Tax update

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Any comments or queries?

Adam Craggs
Partner
adam.craggs@rpc.co.uk
+44 20 3060 6421

Robert Waterson
Senior Associate
robert.waterson@rpc.co.uk
+44 20 3060 6245

News

Beneficial ownership plan: HMRC publishes policy paper

HMRC has published details of how the UK intends to implement the G20 High Level Principles on Beneficial Ownership Transparency agreed in Brisbane in November 2014. more›

Offshore tax evasion: HMRC press release

At the end of November, HMRC launched a campaign warning tax evaders that it would soon start to receive details on UK taxpayers from more than 90 countries, under new global agreements. more›

Consultation reponses on sanctions for tax avoidance

HMRC has released a summary of the responses to its consultation on the introduction of new sanctions for taxpayers who use tax avoidance structures. Proposed new rules would introduce escalating sanctions for those using arrangements which are found not to work and set "warning periods". more›

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Hely-Hutchinson: taxpayer wins legitimate expectation judicial review

In *R(oao Hely-Hutchinson) v HMRC*[1], the High Court has held that a taxpayer who incurred capital losses as a result of the Court of Appeal decision in *Mansworth v Jelley*[2], and subsequent HMRC guidance, had a legitimate expectation that those capital losses would not be denied, and that the closure notices denying those losses should be quashed. more›

Burgess: HMRC fails to discharge burden of proof in discovery assessment case

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Raftopoulou: Tribunal accepts reasonable excuse defence for late claim for repayment of tax

In *Raftopoulou v HMRC*[6], the UT has confirmed that a taxpayer can make a valid claim for repayment of overpaid tax, notwithstanding expiry of the statutory time limit for making such a claim, if the taxpayer has a reasonable excuse for late filing. more›

News

Beneficial ownership plan: HMRC publishes policy paper

HMRC has published details of how the UK intends to implement the G20 High Level Principles on Beneficial Ownership Transparency agreed in Brisbane in November 2014.

A central database is to be established which will be used by authorities in the UK and, in the case of companies, data may be accessed by financial institutions and professionals when undertaking due diligence.

The Policy Paper can be read here.

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Offshore tax evasion: HMRC press release

At the end of November, HMRC launched a campaign warning tax evaders that it would soon start to receive details on UK taxpayers from more than 90 countries, under new global agreements.

The Offshore Tax Evasion (OTE) regime will see information passing to the UK tax authorities from a large number of countries. Although measures to tackle unlawful tax evasion are welcome, there is potential for error on the part of HMRC. Anyone contacted by HMRC following information received through the OTE regime should seek appropriate professional advice.

The government press release can be read here.

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Consultation reponses on sanctions for tax avoidance

HMRC has released a summary of the responses to its consultation on the introduction of new sanctions for people who use tax avoidance structures. Proposed new rules would introduce escalating sanctions for those using arrangements which are found not to work and set "warning periods".

It now seems inevitable that draft legislation will be introduced to implement these proposals. The new regime is likely to be complex and require careful consideration, in particular, the definition of what is "tax avoidance" is very wide.

The consultation responses can be read here.

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Hely-Hutchinson: taxpayer wins legitimate expectation judicial review

In *R(oao Hely-Hutchinson) v HMRC*[1], the High Court has held that a taxpayer who incurred capital losses as a result of the Court of Appeal decision in *Mansworth v Jelley*[2], and subsequent HMRC guidance, had a legitimate expectation that those capital losses would not be denied, and that the closure notices denying those losses should be quashed.

Background

Mr Hely-Hutchinson (the taxpayer), was employed by a bank. He was granted options over shares as part of his employment remuneration package following the commencement of his employment in 1989. He exercised and disposed of the shares in 1999 and 2000 and in each case disposed of the shares on the same day. The taxpayer completed his tax returns for the relevant years on the basis that, as was the understanding at the time, no gain or loss arose on the disposals.

The Court of Appeal, in *Mansworth v Jelley*, held that the acquisition cost for capital gains tax (CGT) purposes of shares acquired on exercise of a non-tax-advantaged employee share option was deemed to be the market value of the shares at the time of exercise of the option, rather than the actual amount paid to exercise the option and acquire the shares.

Following the Court of Appeal's judgment, on 8 January 2003, HMRC issued a technical note (the 2003 Guidance) explaining that it would treat the CGT base cost of shares acquired on an exercise of an employee share option which gave rise to an income tax liability as the sum of:

- the market value of the shares at exercise (as decided in *Mansworth v Jelley*)
- the amount charged to income tax on exercise (under section 120, Taxation of Chargeable Gains Act 1992).

The effect of this was that the amount charged to income tax was included in the base cost twice. A taxpayer who exercised a share and immediately sold the shares would make a capital loss equal to the amount charged to income tax. This beneficial treatment was to apply only for shares acquired under options exercised before 10 April 2003.

On 12 May 2009, HMRC published Brief 30/09 (the 2009 Guidance) announcing that it had received legal advice that the 2003 Guidance was incorrect, as it permitted the option holder to increase the base cost by adding on the amount chargeable to income tax. As a consequence, HMRC considered that the correct CGT base cost for shares acquired on exercise of an employee share option before 10 April 2003, was limited to the market value of the shares on exercise of the option.

In May 2014, HMRC published the decision of its Personal Taxes Contentious Issues Panel (the 2014 Guidance), which confirmed that it could use its collection and management powers to give taxpayers the benefit of the 2003 Guidance where:

- the taxpayer could demonstrate, on the balance of probabilities, that he relied on the 2003 Guidance
- the taxpayer would suffer detriment if those losses were denied

1. [2015] EWHC 3261 (Admin).
2. [2002] EWCA Civ 1829.

- the taxpayer would have been able to demonstrate a legitimate expectation that he could rely on the 2003 Guidance, except that HMRC's delay in dealing with his enquiry meant that the amount of evidence available to him was limited.

Following the Court of Appeal's decision in *Mansworth v Jelley* and the publication of the 2003 Guidance, the taxpayer adjusted his tax returns for the relevant years to claim capital losses for the amounts charged to income tax. In June 2003, HMRC opened enquiries into his returns. As is so often the case, the enquiries dragged on for many years and it was not until 12 November 2010 that HMRC finally issued closure notices refusing the capital losses. On 7 December 2010, the taxpayer appealed the closure notices and commenced judicial review proceedings.

The High Court's decision

The Court found in favour of the taxpayer and quashed the closure notices.

In the view of the Court, HMRC's responsibility for the collection and management of taxes under section 1, Taxes Management Act 1970 (TMA), co-existed with its duty to treat taxpayers fairly and not to discriminate between them, and to stand by its published statements in order to provide certainty to taxpayers.

The Court said that HMRC's duty to collect tax could not prevail over all other considerations where collection of tax would cause such unfairness as to amount to an abuse of power. Contrary to the 2014 Guidance, such unfairness was not limited to cases where a taxpayer had relied, to his detriment, on HMRC's published statements.

In the view of the Court, the 2003 Guidance was clear, unambiguous and devoid of relevant qualification (the criteria laid down in *R (Davies and Another) v HMRC* and *R (Gains-Cooper) v HMRC*[3]). The Court therefore concluded that the 2003 Guidance gave the taxpayer a legitimate expectation that his capital losses would be taxed in accordance with it.

Although the 2009 Guidance was a valid exercise of its powers, HMRC had failed to exercise its duty of fairness, which required it to balance the taxpayer's legitimate expectation arising from the 2003 Guidance and the unfairness caused by its withdrawal, against its duty to collect tax.

HMRC claimed that there had been no detrimental reliance by the taxpayer, but the Court said that HMRC should have considered:

- whether its action was fair as between taxpayers – HMRC had accepted similar claims for capital losses from many other taxpayers
- whether the 2009 Guidance was unfair because it was retrospective in its application and applied a new interpretation of the law to past disposals
- the fact that unfairness had arisen as a result of a mistake by HMRC which it had taken a considerable amount of time to rectify
- the length of the enquiries – closure notices had been issued 11 years after the claims had been submitted to HMRC.

Comment

This is an important decision in the context of public law and confirms that it is not necessary for a taxpayer to rely to his detriment on a published statement of HMRC, in order to be successful in an application for judicial review following the withdrawal, or disapplication, of that statement.

3. [2011] UKSC 47.

This case also illustrates the Courts' dislike of attempts by HMRC to resile from its own published guidance in circumstances where to do so is "conspicuously unfair".

The decision can be read here.

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Burgess: HMRC fails to discharge burden of proof in discovery assessment case

The following is taken from an article originally published in *Tax Journal* (4 December 2015, pp. 4-5, www.taxjournal.com).

In the recent case of *Burgess and Brimheath Developments Ltd v HMRC*[4], the UT confirmed that in appeals against discovery assessments (issued pursuant to section 29, TMA or paragraph 41, Schedule 18, Finance Act 1998 (FA 1998)), HMRC bears the burden of demonstrating that the assessments are valid, irrespective of whether the appellant has raised objections as to the validity of the assessments.

Background

Once the time limit for opening an enquiry has expired, or an enquiry is closed, the taxpayer's liability for the relevant tax year is generally regarded as final. In such circumstances, HMRC can only demand a further tax payment by issuing a discovery assessment pursuant to section 29 TMA, in relation to individuals and paragraph 41, Schedule 18, FA 1998, in relation to companies. As there are no material differences in the wording of the two provisions, for ease of reference, these provisions are referred to as the "discovery assessment provisions", throughout the remainder of this commentary.

A discovery assessment, as the name suggests, can only be made by HMRC in circumstances where it has made a "discovery" that tax has been underpaid in relation to a period where it is not open to HMRC to make an adjustment through the enquiry process. It is important to remember that the discovery assessment provisions can only be relied upon by HMRC in circumstances where:

- a loss of tax has been brought about by careless or deliberate conduct by the taxpayer (or a person acting on his behalf); or
- in circumstances where an HMRC officer could not reasonably be expected, on the basis of the information available to him at the end of his enquiries or expiry of the enquiry window, to be aware of the facts leading to the potential tax loss.

The underlying facts of *Burgess* are not important for present purposes. In the case of Mr Burgess, HMRC issued discovery assessments for income tax in relation to alleged failures to return profits of his business as a sole trader for the tax years 1996–97 to 1999–2000. In the case of Brimheath, the assessments related to corporation tax on alleged under-declarations of profits for the accounting periods ended 30 November in each of the years 1999 to 2008 (apart from 2000).

The taxpayers appealed against the discovery assessments to the FTT.

The FTT's decision

Before the FTT, the taxpayers' appeals were unsuccessful. The FTT found that in relation to both taxpayers, profits had been under declared and upheld HMRC's assessments to tax (with one exception, which is no important for present purposes).

The taxpayers appealed the FTT's decision to the UT.

4. [2015] UKUT 578 (TCC).

The UT's decision

Before the FTT, the validity of the discovery assessments did not form the basis of the taxpayers' appeals and the FTT made no findings in relation to whether the above tests had been satisfied, seemingly content to proceed on the basis that as the taxpayers had not raised the issue it was not necessary for it to satisfy itself that the discovery assessments were valid.

In the UT, the taxpayers did not challenge the FTT's substantive finding that they had under-declared their profits for the relevant periods, but contended that it had made errors of law in failing to consider the underlying validity of the discovery assessments. The focus of the appeal before the UT was therefore whether the FTT had properly considered whether the discovery assessments had been validly made.

The taxpayers argued that the FTT had made errors of law in failing to consider:

- whether the relevant conditions for the issue of an assessment under the discovery assessment provisions, namely, that the taxpayers' conduct had been deliberately fraudulent or careless, had been satisfied – the "competence" issue and
- whether the assessments were issued within the necessary statutory time period (section 36, TMA and paragraph 46, Schedule 18, FA 1988) – the "time limit" issue.

HMRC submitted that it understood, from the way the taxpayers had argued their case before the FTT, that only the underlying substantive issue required determination and there was no obligation on it to raise the competence and time limit issues. It argued that these issues were new points of law which had not been argued by the taxpayers before the FTT and as such they should not be allowed to raise them before the UT.

The UT was not impressed with HMRC's arguments and agreed with the taxpayers that HMRC had not discharged the burden of proving that in their case the conditions necessary for issuing a discovery assessment had been met (namely, that the tax loss had arisen from the taxpayers' deliberate conduct and that the assessments were therefore in time). In the view of the UT, this was a positive requirement of the legislation and it was not sufficient for HMRC to simply rely on the taxpayers' failure to raise validity objections in their appeals and to assume that validity issues had been conceded by the taxpayers. Appeals against discovery assessments do not require taxpayers to expressly object to the validity of the assessments. The UT concluded that given HMRC's failure, it was not open to the FTT to uphold the discovery assessments simply because it had been established that there were under-declared profits of the businesses. The FTT erred in not allowing the appeals because HMRC had failed to prove that the assessments were validly issued. The UT also refused to remit the matter to the FTT because to do so would give HMRC a "second bite of the cherry", which, in the view of the UT, would not be just and fair.

Comment

The UT confirmed that when considering an appeal against a discovery assessment, HMRC must establish before the FTT that the necessary conditions for issuing the discovery assessment were satisfied and that the assessment is therefore valid. The appeal cannot be dismissed simply because the FTT is satisfied that there has been an underpayment of tax.

Generally, in an appeal to the FTT, it is the appellant taxpayer who bears the burden of proof. He must prove his case, on the balance of probabilities, and demonstrate, for example, that an assessment is excessive. However, in relation to the validity of discovery assessments, the burden shifts and it is incumbent upon HMRC to prove, on the balance of probabilities, that the necessary circumstances existed to permit a discovery assessment to be made.

There are very good reasons for this. The discovery assessment provisions are designed to afford additional protection to the Crown beyond the ordinary statutory limitation periods. In cases of carelessness, the ordinary time limit of four years is extended to six years and in cases where the loss is brought about deliberately the period is extended to 20 years (sections 34 and 36, TMA). The ordinary limitation period is designed to provide certainty and finality to taxpayers. As mentioned above, once the time limit for opening an enquiry has expired, or an enquiry has been closed, the taxpayer's liability for the relevant year is generally regarded as final. However, as HMRC have the power to demand a further tax payment by issuing a discovery assessment, Parliament has provided that certain conditions must be satisfied before a discovery assessment can be issued. Such pre-conditions are designed to moderate the issue of discovery assessments and as it is HMRC who will be asserting that it is entitled to issue a discovery assessment, and that the necessary conditions are therefore satisfied, the burden of establishing that those conditions are satisfied, naturally falls on HMRC.

During the UT hearing, HMRC argued that it was not for it to argue a point which was not in issue before the FTT. The UT had little difficulty dismissing this argument. Citing *Phipson on Evidence*, the UT explained that if one party bears the burden of proof on an issue, but fails to plead a positive case on it, the other side has no obligation to argue against the point. If HMRC fails to plead, it will fail to discharge the burden.

HMRC had assumed that because the taxpayers had not advanced specific arguments on the validity of the discovery assessments the issue of validity did not need to be determined by the FTT. The UT was of the view that the validity of the assessments was an "essential element of HMRC's case" which needed to be positively proved by HMRC. By making no findings on whether HMRC had discharged the burden of proof regarding the validity of the assessments and yet still dismissing the taxpayers' appeals, the UT found that the FTT had made an error of law.

As HMRC had failed to argue the point, the UT refused to permit it to do so on appeal – following the long standing rule that new issues should not be introduced for the first time on appeal (barring exceptional circumstances which were not present in this case).

HMRC regularly seeks to use the discovery assessment provisions and a number of judicial decisions have reduced the substance of what amounts to a "discovery" to an almost meaningless level. What is required for there to be a "discovery" was succinctly expressed by the tribunal in *HMRC v Charlton*[5]:

"In our judgment, no new information, or fact or law, is required for there to be a discovery. All that is required is that it has newly appeared to an officer, acting honestly and reasonably, that there is an insufficiency in an assessment. That can be for any reason, including a change of view, change of opinion or correction of an oversight."

As a consequence of the wide meaning given to the word "discover" by the courts, in order for a discovery assessment to be found to be invalid, the focus tends to be on whether the taxpayer has acted with reasonable care and provided HMRC with sufficient information.

The UT's decision represents an important restatement of the legal position in relation to the burden of proof which operates where HMRC decides to issue a discovery assessment which is subsequently appealed.

The decision can be read here.

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5. [2013] STC 866.

Raftopoulou: Tribunal accepts reasonable excuse defence for late claim for repayment of tax

In *Raftopoulou v HMRC*[6], the UT has confirmed that a taxpayer can make a valid claim for repayment of overpaid tax, notwithstanding expiry of the statutory time limit for making such a claim, if the taxpayer has a reasonable excuse for late filing.

Background

Dr Raftopoulou (the taxpayer) submitted her 2006/07 self-assessment return on 14 January 2008. According to the return, a liability of about £18,000 arose. The taxpayer believed the amount of tax due was the result of a mistake. However, instead of amending her return under section 9ZA TMA, she made a repayment claim on 13 October 2011 under Schedule 1AB TMA. In a letter dated 9 November 2011, HMRC rejected her claim on the basis that it was out of time. The taxpayer appealed HMRC's decision to the FTT.

HMRC applied to the FTT to have the appeal struck out pursuant to Rule 8 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009, on the basis that the claim had been made out of time and was therefore not within the FTT's jurisdiction.

The FTT agreed with HMRC. Under the provisions of Schedule1AB TMA, the claim should have been made by 5 April 2011, but was not submitted until 13 October 2011. Accordingly, the FTT was of the view that in the absence of a statutory provision to extend or appeal against the time limit, the claim did not fall within its jurisdiction.

The taxpayer appealed to the UT.

The UT's decision

The taxpayer argued that the FTT had jurisdiction in respect of her appeal if she was able to show, by application of section 118(2) TMA, that she had a reasonable excuse for not having made the claim within the four-year time limit and that she had made the claim without unreasonable delay after the excuse had ceased.

Before the UT, the issues were, first, whether, in the circumstances of a claim under Schedule 1AB TMA, which had been made out of time, an appeal right could arise at all, and if it could, whether such a right had arisen in the present case. The parties accepted that for the FTT to have jurisdiction on an appeal under Schedule 1A, the following matters were required in the following sequence:

- a claim within the meaning of Schedule 1A
- an enquiry by HMRC into that claim
- a closure notice in respect of that enquiry and
- an appeal in time against the closure notice.

The second issue was whether section 118(2) TMA could have effect in relation to such a claim so as to permit a claimant, who had a reasonable excuse and who otherwise satisfied the conditions of section 118(2), to be treated as not having failed to make the claim on time, with the result that the claim was to be regarded as having been made within the statutory time limit.

The UT said that the taxpayer's letter to HMRC of 13 October 2011 could not constitute a claim in time and could not therefore constitute one under Schedule 1AB, unless section 118(2) applied with the effect that it was treated as having been made in time.

6. [2015] UKUT 579.

In the view of the UT, nothing on the face of section 118(2) indicated that the words "required to be done" should be limited to mandatory acts and must exclude voluntary ones. However, for an act to be valid there was a requirement that it be done by a certain time, or in a particular way. The UT concluded that section 118(2) could therefore apply to a claim made under Schedule 1AB.

The UT concluded that, if the taxpayer had a reasonable excuse for not filing her claim within the time limit and made the claim without unreasonable delay after the excuse had ceased, section 118(2) would deem her claim to have been filed within the relevant time limit so that the appeal could fall within Schedule 1A, and the FTT had jurisdiction to decide this issue.

Interestingly, referring to *Portland Gas Storage v CRC*[7], the UT noted that the opening and closing of an enquiry does not require any formalities. The legislation does not specify a minimum length of time between the opening and the closing of an enquiry. As a result, a single letter may constitute both the opening and the closing of an enquiry. This was the case with the letter sent by HMRC to the taxpayer informing her that her claim had been reviewed and rejected.

The UT allowed the taxpayer's appeal and remitted the case to the FTT.

Comment

This decision confirms that the opening and closing of an enquiry does not require any specific formality. What is important is the substance of what is communicated by HMRC to the taxpayer. One letter from HMRC can both open and close an enquiry. Depending on the circumstances, this may, or may not, be to the advantage of the taxpayer.

The decision can be read here.

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7. [2014] STC 2589.

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15581

Tower Bridge House
St Katharine's Way
London E1W 1AA
T +44 20 3060 6000

Temple Circus
Temple Way
Bristol BS1 6LW
T +44 20 3060 6000

11/F Three Exchange Square
8 Connaught Place
Central Hong Kong
T +852 2216 7000

8 Marina View #34-02A
Asia Square Tower 1
Singapore 018960
T +65 6818 5695

RPC