stage test set out in *Steel v NRAM Ltd* [2018] UKSC 13 in determining whether a duty of care had arisen. The barrister was aware that his advice would form part of an information memorandum shared with potential investors, and that his opinions would be made available to investors on request. However, the Court held that the fact that this was in the context of an unregulated scheme which required investors to take independent advice by law absolved him of a duty of care. It was not reasonable for the investors to rely on the barrister's advice in this context, nor was it reasonably foreseeable that they would.

However, the Court of Appeal departed from the previous conclusion in the Upper Tribunal in finding that, had there been a duty of care, it would have been breached. The Court considered that, although the conclusion reached by Thornhill (based on *Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes)* [1992] 1.A.C. 655) was reasonable, the unequivocal nature of the advice, which was without any qualification or risk warning whatsoever, caused it to fall below the standard of that required by a reasonably competent tax silk.

Volkerrail Plant Limited & Ors. v HMRC [2023] EWCA Civ 210

The case is focused on the compatibility of the UK rules on group relief (in particular, section 403D(1)(c) of the Income and Corporation Taxes Act 1988, "**ICTA 1988**") with the principle of freedom of establishment under EU law (Articles 49 and 54 of the Treaty on the Functioning of the European Union) and, if not, whether the UK provision can be read with a conforming interpretation or must be disapplied. The Court of Appeal held that a UK branch of a Dutch group company could not surrender its losses to UK group companies. The Court of Appeal analysed: (i) whether section 403D(1)(c) ICTA1988 created a restriction in objectively comparable situations, comparing the position of a non-resident company with a permanent establishment in the UK with that of a UK resident company; (ii) whether such restriction is justifiable by reference to prevention of double deduction of losses; and (iii) whether any restriction is proportionate. The Court of Appeal concluded that the restriction on freedom of establishment was justified and not disproportionate. On that basis, there was no need for the Court to adopt a conforming interpretation. There was also no need for the Court to consider HMRC's alternative argument that it should exercise its powers under section 6 of the EU (Withdrawal) Act 2018 (and the accompanying regulations) to depart from EU law.

Oisin Fanning v HMRC [2023] EWCA Civ 263

This Court of Appeal decision on Stamp Duty Land Tax ("**SDLT**") raises issues of wider relevance, with 41 appeals standing behind it. The taxpayer had purchased a property worth £5,200,000 and granted an option to an Irish-incorporated company to purchase the property. The consideration for the grant of the option was £100 and the consideration payable on the exercise of the option was the market value of the property at that time. The SDLT return was filed on the basis of the application of sub-sale relief, pursuant to section 45 of the Finance Act 2003 ("**FA 2003**") (as in force at the relevant time), on which basis the taxpayer concluded that his SDLT liability was nil. HMRC disagreed and raised a discovery assessment. The Court considered the purpose and context of the relevant legislation and reached the conclusion that Parliament's aim could not have been to permit SDLT avoidance by the simple mechanic of the grant of an option where it is the grantor of the option who ends up with the enjoyment of the land. Therefore, the Court of Appeal decided that the grant of an option does not fall within the statutory definition of "other transaction" under section 45(1)(b) FA 2003.

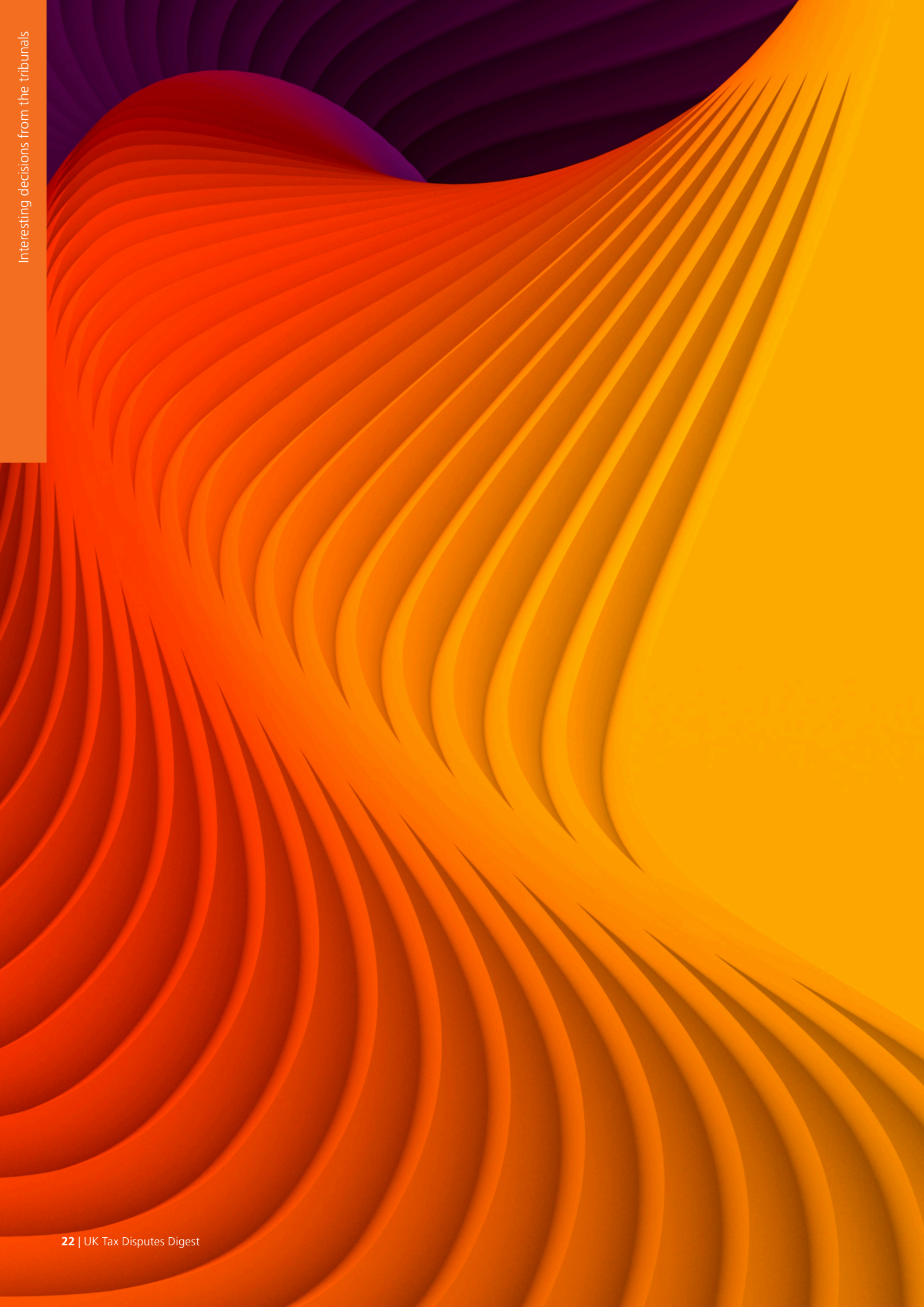
London Luton Hotel BPRA Property Fund LLP v HMRC [2023] EWCA Civ 362

This is the first case on business premises renovation allowances ("**BPRA**"), a form of capital allowance, and specifically their availability on the conversion of a former flight training centre into a hotel. The Court of Appeal first addressed the extent to which costs could be treated as qualifying expenditure on, or in connection with, the conversion works. The Court held that the expenditure must have a strong and close nexus with the physical work on the building to qualify for BPRA, and held that the relationship was too remote on the facts of this case.

Kieran Corrigan & Co Ltd v OneE Group Limited & Ors. [2023] EWHC 649 (Ch)

The claimant in this case was an Irish company specialising in accountancy and tax advisory services. The first defendant was a company involved in developing and marketing tax efficient investment products, and the second to fourth defendants were directors or employees of the first defendant or its subsidiaries. The claimant, alongside senior tax counsel, developed a tax efficient structure involving the use of limited liability partnerships, aimed at permitting small and medium sized enterprises to access enhanced subcontractor research and development tax relief. The claimant approached the first defendant with a view to marketing the structure and the parties entered into a non-disclosure agreement. Confidential information in relation to the structure was shared by the claimant with the first defendant. Subsequently the first defendant began to market a similar scheme, which incorporated elements of the claimant's proposed structure. The claimant issued proceedings for: (i) breach of confidence; (ii) procuring breach of contract (the non-disclosure agreement); and (iii) unlawful means conspiracy.

The Court held the first, third and fourth defendants liable for breach of confidence on the basis that they misused confidential information about the structure noting that creating complex tax-planning products requires time, effort and significant skill, so that such products are more likely to hold the necessary quality of confidence than publicly available information. The first, third and fourth defendants were also held liable for unlawful means conspiracy finding that the requisite "intention to injure" was the use of the claimant's ideas without recompense to market fee-generating products. The claim for procuring a breach of contract was time-barred.



Interesting decisions from the tribunals

Appellants score "knockout points" on IR35

In *Gary Lineker and Danielle Bux t/a Gary Lineker Media v HMRC* [2023] UKFTT 00340 (TC), the FTT held that the IR35 regime did not apply to a presenter's services to broadcasters because such services were provided via an intermediary partnership under contracts executed by the individual.

Background

The appellant in this case was Gary Lineker Media ("**GLM**"), a general partnership between well-known presenter Gary Lineker and his ex-wife, Danielle Bux. Between February 2013 and June 2015, GLM entered into three contracts with various broadcasters for the provision of Gary Lineker's services as a television presenter and commentator. In each case, Mr Lineker signed the contract in his capacity as a partner in GLM. The appeal concerned whether the intermediaries legislation (commonly known as "IR35") applied to income received by GLM for the provision of such services in the tax years 2013/14 to 2017/18 (inclusive). If the IR35 regime applied, as HMRC submitted, GLM would face liabilities to income tax and National Insurance Contributions ("**NICs**").

The IR35 legislation in relation to income tax is set out in section 49 of the Income Tax (Earnings and Pensions) Act 2003 ("**ITEPA**"), which provides as follows (so far as relevant):

49 Engagements to which this Chapter applies

(1) This Chapter applies where —

(a) an individual ("the worker") personally performs, or is under an obligation to perform, services for another person ("the client"),

(aa) the client is not a public authority,
(b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and
(c) the circumstances are such that –
(i) if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client or the holder of an office under the client, or […]

(4) The circumstances referred to in subsection (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided.

The equivalent provisions for NICs are set out in regulation 6 of the Social Security Contributions (Intermediaries) Regulations 2000. The wording of the two sets of provisions is materially the same for relevant purposes and we therefore refer only to the income tax provisions below for ease of reference.

Most IR35 appeals are primarily focused on whether the worker in question "would be regarded…as an employee of the client or the holder of an office under the client" (per section 49(1)(c) ITEPA). In this appeal, however, counsel for GLM submitted two novel grounds of appeal around section 49(1)(b) ITEPA:

— that the condition imposed by section 49(1)(b) ITEPA for the application of the intermediaries legislation was not satisfied because there was no "intermediary" either as a matter of general law or on the particular facts of the case; and

— that the condition imposed by section 49(1)(b) ITEPA for the application of the intermediaries legislation was not satisfied because the relevant services were provided under a direct contract with each relevant client.

These grounds were heard by the FTT as preliminary issues on the basis that both raised a "knockout point" to HMRC's case.

Decision

Counsel for the appellants argued that, as a general partnership (governed by the Partnership Act 1890) with no separate legal identity, GLM was not capable of being an "intermediary" for the purposes of section 49(1)(b) ITEPA. The FTT rejected this argument and confirmed that the IR35 legislation does apply to general partnerships. The FTT also determined on the facts that GLM was a partnership.

GLM's primary argument was that the condition in section 49(1)(b) ITEPA was not satisfied in this case because there were direct contracts between Mr Lineker and the broadcasters. The FTT, quoting the decision in *Memec Plc v IRC* [1998] STC 754, held that section 5 of the Partnership Act 1890 provides that each partner of the partnership acts as "both as principal… and as agent, binding the firm and his partners in all matters under his authority". The effect of this was that, as Mr Lineker had executed all the relevant contracts himself, he acted as principal in those circumstances and therefore his services were provided under direct contracts between Mr Lineker and the broadcasters. On that basis, the FTT held that the condition in section 49(1)(b) ITEPA was not satisfied and disposed of the appeal in favour of the appellants.

Comment

This is the first time that the issue of whether there was a direct contract for the purposes of IR35 has come before the FTT. One of the reasons for this is that, in previous IR35 cases, the "intermediary" in question has been a limited company (with its own legal identity and limited liability) instead of a general partnership (with no legal identity and unlimited liability).

Anticipating that the conclusion regarding the existence of a "direct contract" might appear inconsistent with its decision that the IR35 legislation can apply to partnerships (and that GLM was a partnership), the FTT noted that this was the effect of the facts in this case (and that the decision may have been different had the relevant contracts been executed only by Ms Bux on behalf of GLM). At the time of writing, it has been reported that HMRC have lodged an appeal and therefore caution should be applied before trying to rely on the FTT's decision.

VAT place of supply rules for football agent services

In *Sports Invest UK Limited v HMRC* [2023] UKFTT 00376 (TC), the FTT considered the VAT place of supply rules to determine the VAT treatment of a payment made to a football agent.

Background

The taxpayer in this case represented footballer Joao Mario (the "**Player**") for his transfer to Football Club Internazionale Milano ("**Inter**") in August 2016. The taxpayer received €4 million for the transfer, which was paid by Inter. No consideration was given by the Player.

The appeal before the FTT essentially boiled down to a simple question: "who supplied what to whom?". HMRC argued that the taxpayer supplied services to both Inter and the Player. If services were held to be supplied to the Player, this would constitute a B2C supply and the relevant place of supply would be the UK (where the taxpayer is established). On that basis, UK VAT would be chargeable on the part of the €4 million payment treated as consideration for that supply of services. On the contrary, if those services were supplied only to Inter, this would be a B2B supply and the relevant place of supply would be that of Inter (with no UK VAT payable as a result).

Decision

Consistent with the approach taken in previous case law, the FTT's approach was evidence-led and focused on the contractual arrangements between the relevant parties. At the same time, the FTT was cognisant of the economic and commercial realities in categorising a transaction as taxable (see *HMRC v Newey* [2018] EWCA Civ 791). The arrangements in connection with the transfer of the Player are summarised as follows:

1. On 1 August 2016, the Player entered into an exclusive player representation agreement ("**Player Representation Agreement**") with the taxpayer. Under this agreement, the taxpayer was given exclusivity to represent the Player in negotiations for club transfers. In exchange, 10% of the Player's income was payable to the taxpayer and the taxpayer was to use "reasonable endeavours" to ensure that the transferee club would take on responsibility for paying this commission.
2. On the same date and in conjunction with the Player Representation Agreement, the Player and the taxpayer entered into a waiver letter to waive the Player's payment obligations under the Player Representation Agreement ("**Waiver Letter**"). The Waiver Letter confirms that any commission payable to the taxpayer for the transfer will be supported by the transferee club.
3. On 25 August 2016, the taxpayer and Inter entered into a contract which provided a €4 million commission payable by Inter to the taxpayer contingent upon the Player entering into a sports labour contract ("**Inter Agreement**").

HMRC argued that €3 million should be subject to UK VAT on an apportionment of the €4 million paid to the taxpayer by Inter (calculated as 10% of the €30 million payable to the Player under the Player Representation Agreement). The €3 million represented payment for the bulk of negotiations undertaken by the taxpayer in regards the player transfer. As those negotiations were concluded prior to 25 August 2016 and Inter was not a party to the Player Representation Agreement, HMRC argued that supplies of those services could not be made to Inter. Moreover, the Waiver Letter waived the taxpayer's right to enforce payment against the Player but not the actual payment itself – the payment obligation was merely met by a third party, namely Inter.

On the other hand, the taxpayer argued the Inter Agreement reflected the fact that the €4 million paid by Inter was for the supply of services to Inter. Waiver of the commission fee merely represented competitive market practice to ensure exclusivity with the Player. Moreover, regulations governing player representation contracts required the taxpayer as agent to notify the relevant football authorities and seek consent if template terms of the contract were amended. The Waiver Letter was therefore a practical solution to skirt around that requirement and was implicitly sanctioned by the relevant football authorities.

The FTT considered the competing economic and commercial narratives provided by the parties and found in favour of the taxpayer. There was no allegation by HMRC that the arrangements were a sham. Nor was there any evidence from the contracts that the payment was made for anything other than services supplied to Inter. The Waiver Letter was an acceptable means for the taxpayer to flex its "financial muscle" in order to obtain a competitive advantage in the market.

Comment

Professional football has long been an area of interest for HMRC and recent reports indicate that there is now an unprecedented level of scrutiny over the industry's tax arrangements. As noted in our November 2022 edition, there are two current areas of focus for HMRC: firstly, so called "dual representation", where the agent represents both the club and the player; and secondly, the tax treatment of image rights of players. Any clubs, players or agents who receive a notice of enquiry or other correspondence from HMRC should seek professional advice as soon as possible. The CMS Tax Disputes and Investigations team is currently advising clients on football-related investigations.

Remuneration trust documentation held to be a sham

In *Mark Northwood v HMRC* [2023] UKFTT 351 (TC), a sole trader was found to have entered into artificial documentation setting up a purported trust structure, in an attempt to manufacture deductible expenses of his trade.

Background

Mark Northwood ("**MN**"), a dentist who ran his business as a sole trader, appealed against HMRC closure notices for the tax years ended 2010-2013, which had denied him deductions with respect to certain contributions he made into a so-called "remuneration trust" (the "**Trust**"). The key issues were: (a) whether the deductions were allowable under the relevant law; and (b) even if they were so allowable, whether the deductions should be disallowed on the basis that the documentation constituted a sham by which MN intended to make things appear other than they were.

The Trust had been established in 2009 by MN, originally with an independent trustee, supposedly as a means for MN to meet commercial obligations to his suppliers without creating legal obligations. Under the terms of the Trust, the beneficiaries were stated to be "Providers", being anyone who had provided services or finance to MN. MN would provide a list of the Providers to the trustee, and the Providers could then make representations to the trustee explaining why they should be entitled to distributions from the Trust.

Subsequently, the trustee delegated its powers to a company incorporated in Belize, which then entered into a fiduciary services agreement with a UK company ("**MML**") of which MN and his wife were the directors and shareholders. The management of the Trust assets was then transferred to MML at MN's request.

Over the four subsequent accounting years, MN made a number of contributions into the Trust, totalling some £2 million over the four tax years to 2014, which were claimed as deductions on MN's tax return. In the same period, some £1 million of loans were made to MN.

The FTT made certain findings of fact prior to setting out its decision. In particular, the FTT held that, although MN had not acted dishonestly, certain key parts of his witness evidence were not credible. The FTT did not agree that the Trust had been set up to meet commercial obligations to MN's suppliers. Instead, a 2014 slide deck shared as part of a mortgage application revealed the true purpose: i.e., the Trust provided "tax free wealth and personal control". The FTT therefore held that the payments had been made to the Trust with the purpose of obtaining tax advantages, and the documentation did not accurately reflect the arrangements.

Decision

Issue (a): Were deductions allowable under relevant law?

With respect to the first issue, the key legislation was at sections 25(1) and 34(1) of the Income Tax (Trading and Other Income) Act 2005, which together establish that profits of a trade should be calculated in accordance with generally accepted accounting practice, subject to adjustment required by law. Deductions are denied for expenses not incurred wholly and exclusively for the purposes of a trade.

It was clear, on the basis of the expert accounting evidence as well as the FTT's findings of fact with regards to MN's witness evidence, that the contributions should not have been recognised as an expense in the accounts under UK GAAP, and that the contributions and associated fees were not wholly and exclusively for the purposes of the trade. The FTT therefore dismissed MN's appeal on this point.

Issue (b): Sham pleading

As a preliminary matter, the FTT considered whether HMRC should be permitted to raise a pleading of sham at all, on the basis that they had not included the pleading in their original Statement of Case in June 2020 and only raised the pleading later in their January 2022 Skeleton Arguments. Based on previous case law, it was clear that HMRC would be able to raise a case of dishonesty or sham in light of evidence that emerged during cross-examination, provided that: (i) counsel had clear instructions from HMRC to put questions to the witness suggesting fraud or dishonesty; and (ii) the allegation was put fairly and squarely to the witness, with supporting evidence, and the witness was given a fair opportunity to respond. This had been satisfied in this case, and the pleading was allowed.

The FTT held that a pleading of sham did not require HMRC to prove dishonesty. Instead, there would need to be a "common intention to make things appear other than as they are". This did not go so far as to require evidence of tax evasion, because "there was no attempt, as there would be in the case of evasion, to conceal what actually happened, however the parties chose to dress it up."

In this case, the allegation of sham had been put fairly and squarely to MN, and he had been given an opportunity to rebut it. Although there had not been dishonesty, there had been pretence, and it was clear that the Trust documentation had been dressed up to achieve a tax benefit. On that basis, the judge found in favour of HMRC.

Comment

Although the case does not add significantly to our understanding of the general law establishing when deductions will be allowable, it is particularly interesting for the fact that, unusually, HMRC decided to make an additional pleading of sham.

It is clear from the decision that, where the burden of proof in the case as a whole sits with the taxpayer, HMRC will be able to raise a pleading of sham at a later stage in proceedings, in light of evidence given in cross-examination.

Nonetheless, this case does not expand the scope of the sham doctrine, or suggest that it is likely to be relevant except to the most egregious tax structuring arrangements. This is an extreme case, in which the economic and commercial reality was entirely divorced from the way the Trust was described in the relevant documentation. It will be interesting to see whether HMRC will begin to raise sham as last resort in contexts where their arguments on the primary case are less secure, but in this particular case the doctrine remains fairly limited to the specific facts.

Enquiry into "voluntary" SDLT return held to be valid

In *Redmount Trust Company Ltd v HMRC* [2023] UKUT 68 (TCC), the UT upheld the FTT's decision on HMRC's power to open an enquiry into a "voluntary" SDLT return, confirming that HMRC may open an enquiry into an SDLT return even where there is no obligation to submit it, and that there is no time limit for HMRC to issue a closure notice.

Background

The taxpayer purchased a property in southwest London for £4.2 million. Shortly after entering into the contract to acquire the property, the taxpayer entered into an agreement to grant a call option. The property purchase was completed and on the same day the option was granted, but never exercised. The taxpayer filed a voluntary nil SDLT return on the purchase of the property. An SDLT return was also filed as regards the acquisition of the option.

The taxpayer relied on sub-sale relief pursuant to section 45(3) FA 2003 in arguing that no SDLT was due on the purchase, in particular the application of section 45(1)(b) FA 2003 to the agreement to grant the option. However, subsequent legislative amendments, with retrospective effect, disallowed sub-sale relief in these circumstances. The taxpayer had previously tried to challenge the legality of this retrospective amendment in judicial review proceedings, but to no avail.

HMRC issued two documents in relation to the nil SDLT return:

— on 7 September 2016 - a closure notice concluding that SDLT was due on the full purchase price of the property amounting to £294,000; and

— on 25 September 2018 - a discovery assessment for the same amount, in case it was determined that the closure notice had not been validly issued.

The taxpayer sought to argue that the SDLT return had been made on a "voluntary" and "unsolicited" basis, and accordingly that HMRC's enquiry into the return was not valid. Further, it argued that the closure notice was not valid because the time limit in paragraph 31 of schedule 10 FA 2003 applied.

Decision

The UT concluded that HMRC's enquiry into the SDLT return was validly opened even if such return was not strictly necessary. The UT also agreed with the FTT's finding that, once an enquiry into a return has been opened, there is no time limit within which HMRC must issue a closure notice. It was concluded that the time limit in paragraph 31 of schedule 10 FA 2003 only applied to discovery assessments, which did not include self-assessments contained in land transaction returns that may be amended by HMRC following an enquiry.

Comment

This decision ensures that HMRC are not left with the difficult task of determining whether an SDLT return is strictly necessary before deciding whether a notice of enquiry can be issued – which may be impractical to determine without first opening an enquiry. Taxpayers should also be aware that simply failing to submit a return will not necessarily avoid an enquiry. In that event, HMRC have powers to issue determinations as to tax, which can then only be displaced by the taxpayer submitting a self-assessment return (thereby allowing HMRC to open an enquiry).

FTT makes strict Unless Order following extensive HMRC delays

In *Ellis v HMRC* [2023] UKFTT 388 (TC), an HMRC application to allow late submission of witness statements was allowed, but came with a strict Unless Order that would automatically bar HMRC if they failed to comply with further FTT directions.

Background

This decision concerns preliminary applications made with respect to an underlying VAT case. In the substantive case, an individual appealed against a personal liability notice issued to him by HMRC, relating to a VAT penalty charged against a company of which he was a director.

The preliminary applications heard by the FTT related to the potential evidence that the parties wished to rely on, and included an application by HMRC for late admission of seven witness statements (with exhibits).

The main litigation had already been marred by a litany of delays and missed deadlines, particularly by HMRC. This included two requests by HMRC for an extension to the deadline for filing witness statements. Although these were granted, HMRC nonetheless missed the extended deadline, and then applied for leave to file one late witness statement. This application was granted, but the judge noted at the time that this would be taken into account in any later case management proceedings.

HMRC then applied for leave to file an additional seven witness statements, which formed the subject of the present decision. HMRC missed the deadline for filing their submissions with respect to this preliminary matter. In addition, they filed their supporting bundle to the FTT late, and failed to provide the bundle to the appellant until less than 24 hours before the date set for the hearing.

Decision

Based on previous case law, the FTT established that the first question when considering whether to admit late evidence was whether the evidence was relevant to the case. If it was, there would need to be a compelling reason not to allow it. Determining this point was a balancing exercise, to achieve a trial that reaches a conclusion by means of a process that is fair to all parties. This would involve considering the likely probative value of the evidence as well as any unfair prejudice to either party, and general principles of good case management.

In this case, the seven witness statements were held to be relevant to the appeal, so there would need to be a compelling reason not to admit them. It was clear that it would be severely damaging to HMRC's case if the statements were not admitted. This needed to be balanced against the potential prejudice to the appellant, which the FTT considered would not be as severe: the delay that came from admitting the witness statements would cause additional financial and emotional strain for the appellant, but would not require a longer hearing than if the witness statements had been admitted on time by HMRC.

In terms of good case management, the hearing had not yet been listed, so the application would not result in the loss of a hearing date. The witness statements were substantively the same as had been submitted in an earlier appeal against the VAT penalty by the taxpayer company, so they were not new to the appellant, and he would have sufficient time to prepare a case. The FTT did note that "[i]t is sometimes easy for a large organisation such as [HMRC] to overlook the difficulties and pressure that an unrepresented litigant faces in conducting litigation" and that its decision may have been different if the appellant had provided medical evidence of the strain the delay was likely to cause.

Finally, the FTT referred to the history of delay by HMRC in this case and that, even in making the present application relating to missed deadlines, HMRC had failed to comply on time with the FTT's directions. The cumulative effect of these missed deadlines was that the substantive hearing had been significantly delayed. The FTT considered that it was required to take a forward view, and that HMRC's behaviour gave rise to concerns about the future progress of the appeal. The FTT felt that such concerns could be met by issuing directions that carried sanctions if there was further breach.

On that basis, the FTT allowed HMRC's application, but also issued an "Unless Order", automatically barring HMRC from playing a further part in the proceeding should they failed to comply with any of the directions. Dismissing HMRC's request that the Unless Order be made discretionary, the FTT stated that HMRC's approach to the appeal so far "suggests there has been considerable 'oversight', and the sanction of automatic barring is the only remedy that will ensure that [HMRC] will focus their attention appropriately to give this matter the priority it merits".

Comment

In our experience, HMRC delays are becoming increasingly common in tax litigation. Although it is clear that the FTT does have the tools available to sanction HMRC in these circumstances (and ultimately bar HMRC from taking part in the proceedings), it can be reluctant or slow to do so in practice even where there has been a long history of delay and missed deadlines (as the circumstances in this case demonstrate). Taxpayers should be prepared to take robust action where appropriate, and their professional advisers will be able to advise on the best strategy depending on the facts of the case.

While the FTT here pointed out that delays can have serious financial and emotional consequences for taxpayers, a further concern is that late payment interest will continue to accrue until tax is paid, even where it is agreed with HMRC that payment of tax may be postponed pending the outcome of litigation. Given that late payment interest rates track Bank of England rates, which continue to rise, the increased rates of interest charged by HMRC may be particularly controversial in circumstances where, such as in this case, a taxpayer feels that HMRC have unreasonably delayed litigation proceedings.

Although there is no formal appeal procedure in respect of the amount of statutory interest charged, it is open to taxpayers to raise objections to statutory interest on certain limited grounds. Objections will normally be considered by HMRC's Interest Review Unit once any underlying tax has been paid (so that the amount of interest chargeable is known). Failing that, the only recourse is likely to be judicial review. Taxpayers who wish to raise an objection should seek professional advice as to whether this may be possible in their particular circumstances and also to discuss related strategy.

First case on HMRC information powers relating to enabler penalties

In *Asset House Piccadilly Ltd v HMRC* [2023] UKFTT 385 (TC), the FTT dismissed an appeal against an HMRC information notice issued under legislation relating to penalties for enablers of defeated tax avoidance arrangements. This is the first case to consider these relatively new HMRC information powers.

Background

Pursuant to part 1 of schedule 16 to the Finance (No. 2) Act 2017, a penalty is payable by the "enablers" of abusive tax arrangements that are later defeated. Arrangements are "tax arrangements" for these purposes if, having regard to all of the circumstances, it is reasonable to conclude that the obtaining of a tax advantage was the main purpose, or one of the main purposes, of the arrangements.

Part 9 of schedule 16 to the Finance (No. 2) Act 2017 modifies HMRC's information powers (under schedule 36 to the Finance Act 2008), so that HMRC may by written notice require a person to provide information or produce a document if reasonably required for the purpose of checking the relevant person's position as regards liability for a penalty under the regime referenced above, or otherwise ascertaining the identity of any other "enablers" of abusive tax arrangements under that regime.

In July 2021, a HMRC officer issued a notice to provide information on suspicions that the appellant was an "enabler" of certain abusive tax arrangements. In this case, the abusive arrangements concerned remuneration trusts using fiduciary receipt arrangements. The appellant appealed against the information notice on three grounds:

— the description of the appellant's activities was incorrect and the appellant was not an "enabler" (meaning that the grounds upon which the notice was issued were invalid);

— the notice amounted to an abuse of process as it required information that was of relevance to ongoing proceedings regarding whether the appellant was a "promoter" under section 307 of the Finance Act 2004 (and that the proper course of action would be for HMRC to either make an application for disclosure as part of, or otherwise await the outcome of, those proceedings); and

— the notice was contrary to Article 6 of the European Convention on Human Rights on the basis that it infringed the appellant's right against self-incrimination.

Decision

The appeal was dismissed on all grounds.
The FTT rejected the argument that the grounds upon which the notice was issued were invalid. The judge stated that the relevant test for the issue of a valid notice requires "objectively viewed… a genuine suspicion that the appellant would, or might, be liable to an enabler penalty if the arrangements suffered defeat". Or, in other words, provided there is a "genuine and legitimate" investigation or enquiry of any kind into the tax position of a taxpayer that is neither irrational nor in bad faith, that is sufficient. After reviewing the evidence upon which the issuing HMRC officer based their suspicion, the judge considered that, despite limitations in the officer's understanding of the tax arrangements, the evidence was that the officer had acted in good faith, and had rationally and reasonably embarked on a genuine and legitimate investigation or enquiry. This evidence included a circular movement of money, a proliferation of offshore vehicles, and confirmation from two users of the trust arrangements that the appellant had introduced them to the concept.

The FTT also did not accept that the notice constituted an abuse of process. The FTT reasoned that the time and place to argue about abuse of process would be as and when (or if) HMRC attempt to utilise any documentation or information provided in response to the notice.

The ground of appeal regarding Article 6 was dismissed on the basis that it was held not to be engaged in preliminary or investigative stages, such as the issue of an information notice (as there was no guarantee that an enabler penalty would be issued). The FTT concluded that "if HMRC seek to rely on material derived from the Notice, then that can be challenged at an appropriate juncture". Additionally, it was noted that Article 6 rights are not themselves absolute because of the need for a balance between the general interest of the community and the personal rights of the individual. The FTT noted that there is a clear public interest in deterring professional advisers from assisting taxpayers to participate in abusive tax arrangements.

Comment

This is the first case that considers HMRC's relatively new information powers in connection with the enablers legislation. It provides valuable guidance for taxpayers and their advisers on the knowledge and extent of understanding required by an HMRC officer in order to issue a valid information notice, and the appropriate timing and forum for appeals based on abuse of process or an infringement of the ECHR Article 6 right against self-incrimination.

Other developments

Public Accounts Committee publishes report on tax compliance during Covid-19

The Public Accounts Committee's report, "Managing tax compliance following the pandemic" (3 May 2023), noted that, in response to the pandemic, HMRC re-deployed more than 4,000 compliance staff to help with Covid-19 support schemes. HMRC therefore opened fewer tax enquiries and prosecuted fewer people for tax evasion during the pandemic (tax years 2020-21 and 2021-22), with tax revenues falling as a result. The report recommends that HMRC should have a clear plan and trajectory to catch up on compliance activity and also to support compliant taxpayers who may require help. In light of a concern that there are clear signs that the tax gap may grow, it was recommended that HMRC build more "resilience" in to the tax system. The report therefore adds further pressure on HMRC to crack down on tax avoidance, evasion and other non-compliance.

The report also notes that there is some evidence of HMRC overcharging taxpayers. HMRC test 400 of its completed compliance cases each year. These tests have identified seven cases where taxpayers had been overcharged by a total of over £32 million. The report recommends that HMRC take all proportionate steps to identify and correct overcharges and make clear what compensation may be available in these circumstances. Any taxpayers who think they may be affected should consult an appropriate professional adviser.

New Code of Practice 9

Where HMRC suspect tax fraud, they may use "Code of Practice 9" ("**COP9**"). This is a civil procedure whereby the relevant individuals are offered the opportunity to make a full disclosure of the fraud through the associated Contractual Disclosure Facility ("**CDF**") and pay any tax due (together with any interest and penalties), in return for which HMRC will agree not to start a criminal investigation with a view to prosecution.

It is HMRC's policy aim to deal with cases of suspected tax fraud by using COP9 wherever appropriate. Criminal investigation is typically reserved for cases where HMRC want to establish a strong deterrent or where the conduct involved means that only a criminal sanction would be appropriate (e.g., organised crime).

On 14 June 2023, HMRC published an updated version of COP9 as "part of a wider push to re-establish COP9 as HMRC's primary civil investigation tool in tackling tax fraud". Key changes to the previous version include, as pre-conditions to HMRC's agreement not to pursue a criminal investigation, the requirement that taxpayers "personally" attend any meetings requested by HMRC, and repay any required tax, interest and penalties within a period of time agreed with HMRC.

New sections have also been added to set out, for example, when COP9 can cover fraud in respect of HMRC functions not involving tax (e.g., Covid-19 support schemes), and setting out what HMRC can do in circumstances where, after having accepted the CDF, an individual rescinds their admission of deliberate behaviour.

New failure to prevent fraud offence

The Government has announced the creation of a new failure to prevent fraud offence, designed to hold organisations to account if they profit from fraud committed by employees. An organisation will be liable where a specified fraud offence is committed by an employee or agent, for the employee's benefit, and the organisation did not have reasonable fraud prevention procedures in place. There is no requirement that the employer knew about or directed the fraud. The offence will only apply to large bodies corporate and partnerships. The new offence echoes the strict liability corporate offences relating to the failure to prevent the facilitation of tax evasion by associated persons, introduced from 30 September 2017.

Tax Administration and Maintenance Day

On 27 April 2023, the Government announced a package of technical proposals as part of "Tax Administration and Maintenance Day". Items of particular interest are summarised below.

Information and data
A call for evidence was published on how HMRC's information and data gathering powers and taxpayer safeguards could be updated to enable digital transformation of taxpayer services, improve HMRC's compliance capabilities, and reduce administrative burdens, whist ensuring taxpayer information is appropriately protected. The call for evidence focuses on standardising data provision from third parties, designing more flexible legislation, considering pre-population of returns, and simplifying powers to make them more consistent across different tax regimes.

Tackling non-compliance in the umbrella company market
The Government announced that it would publish a summary of responses to the 2021 call for evidence on the umbrella company market and a consultation on policy options to regulate umbrella companies and tackle non-compliance. The corresponding consultation was launched on 6 June 2023.

Tackling promoters of tax avoidance
A consultation was published on the introduction of a new criminal offence for promoters of tax avoidance who fail to comply with a legal notice from HMRC to stop promoting a tax avoidance scheme. The consultation also considers the expedition of disqualification of company directors involved in promoting tax avoidance, including those who exercise control or influence over the company.

Charities compliance measures
A consultation was published aimed at tackling tax non-compliance in the charitable sector. It seeks views on tainted charity donations, approved charitable investments, non-charitable expenditure and charity filing obligations.

Tax debt from non-paying businesses
A summary of responses to the consultation on the modernisation of tax debt collection from non-paying businesses was published. Responses had been received from 13 stakeholders. The intention is now to further investigate the approach to modernising HMRC's powers in this area.

Evaluation of HMRC's implementation of powers, obligations and safeguards
The Government has published a report detailing how HMRC have delivered on the commitments made to help build and maintain public trust in the tax system in the February 2021 report "Evaluation of HMRC's implementation of powers, obligations and safeguards". These commitments focused primarily on raising awareness of obligations, ensuring that HMRC continue to use powers professionally and with respect during compliance enquiries and providing reassurance to taxpayers that HMRC are being consistent and proportionate when taxpayers make errors.

Diverted profits tax, transfer pricing and permanent establishment reform
It was announced that a consultation will be published in these key areas, with a view to simplifying and updating the relevant legislation.

Reserved Investor Fund consultation
A consultation was published on the scope and design of the tax regime for a new type of investment fund, the Reserved Investor Fund, to be structured as an unauthorised co-ownership contractual scheme.

Off-payroll working
A technical consultation was published on potential legislative changes to address the over-collection of tax in relation to non-compliance with the off-payroll working rules, potentially allowing the off-set, against the PAYE liability of the deemed employer, of tax and NICs already paid by the worker and their personal service company.

Additions to HMRC's published list of named tax avoidance schemes, promoters, enablers and suppliers

In the last few months, HMRC have made a number of additions to their published list of named tax avoidance schemes, promoters, enablers and suppliers. The list (in its current form) was first published in April 2022, under powers granted to HMRC by section 86 of the Finance Act 2022 ("**FA 2022**").

Additionally, in May, HMRC added a new section entitled "evidence of marketing material used by tax avoidance promoters and suppliers", and at the same time published a copy of a marketing document relating to remuneration trust arrangements circulated by two "promoters". This was accompanied with a statement by HMRC that they were exercising their powers under sections 86(1) and (2) FA 2022, which in particular allow them to publish any information, "including documents", that they consider appropriate to inform taxpayers about the risks associated with a avoidance scheme and/or to protect the public revenue.

Late interest payments

HMRC are required by statute to charge interest where tax is not paid by the required date. The rate of interest charged fluctuates but tracks at 2.5% above Bank of England rates. In contrast, the rate of repayment interest is set at the base rate minus 1% (with a minimum limit of 0.5%). The means that, with effect from 31 May 2023, the rate is 7% for late payment interest and only 3.5% for repayment interest. The further rate rise announced by the Bank of England on 22 June 2023 will see the rates change again in July 2023 (with the late payment rate rising to 7.5%).
Late payment interest will continue to accrue until tax is paid, even where it is agreed with HMRC that payment of tax may be postponed pending the outcome of a statutory appeal or review. The increased rates of interest charged by HMRC may be particularly controversial in circumstances where, for example, a taxpayer feels that HMRC have unreasonably delayed an investigation or litigation proceedings.
Whilst there is no formal appeal procedure in respect of the amount of statutory interest charged, it is open to taxpayers to raise objections to statutory interest on certain limited grounds. Objections will normally be considered by HMRC's Interest Review Unit once any underlying tax has been paid (so that the amount of

interest chargeable is known). Failing that, the only recourse is likely to be judicial review. Taxpayers who wish to raise an objection should seek professional advice as to whether this may be possible in their particular circumstances and also to discuss related strategy.

Retained EU law

The Government has tabled an amendment to the Retained EU Law (Revocation and Reform) Bill, replacing the previous "sunset"' provision (which would have revoked EU retained law by default at the end of 2023, unless expressly excluded or extended) with a specific list of retained EU law to be revoked by the end of 2023. The Government's stated aim is to lighten the regulatory burden on businesses and help to spur economic growth.

In principle, the revocation of retained law could affect certain EU derived subordinate legislation (not primary legislation) such as certain VAT and customs regulations, but the Government has said that there will be a "bespoke approach… in a future Finance Bill".
In theory, it could also cause the re-application of the 1.5% stamp duty/Stamp Duty Reserve Tax charge on an issue of relevant securities to a depositary receipt issuer or to an operator of a clearance service (which HMRC previously accepted that it could not impose on the basis of incompatibility with EU law). However, HMRC have previously stated that there was no intention to do so following Brexit.

Customs Advance Valuation Rulings ("AVRs")

The introduction of AVRs was announced in the 2023 Spring Budget. AVRs provide importers with legal certainty that their chosen customs valuation is correct, but are not mandatory. Once obtained, AVRs are legally binding on both parties for a period of three years, subject to cancellation or withdrawal. Recently HMRC have issued guidance on how to apply for such a ruling. The application must be made before goods are imported or any import declarations are made. If an importer disagrees with an AVR, it can appeal to the Advance Valuation Ruling Team or to the FTT.

High Court judges reported to be investors in tax avoidance schemes

According to the Financial Times, three High Court judges, including one who has ruled on tax avoidance cases, have been investors in tax avoidance schemes which were challenged by HMRC. Two further High Court judges were reported to have been investors in schemes described as "highly abusive" and "completely contrived".

This has raised the question of whether the current ad-hoc discretionary disclosure requirements set out in the UK Guide to Judicial Conduct are stringent enough. High Court judges are only required to disclose their financial interests if they believe there to be a risk of a conflict of interest in a specific set of circumstances. This is in contrast to other jurisdictions, where judges (for example United States federal judges) are required to make systematic disclosures of their financial interests.

Mastermind of one of UK's largest tax frauds sentenced

In May 2023, following a 14-week trial and one of the biggest tax fraud cases ever investigated by HMRC, the mastermind of one of the UK's largest carousel tax frauds was sentenced to 20 years imprisonment. His offences included sales of counterfeit clothing, attempting to steal £97 million through fraudulent VAT claims on false exports of textiles and phones, and money laundering of the criminal proceeds through offshore bank accounts. HMRC managed to stop £64 million of the fraudulent VAT claims from being obtained by the defendant's gang, and have seized more than £78 million of the gangs UK assets. HMRC's Fraud Investigation Service have said the process is now underway to recover all the relevant proceeds of crime. At the Spring Budget 2023, Chancellor Jeremy Hunt announced the doubling of the maximum sentences for the most egregious forms of tax fraud (from seven to 14 years).

Latest HMRC nudge letter campaigns

The behavioural science of "nudge theory" has become an increasingly used weapon in HMRC's arsenal over the last decade or so – i.e., the idea that people can be better directed towards a desired course of action through suggestion rather than obligation. UK taxpayers may have noticed the same concept at work when completing their online tax returns, where certain information is now pre-populated based on figures held by HMRC (the idea being that the taxpayer will likely accept those figures by default). Over the last few months, HMRC have launched several new nudge letter campaigns on various issues, as summarised below.

Electronic sales suppression disclosure (April 2023)
HMRC have issued nudge letters relating to the use of till systems that hide or reduce the value of individual transactions on a business's electronic sales records (known as "electronic sales suppression"). The stated intention of the letters is to provide an opportunity for recipients to come forward voluntarily and disclose undeclared sales. The nudge letters direct recipients to a specific online process that has been set up for the purpose of making disclosure. The material does not appear to make any reference to reduced penalties being available. Taxpayers should also be aware that this online process is different to the CDF (see above), which may be more suitable for making a disclosure to HMRC in certain circumstances. Recipients are also requested to contact HMRC at an email address provided if they do not believe they have any undeclared sales.

Business Asset Disposal Relief ("BADR") claims (May 2023)
HMRC are sending nudge letters to taxpayers who they believe have exceeded statutory limits for BADR claims. One letter is being sent to taxpayers who appear to have exceeded the lifetime limit of £1 million prior to making a claim in their 2021 to 2022 tax return, with another letter to those whose claim in that return would cause them to exceed the limit. Recipients are asked to amend their self-assessment return within 30 days from the date of the letter, or risk HMRC opening an enquiry.

Gift aid repayment claims (May 2023)
HMRC have launched a nudge campaign targeted at charity trustees, with the stated aim of helping them with their compliance in relation to Gift Aid claims on aggregated donations. The letter reminds recipients of the requirements for Gift Aid on aggregated donations, and in particular notes the associated record keeping obligations. There is no suggestion in the letter that HMRC believe the recipient to have failed to comply with the rules, and it appears to have been sent to those who have claimed aggregated donations in recent months.

UK residents named in the leaked "Pandora Papers" (June 2023)
In a press release published on 12 June 2023, HMRC announced that they are writing to UK residents named in the files of 14 offshore financial services providers which were leaked during 2021 and 2022 and became known as the "Pandora Papers". The letters remind recipients to report all their overseas income or gains on which they owe UK tax, and warn them that, should they fail to do so, HMRC may charge penalties of up to 200% of any tax due. Recipients are asked to check that they have correctly reported all overseas income and gains within 30 days of the date of the letter. Additionally, the letter states that HMRC may also prosecute recipients should their behaviour be found to be dishonest. The press release states that recipients can make disclosures under either the CDF (see above) or the Worldwide Disclosure Facility (as appropriate).

Profit Diversion Compliance Facility ("PDCF") (June 2023)
A new tranche of nudge letters has been issued by HMRC in relation to the PDCF. The PDCF was launched in 2019 for multinational enterprises using arrangements targeted by diverted profits tax, to give them the opportunity to bring their tax affairs up to date, review the design and implementation of their transfer pricing policies, alter such policies if appropriate, and put forward a report with proposals to pay any additional tax, interest and (if applicable) penalties due. The letters are sent to those who HMRC have identified as using arrangements targeted by diverted profits tax – the letter advises recipients to register on the PDCF within 30 days of receipt, or risk HMRC opening an investigation.

Action points
Any taxpayers who receive nudge letters, even those confident of their tax position, should seek professional advice as soon as possible. Whilst nudge letters do not make specific accusations and are rarely overtly threatening in tone, they are generally based on actual data held by HMRC. Taxpayers who ignore these letters do so at their peril – failure to take action or respond is likely to mean that there is an imminent risk of HMRC starting an investigation (either under civil procedures or, in cases of suspected fraud, using their criminal powers). Early disclosure may also mitigate penalties.

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