Tax update

August 2018

In this month's update we report on (1) the summary of responses to HMRC's consultation on extending time limits for offshore non-compliance; (2) HMRC's policy paper on "profit-fragmentation"; and (3) HMRC's consultation on proposals for new civil information gathering powers for HMRC. We also comment on three recent decisions relating to (1) the appropriate forum in which to litigate; (2) the Supreme Court's decision in "Project Blue"; and (3) whether a loan by a pension scheme was an unauthorised payment.

News items

HMRC publishes summary of responses to its consultation on extending time limits for offshore non-compliance

On 6 July 2018, HMRC published an updated version of the summary of responses to its consultation on the implementation of a new minimum tax assessment time limit of 12 years to make assessments or issue notices of determination in cases involving offshore income, gains or chargeable transfers. more›

HMRC publishes policy paper on "profit fragmentation"

On 10 July 2018, HMRC published a policy paper on "profit fragmentation". The government intends to tackle tax avoidance schemes which move profits outside the charge of UK tax, often by using offshore trusts and companies, by introducing new rules which will add such profits to the profit of the UK trade. more›

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Case reports

Bell: The importance of selecting the correct forum when alleging unfairness on the part of HMRC

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Any comments or queries

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About this update

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Project Blue: Supreme Court allows HMRC's appeal in SDLT sub-sale case

In *Project Blue Limited v HMRC* [2018] UKSC 30, the Supreme Court (by a majority) has found that section 75A, Finance Act 2003 (an anti-avoidance provision), was applicable resulting in stamp duty land tax (SDLT) being payable notwithstanding that sections 45 (sub-sale relief) and 71A (exemption for alternative property finance) Finance Act 2003, would have otherwise resulted in no SDLT being payable. more>

Bayonet Ventures: Loan by pension scheme was not an unauthorised payment

In *Bayonet Ventures LLP & Anor v HMRC* [2018] UKFTT 262 (TC), the First-tier Tribunal (FTT), has held that a loan made to a limited liability partnership (LLP) by a pension scheme in which one of the partners of the LLP was a member, was not an unauthorised payment (section 164, Finance Act 2004) and should not be treated as a loan to the partner (section 863, Income Tax (Trading and Other Income) Act 2005 (ITTOIA)) as section 863 only applies if the LLP is carrying on a "trade, profession or business with a view to profit", which it was not. more>

News items

HMRC publishes summary of responses to its consultation on extending time limits for offshore non-compliance

On 6 July 2018, HMRC published an updated version of the summary of responses to its consultation on the implementation of a new minimum tax assessment time limit of 12 years to make assessments or issue notices of determination in cases involving offshore income, gains or chargeable transfers. It states that respondents supported the government's overall aim to act decisively against offshore tax evasion, avoidance and non-compliance, and that concerns that were raised mainly related to the scope of the measure and the burden it could impose on taxpayers.

A copy of the summary of responses can be viewed here.

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HMRC publishes policy paper on "profit fragmentation"

On 10 July 2018, HMRC published a policy paper on "profit fragmentation". The government intends to tackle tax avoidance schemes which move profits outside the charge of UK tax, often by using offshore trusts and companies, by introducing new rules which will add such profits to the profit of the UK trade.

Draft legislation has been published for technical consultation and the changes are intended to come into force from April 2019.

Where it is "reasonable to conclude" that the arrangements were entered into to obtain a UK tax advantage, HMRC will be able to issue a counteraction notice to remove that advantage – essentially by adding the alienated profits to the UK resident party.

HMRC has listened to concerns and the proposal requiring payment of any disputed tax upfront has been abandoned. It is claimed that the proposals will affect up to 10,000 taxpayers.

A copy of the policy paper can be viewed here.

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HMRC publishes consultation on amending its civil information powers

On 10 July 2018, HMRC published a consultation paper on options for amendments to its civil information powers.

Most of the proposals relate to third party notices about a known taxpayer. The proposed options include:

- aligning the process for issuing third party notices with that for taxpayer notices. This would mean that tribunal approval would not be required before issuing such a notice and the third party would have a right to appeal to the tribunal if the requirements were too onerous
- introducing a targeted power to obtain banking information. This would be modelled on the existing power contained in paragraph 34, Schedule 36, Finance Act 2008 (information relating to goods or services forming part of any person's statutory records) and, again, could be exercised without tribunal approval.

Additionally, HMRC proposes to extend Schedule 36 to allow information to be obtained if it is reasonably required for the purposes of any of its tax functions (for example, debt collection). HMRC also proposes to remedy a defect in the legislation charging increased daily penalties for failing to comply with a notice and to harmonise the penalty regime by extending increased daily penalties to all Schedule 36 notices.

The closing date for comments is 2 October 2018 and a response document will be published in the autumn.

A copy of the consultation document can be viewed here.

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Case reports

Bell: The importance of selecting the correct forum when alleging unfairness on the part of HMRC

In *Bell v HMRC* [2018] UKFTT 261 (TC), the taxpayer's appeal was struck out by the First-tier Tribunal (FTT), because that tribunal does not have jurisdiction to consider issues of public law.

Background

Mr James Bell (the taxpayer) appealed against a self-assessment to income tax in the sum of £24,926.40, in respect of the 2009/10 tax year.

The taxpayer argued that HMRC should have waived his liability to the tax in question on the basis that he was entitled to relief under Extra-statutory Concession A19 (ESC A19). ESC A19 applies where various conditions are satisfied, one of which is that, before being notified of the relevant tax arrears, the taxpayer in question formed the reasonable belief "that his or her tax affairs were in order".

The taxpayer claimed that prior to being made aware of the tax arrears, given the information about his earnings held by HMRC and the fact that he had not been informed of the claimed tax arrears by HMRC at an early stage, he reasonably believed that his tax affairs were in order.

HMRC disputed this and alleged that although there had been errors on its part in processing and acting on information which was in its possession, it was not reasonable for the taxpayer to have concluded, prior to him being informed of the tax arrears in question, that his tax affairs were in order on the ground that as he earned a large salary he should have realised that he ought to be paying more tax.

HMRC applied to the FTT to strike out the taxpayer's appeal.

HMRC argued that the FTT did not have jurisdiction to determine the appeal for the following reasons:

- the FTT has no jurisdiction to consider whether HMRC has acted unreasonably in failing to apply an extra-statutory concession because the remit of the FTT is confined to the appropriate application of the tax legislation; if a taxpayer wishes to challenge HMRC's refusal to apply an extra-statutory concession this must be done by way of judicial review proceedings, and
- the FTT has no jurisdiction to hear an appeal against a liability to income tax that has been self-assessed as section 31, Taxes Management Act 1970 (TMA), does not allow for appeals against self-assessment.

FTT decision

The appeal was struck out.

Although the FTT was of the view that the taxpayer had a "justifiable grievance" in relation to the manner in which his tax affairs had been dealt with by HMRC, it confirmed that it was not within its power to adjudicate on the matter. The FTT referred to *The BT Pension Scheme (Trustees of) v HMRC* [2015] EWCA Civ 713, in which both the Upper Tribunal and the Court of Appeal confirmed that the FTT has no jurisdiction to determine common law issues of fairness. Such matters can only be dealt with by way of judicial review.

The FTT also found that as the taxpayer had completed a self-assessment he had no valid grounds to appeal under section 31, TMA.

Comment

This case demonstrates the importance of establishing the correct litigation forum. In practice, identifying the correct forum is not always straightforward, especially since the decision of the Court of Appeal in *R (oao Glencore Energy UK Ltd) v HMRC* [2017] EWCA Civ 1716.

If a taxpayer commences judicial review proceedings in the High Court, HMRC often argues that the taxpayer has an alternative remedy and should have brought an appeal before the FTT and if the taxpayer has pursued an appeal before the FTT, rather than judicial review proceedings, HMRC often argues that the FTT lacks jurisdiction (as it did in this case).

In circumstances where there is jurisdictional uncertainty it may be prudent for a taxpayer to make a "protective" application for judicial review (as there are strict time limits within which judicial review proceedings must be commenced) and file an appeal with the FTT. If appropriate, the judicial review proceedings can then be stayed pending the outcome of the proceedings before the FTT.

This is a complex area and it is important that taxpayers obtain specialist legal advice at the outset of a dispute in order to ensure their position is not prejudiced.

A copy of the decision can be viewed here.

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Project Blue: Supreme Court allows HMRC's appeal in SDLT sub-sale case

In *Project Blue Limited v HMRC* [2018] UKSC 30, the Supreme Court (by a majority) has held that section 75A, Finance Act 2003 (an anti-avoidance provision), was applicable resulting in stamp duty land tax (SDLT) being payable notwithstanding that sections 45 (sub-sale relief) and 71A (exemption for alternative property finance) Finance Act 2003, would have otherwise resulted in no SDLT being payable.

Background

In 2007, Project Blue Limited (PB), owned by the Sovereign Wealth Fund of Qatar, purchased the freehold of the Chelsea Barracks in London from the Ministry of Defence (MoD) for £959m. In order to make the purchase, PB obtained finance from a Qatari bank, Masraf al Rayan (MAR), which specialises in Islamic finance. Islamic finance seeks to comply with Sharia law, which prohibits interest being paid in connection with the lending of money.

On 5 April 2007, PB and the MoD entered into a contract to purchase the barracks. On 29 January 2008, PB contracted to sub-sell the freehold to MAR. Also on 29 January 2008, MAR agreed to lease the barracks back to PB. Upon completion, on 31 January 2008, the following occurred:

- MAR and PB entered into put and call options respectively requiring or entitling PB to repurchase the freehold in the barracks
- the MoD conveyed the freehold in the barracks to PB
- PB conveyed the freehold in the barracks to MAR, and
- immediately after that, MAR leased the barracks back to PB.

PB claimed that there was no liability to SDLT because of sub-sale relief provided by section 45(3), Finance Act 2003 (section 45 enables a purchaser of land to drop out of the SDLT equation if a secondary contract is substantially performed at the same time and in connection with the original property transfer). MAR claimed alternative property finance relief under section 71A, Finance Act 2003 (section 71A creates exemptions for alternative property finance which complies with the prohibition of usury in Sharia law). Section 71A relief was also claimed in relation to the lease by MAR to PB.

The parties therefore claimed that no SDLT was payable in relation to the acquisition of the barracks.

HMRC challenged PB's £0 SDLT return and issued a closure notice which amended the amount of SDLT due from £0 to £38.6m.

PB appealed to the First-tier Tribunal (FTT). In the FTT, HMRC successfully applied to amend its case to increase the amount of SDLT due from £38.6m to £50m (being 4% of the total £1.25bn which MAR paid to PB). The FTT dismissed PB's appeal holding that the anti-avoidance provision in section 75A, Finance Act 2003, was applicable.

PB appealed to the Upper Tribunal (UT). In the UT, PB changed its position and argued that MAR was not entitled to section 71A relief because, on a proper understanding of the related provisions of Finance Act 2003, the MoD was the vendor of the barracks in terms of section 71A(2). The UT rejected this argument and concluded that PB was the vendor. PB's appeal was dismissed but the UT revised the chargeable consideration back to £959m.

Both parties appealed to the Court of Appeal (CA).

In the CA, PB successfully argued that MAR should be treated as the purchaser for SDLT purposes and therefore it was MAR who was liable to £50m SDLT on the £1.25bn it had paid to PB for the barracks. This was on the basis that alternative property finance relief, under section 71A, was not available due to the interaction with the sub-sale rules.

Following the CA's decision in *DV3 RS LP v HMRC* [2013] EWCA Civ 907, the CA was obliged to disregard PB's acquisition from the MoD for SDLT purposes. Accordingly, for the purposes of SDLT, MAR was to be treated as acquiring an interest in land directly from the MoD and it was on MAR that the liability for SDLT fell.

HMRC argued that section 71A had the effect of shifting any liability for SDLT from MAR to PB. The CA found, however, that section 71A relief only applied in circumstances where the vendor was the person making the financial arrangements with the financial institution. Following the decision in *DV3 RS LP*, the vendor was not PB, as the transaction between MAR and PB had to be disregarded under sections 44-45, Finance Act 2003. The vendor was the MoD. Accordingly, in the view of the CA the exemption to SDLT, contained in section 71A, did not apply to MAR and SDLT remained payable by MAR.

The CA dismissed HMRC's arguments on the application of section 75A, on the basis that the amount of SDLT that would have been payable on the "notional transaction" was equal to the £50m that was payable by MAR.

HMRC appealed.

Supreme Court judgment
The appeal was allowed (Lord Briggs dissenting).

The Court considered:

- who acquired the chargeable interest from the sale of the property by the MoD (ie who was the vendor for the purposes of section 71A), and
- does section 75A apply to impose SDLT on PB and if so, what was the value of the chargeable interest?

On the first issue, the Court concluded that PB was the vendor (under section 71A(2)), despite PB not acquiring a typical chargeable interest. The contract between the MoD and PB was disregarded, so the chargeable interest was considered to be the lease from MAR under section 75A.

With regard to the second issue, the Court concluded that the combined effect of sub-sale relief under section 45 and alternative property finance relief under section 71A, would have resulted in the transactions escaping SDLT, but for the anti-avoidance rule in section 75A. Following *Barclays Mercantile Business Finance Ltd v HMRC* [2015] 1 AC 684, the Court adopted a wide purposive approach to its interpretation and concluded that the relevant "notional transaction" to be assessed involved the MoD as vendor and PB as purchaser, of its chargeable interest in land, being the leasehold interest it obtained from MAR. In the view of the Court, the various transactions were all "involved in connection with" the disposal by the MoD of its chargeable freehold interest in the barracks. The chargeable consideration was £1.25bn paid by MAR to PB, as this was the largest amount given by any one person under the arrangements. As the SDLT payable in respect of the arrangements was £0 and this was less than the amount that would have been payable on the "notional transaction", SDLT of £50m (4% of £1.25bn) was due under section 75A.

Comment
The Supreme Court has endorsed the position adopted by both the UT and CA that section 75A has a broad application and that the taxpayer's motive for entering into the transactions is irrelevant. There is no requirement that the taxpayer has a tax avoidance motive. HMRC will no doubt be encouraged by this decision and given the pressure it is under to raise as much tax as possible it is likely that it will seek to rely on section 75A whenever a series of transactions produces less SDLT than would otherwise have been the case. In other words, HMRC is likely to invoke section 75A in circumstances where more SDLT could have been charged irrespective of whether there is an avoidance motive.

A copy of the judgment can be viewed here.

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Bayonet Ventures: Loan by pension scheme was not an unauthorised payment

In *Bayonet Ventures LLP & Anor v HMRC* [2018] UKFTT 262 (TC), the First-tier Tribunal (FTT), has held that a loan made to a limited liability partnership (LLP) by a pension scheme in which one of the partners of the LLP was a member, was not an unauthorised payment (section 164, Finance Act 2004) and should not be treated as a loan to the partner (section 863, Income Tax (Trading and Other Income) Act 2005 (ITTOIA)) as section 863 only applies if the LLP is carrying on a "trade, profession or business with a view to profit", which it was not.

Background

Up until 2012, Ronald Keith Howard (the second appellant) had operated as a sole trader. He set up Bayonet Ventures LLP (the first appellant) in around 2009 but did not transition his business into it immediately and it was not until 2012 that the first appellant began to trade. In November 2009, the second appellant established the Bayonet Ventures Pension Scheme (BVPS). The first appellant was the principal employer and administrator and the second appellant was a trustee and scheme member. In the same month, the scheme entered into a loan agreement with the first appellant, agreeing to lend it £66,000. The money was paid into the second appellant's bank account and the loan was not recorded in the first appellant's accounts for the relevant period.

BVPS filed its pension scheme tax return for the 2009/10 tax year. HMRC opened an enquiry into the return and on 13 June 2013 wrote to the scheme administrator, the first appellant, claiming that BVPS had made an unauthorised member payment of £66,000. The letter went on to assert that by reason of section 863, ITTOIA "the loan to the LLP is treated as a loan to the partners of the LLP. One of the partners of the LLP is also a member of the pension scheme". The letter went on to explain that HMRC considered the loan to be an "unauthorised member payment", within the meaning of section 164, Finance Act 2004.

The letter confirmed that HMRC had made an assessment in respect of a Scheme Sanction Charge at 40% of £66,000, being £26,400 and HMRC sent a notice of assessment to the second appellant.

On 17 June 2013, HMRC wrote to the second appellant asserting that BVPS had made a loan of £66,000 to the first appellant on 27 November 2009. It asserted that that loan must be treated as made to the individual members of the LLP and said that it was of the view that the loan was an unauthorised member payment because it fell outside of section 164, Finance Act 2004. Accordingly, the second appellant had to pay an unauthorised payment charge under section 208, Finance Act 2004, in the sum of £26,400 and an unauthorised payment surcharge under section 209, Finance Act 2004, at a rate of 15%, being £9,900. The letter enclosed an assessment dated, 17 June 2013, against the second appellant, in the total sum of £36,300.

The first appellant and second appellant appealed the assessments.

The appeals involved:

- an appeal by the second appellant against the assessment of £26,400 made against him on the basis that HMRC had deemed him to be the scheme administrator when, as a matter of fact, he was not
- an appeal by the first appellant against the scheme sanction charge which had been levied on the basis that there had been an unauthorised member payment, and
- an appeal by the first appellant against the surcharge on the allegedly unauthorised member payment.

FTT decision
The appeals were allowed.

With regard to the unauthorised payment charge in the sum of £26,400, the FTT concluded that the assessment had to be discharged. HMRC had no statutory power to appoint the second appellant as, or deem him to be, a scheme administrator.

In relation to the unauthorised member payment charge and surcharge, the FTT determined that pursuant to the loan agreement, the £66,000 had been loaned by the scheme to the first appellant. The first appellant was free to use the money as it pleased, and it was free to pay it to the second appellant, provided that such payment did not breach the terms of the loan agreement. Thus, the mere fact that the money passed from the scheme to the second appellant did not mean that the loan had been made to the second appellant.

The FTT said that the identity of the parties to a loan is a matter of law, albeit informed by the factual matrix. The issue was whether section 863(1), ITTOIA, required HMRC to treat the loan as having been made to the second appellant. Under section 863(1), if an LLP carries on a trade, profession or business with a view to profit, its activities are to be treated for income tax purposes as being carried on "in partnership by its members", and not by the LLP as such.

In the instant case, the question was whether section 863(1) applied even though the first appellant had not begun trading until after the loan had been made. HMRC argued that it did, on the basis that an LLP was to be treated as carrying on a business with a view to profit from the moment it comes into existence, regardless of when it actually begins trading. The FTT rejected that argument. In doing so, the FTT commented that there was no basis for departing from the literal rule of statutory construction. If that gave rise to some perceived gap in the legislation, it was to be filled by Parliament and not by the inventiveness of judges.

The first appellant had not been carrying on a trade, profession or business with a view to profit when the loan was made, and the mere fact of it having entered into a loan agreement and received a loan did not mean that it had. Furthermore, section 863(1) did not say that all the activities of an LLP were to be treated as being carried on by its members. It simply assimilated the position of partners in an LLP with that of partners in a non-LLP. In conclusion, there had been no unauthorised member payment. The assessments in respect of the unauthorised member payment and the surcharge therefore had to be discharged.

Comment
Although this case relates to a payment by a pension scheme, it could have wider ramifications in that it clarifies the meaning of the deeming provisions relating to LLPs and their members, in particular, the notion that the activities of an LLP are the activities of its members.

This decision is yet another example of HMRC unsuccessfully inviting the FTT to depart from a literal interpretation of the statutory provisions under consideration (see our recent blog on *Patel & Anor v HMRC* [2018] UKFTT 0185 (TC), which can be viewed here). When a literal interpretation is unhelpful and does not suit HMRC, it tends to argue for a purposive interpretation. This decision demonstrates that the FTT and the courts will not always be amenable to such an approach.

A copy of the decision can be viewed here.

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