Field Court Tax Chambers

FCTC Digest

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EDITORIAL

Patrick C Soares

A warm welcome to the ninth edition of the *FCTC Digest*.

You have a treat in store.

The first article by the editor is about **purchasers who are receiving letters from brokers saying they have overpaid SDLT** on their recent property purchases and for a percentage fee they may be able to get the overpaid SDLT back. Why are the solicitors who acted in the purchases worried - read the article and all will be revealed!

A second article also by the editor looks at when lawyers and accountants should charge **VAT on providing tax and legal services to clients who are not resident (do not "belong") in the UK.** It also deals with the HMRC concessionary treatment where counsel is instructed by a UK solicitor and the fee is paid by the overseas client direct.

Patrick Way QC has done the third article on the 31st March 2021 HMRC statement setting out their

new practice in relation to payments by football clubs to agents acting for both club and player.

The old "50:50" split has gone and now detailed records will need to be kept to demonstrate the value of the benefit accruing to the club on the one hand and the footballer on the other.

Peter Vaines in his article "**Discovery Assessments The Level of Awareness"** brings us up to date on discovery assessments. Before examining a tax problem the practitioner *must* first see if HMRC are in time in making an assessment. This requires an understanding of the discovery powers of HMRC and this article brings practitioners up to date on the latest case law.

Katherine Bullock in her article "**One House or Two? The Relevance of Curtilage to the Main Residence Exemption"** warns us that HMRC are demonstrating an increasing tendency to check on CGT residence exemption situations: is the exemption really available? Katherine has done a leading article on situations where there may be two buildings which comprise a single dwellinghouse for the purposes of the exemption: if the taxpayer is in this situation the article is a must read.

The sixth article is the prize winning article of **Dilpreet K Dhanoa** on the critical line between tax avoidance and tax evasion entitled **"Tax 'Avoision' – Where do we Draw the Line."** It is a joy to read and makes us think about out subject. Peter Vaines adds some strident comments about the GAAR – what it is and what it could have been.

BROKERS' LETTERS AND SDLT REFUNDS

Patrick C Soares

INTRODUCTION

Purchasers are receiving letters from brokers claiming they can get an SDLT refund for the purchaser for a percentage fee and the solicitors who acted on the purchases are concerned.

There is set out below, taken from the tax press and the writer's own experience, some cases where this may be in point.

TEN CASES

1 Multiple dwellings relief (MDR) – annexe

MDR can be claimed where 2 or more separate dwellings have been purchased. An "annexe" or a granny flat or outbuildings may amount to separate dwellings. The Upper Tribunal give guidance in *Fiander v HMRC* and see also SDLTM00401.

2 Multiple dwellings relief (MDR) – future residential works

When land has been bought with planning permission to build houses, or there are permitted development rights for an existing building to be converted to flats, some brokers claim it is possible for MDR to be claimed even though physical work had not started by the date of completion of the purchase. See *Ladston Preston Ltd* (where the taxpayer has failed on this contention so far) which is being appealed and see SDLTM00400.If a block of flats is being built a successful contention in this area can result in a big SDLT savings.

3 Multiple dwellings relief (MDR) - MDR and mixed use property – no 3% surcharge

Where MDR is claimed for a "mixed use property" (i.e. a mixture of "residential property" and "non-residential property"), the 3% surcharge for additional properties should not apply

4 Mixed use treatment or non-residential property

The rates of SDLT for non-residential or mixed use property are generally lower than for residential property, with the difference being more pronounced for higher value properties, or where the 3% extra SDLT would apply to a residential purchase.

5 Mixed use – communal gardens

It seems that some brokers obtain details of properties sold with a right to use a communal garden and buyers are contacted and told a refund might be due. The tribunal in *Khatoun* did not accept that argument.

6 Mixed use – some non-residential feature

Another angle taken by brokers is that there is something about the property which means the property is not wholly residential, such as: there is an overflying electricity cable. These arguments are not easy to sustain (SDLTM00440 and *Hyman Pensfold and Goodfellow*).

7 Non-residential – derelict building

A building which is so derelict as not to be "suitable for use as a dwelling" might benefit from the lower rates of SDLT applicable to non-residential property. This follows a Tribunal decision in the ***P***

N Bewley Ltd case. See also SDLTM00385 and *Fish Homes Ltd*.

8 Fixtures and fittings

There may be some scope for reducing the SDLT charge in appropriate cases.

9 Multiple flat purchases

If a taxpayer buys one flat no reliefs are available but if he buys six or more it is treated as a commercial building purchase and the maximum SDLT is 5% even in the case of a non-UK resident purchaser where the SDLT can otherwise be as high as 17%.

10 Freeports

This has only just been added to the list!

The Finance Act 2021 introduced a number of tax incentives to build new Freeport sites in England, including stamp duty land tax (SDLT) relief on certain land purchases.

The relief will be available for transactions involving 'Qualifying Freeport land' with an effective date between the date a Freeport site is formally designated and 30 September 2026. Qualifying Freeport land means land that is situated in a designated Freeport tax site and which is purchased with the intention that it will be used in a 'qualifying manner'.

For these purposes 'qualifying manner' means that the land must be used, developed, redeveloped or exploited by the purchaser, or a connected person, in the course of a commercial trade or profession.

What land is excluded from the relief?

- Land used as a dwelling or as the gardens or grounds to a dwelling
- Purchases of land to be developed or re-developed to become residential property
- Any land held as stock of the business for resale without development or redevelopment
- Land that is exploited as a source of rents payable by a person using the land as a dwelling

CONCLUSION

It is clearly important for solicitors to ensure they give the correct SDLT advice.

Brokers are writing to purchasers offering to get SDLT refunds for them.

Warning to estate agents

Often the estate agent's particulars will influence a tribunal and agents must take care in how they describe properties.

VAT AND THE SUPPLY OF INTERNATIONAL LEGAL AND TAX SERVICES

Patrick C Soares

INTRODUCTION

This article looks at the VAT position on the supply of international legal and tax services by lawyers and accountants who belong in the UK.

The principal legislation is in VATA 1994 s7A and Schedule 4A.

The HMRC guidance is in VAT Notice 741A (the notice).

The position can be broken down into a number of rules.

RULE I – SUPPLIES OF SERVICES MADE IN THE UK ARE GENERALLY VATABLE AT THE POSITIVE RATE OF 20%

VAT is chargeable on the supply of services provided the services are made in the UK (VATA 1994 s1(1)).

The general rule is the place of the supply of a service is determined by the place where the parties belong.

VATA 1994 s7A(2) and (4) provides thus:

> 7APlace of supply of services
>
> .....
>
> (2) A supply of services is to be treated as made—
>
> (a) in a case in which the person to whom the services are supplied is a relevant business person, in the country in which the recipient belongs, and
>
> (b) otherwise, in the country in which the supplier belongs.
>
> ....
>
> (4) For the purposes of this Act a person is a relevant business person in relation to a supply of services if—

(a) the person carries on a business, and

(b) the services are not received by the person wholly for private purposes,

whether or not the services are received in the course of business.

9 Place where supplier or recipient of services belongs.

(1) This section has effect for determining for the purposes of section 7A (or Schedule 4A).... in relation to any supply of services, whether a person who is the supplier or recipient belongs in one country or another.

(2) A person who is a relevant business person is to be treated as belonging in the relevant country.

(3) In subsection (2) “the relevant country” means—

(a) if the person has a business establishment, or some other fixed establishment, in a country (and none in any other country), that country,

(b) if the person has a business establishment, or some other fixed establishment or establishments, in more than one country, the country in which the relevant establishment is, and

(c) otherwise, the country in which the person's usual place of residence or permanent address is.

(4) In subsection (3)(b) “relevant establishment” means whichever of the person's business establishment, or other fixed establishments, is most directly concerned with the supply.

(5) A person who is not a relevant business person is to be treated as belonging—

(a) in the country in which the person's usual place of residence or permanent address is (except in the case of a body corporate or other legal person);

(b) in the case of a body corporate or other legal person, in the country in which the place where it is established is.

Examples

If a UK relevant business person (X) supplies services to a non-relevant business person (a client for private use) in France the supply is treated as made in the UK and thus VAT on the face of it is chargeable. HMRC call these “Business to Client” cases (B2C) (see para 2.4 of the notice). This general rule (Rule I) is subject to Rule II and Rule VI. Thus if a UK lawyer charges a Dublin lay client for tax services he would not charge VAT and can reclaim any input VAT as the situation comes within Rule II and Rule VI below and the general rule in Rule I is displaced.

If X supplies the services to a relevant business person in France the supply is treated as made in France. HMRC call these Business to Business cases (B2B) (see para 2.4 of the notice). Thus if a UK lawyer charges a Dublin business client a fee for tax services he would not charge VAT and can reclaim any input VAT. This is because the supply is made outside the UK within s7A(2)(a) and the input tax reclaim is not restricted because of s26(2)(b) (Rule II).

If a non-relevant business person in the UK makes “supplies” to a relevant business person in France or a non-relevant business person in France VAT is not in issue. Thus C2B and C2C cases have no relevance to VAT as there will be no taxable supplies.

A relevant business person is someone who is registered for VAT in their jurisdiction or is in business outside the UK. A non-relevant business person is the ultimate consumer who does not use the supply for business purposes.

How does one tell one from the other?

Para 6.3B2B provides thus:

6.3 B2B supplies

The B2B general rule for supplies of services is that the supply is made where the customer belongs.

Where the B2B rule applies you should obtain commercial evidence showing that your

> customer is in business and belongs outside the UK. For EU customers their VAT registration numbers is the best evidence that your EU customer is in business. If your customer is unable to provide a VAT number you can accept alternative evidence. This includes certificates from fiscal authorities or other commercial documents indicating the nature of the customer's activities in their home country. Such evidence should be kept as part of your records.
>
> Where a customer is unable to provide a VAT number, or other evidence to clearly demonstrate business activities, the supply should be treated as a B2C transaction.

One can see from the examples above of a lawyer giving tax advice the distinction between B2C and B2B is not of great significance in such cases as far as the UK tax position is concerned.

RULE II – RECLAIM INPUT TAX

A taxable person can reclaim input tax and does not charge output tax if it makes "supplies outside the

UK which would be taxable if made in the United Kingdom" (s26(2)(b)).

These s26(2)(b) supplies are not zero rated supplies as such (s30) but they have the same effect

RULE III – AGENCY AND REIMBURSEMENT

Where services are supplied through an agent who acts in his own name HMRC may treat the supply as a supply to the agent and as a supply by the agent (s47(3)).

The implication is a supply to an agent of X is a supply to X.

Also, if a supply is made by S to P and this is reimbursed by C, HMRC can treat the supply as being made by S to C if certain conditions are fulfilled.

RULE IV – SPECIAL SCHEMES AND CONCESSIONS

HMRC may agree particular arrangements or give concessions.

If UK counsel supplies services to a UK solicitor then counsel in the normal case must charge VAT as the supply is to the solicitor and the solicitor can claim back the VAT depending on the nature of the onward supply made by the solicitor. If the onward supply is to an overseas client within Rule II above and Rule IV below the solicitor does not charge the overseas client VAT and can reclaim the VAT on counsel's fees.

HMRC have a concessionary practice whereby counsel can bill the solicitor and not charge VAT and the solicitor confirms on the invoice that the client does not belong in the United Kingdom and the supplies are within VATA 1994 s26(2)(b) or the like.

If the onward supply to the client by the solicitor will have been at the positive rate (i.e. the client belongs in the UK) the concession will still apply to cut the solicitor out of the VAT supply chain. Note HMRC consider the situation to be a concessionary one but it may be possible for the taxpayer if needs be to bring the situation within Rule III.

The concession reads thus:Confirmation and review of VAT concessionary treatment for counsel’s fees

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The Law Society reports that HMRC has confirmed that an existing VAT concession for counsel’s fees remains in place at present but is under review.

The concessionary treatment for counsel's fees paid into and kept in a client account was agreed between the Bar Council and the Law Society at the time VAT was first introduced. The concession allows solicitors to treat counsel’s advice as supplied directly to their clients and the settlement of the fee as a disbursement, meaning that the client may recover the VAT on counsel’s fees, and the solicitor does not need to keep any VAT record of it.

The Law Society reports that HMRC has recently confirmed that the concession still currently stands, but that HMRC is reviewing the concession to consider whether it should be withdrawn.

If the concession is withdrawn, HMRC has confirmed that it would do so prospectively, with appropriate advance notice given.

The Law Society is inviting solicitors to respond, by 30 September 2021, with information on the extent and ways in which the concession is being used and its benefits or deficiencies, so that the Law Society may provide this evidence to HMRC to inform its review.

See *De Voil Indirect Tax Service*:V1.239

Source:Confirmation and review of VAT concessionary treatment for counsel's fees – share your experiences

RULE V – SERVICES RELATING TO LAND IN THE UK

If a service relates to UK land then the supply is treated as made in the UK. VAT at the positive rate must be charged (as the supply is made in the UK) and the input tax charged to the supplier can be reclaimed. The supply is not zero rated and is not within Rule II above. These special provisions are found in VATA 1994 Schedule 4A and they override Rule II; Rule I thus applies and VAT at the positive rate (20%) is chargeable.

This head applies to:

> (a) the grant, assignment or surrender of any interest in or right over land,
>
> (b) the grant, assignment or surrender of a personal right to call for or be granted any interest in or right over land,
>
> (c) the grant, assignment or surrender of a licence to occupy land or any other contractual right exercisable over or in relation to land (including the provision of holiday accommodation, seasonal pitches for caravans and facilities at caravan parks for persons for whom such pitches are provided and pitches for tents and camping facilities),

(d) the provision in an hotel, inn, boarding house or similar establishment of sleeping accommodation or of accommodation in rooms which are provided in conjunction with sleeping accommodation or for the purpose of a supply of catering,

(e) any works of construction, demolition, conversion, reconstruction, alteration, enlargement, repair or maintenance of a building or civil engineering work, and

(f) services such as are supplied by estate agents, auctioneers, architects, surveyors, engineers and others involved in matters relating to land.

The rule applies only to services which relate directly to a specific site of land or buildings (*Heger Rudi v Finazamt* [2008] STC 2679).

Notice 7.3 – 7.5 gives the following examples.

7.4 Examples of land related services Examples of services that are land related include:

- ....
- arranging the sale or lease of land or property
- .....
- legal services such as conveyancing and drawing up of contracts of sale or leases, including title searches and other due diligence on a specific property

7.5 Examples of services only indirectly related to land

Examples of services that are not directly land related include:

- .....
- accountancy or tax advice, even when that relates to tax on rental income
- ....
- general legal advice on contractual terms

Example

A firm of solicitors which belong in the UK act for a Hong Kong client on the purchase of a London flat. VAT is chargeable on their fees.

RULE VI – SPECIAL CASES WHERE NO VAT IS CHARGEABLE ON THE OUTPUT BUT THE INPUT TAX CAN BE RECLAIMED – THE HALCYON LIST

If the recipient of the services is not a relevant business person and does not belong in the UK or the IOM the services if they fall under this head are treated as made in the county where the recipient belongs. The situation will fall within Rule II.

This head covers (*amongst others*) :

> (d) services of consultants, engineers, consultancy bureaux, lawyers, accountants, and similar services, data processing and provision of information, other than any services relating to land,

This is the halcyon head – no output tax is charged but the input tax referable to the supply can be reclaimed. This is sometimes called "the consultancy" head.

Example

An accountant who belongs in the UK gives tax advice to a lay client in Jersey. He does not charge VAT and he can reclaim any input tax referable thereto (e.g. if he has paid counsel's fee with respect thereto).

If the supply of services does not fall within this head then Rule I applies and the supply is vatable as being made by a supplier who belongs in the UK to a non-business client (*Gray & Farrar* [2019] UKFTT 684(TC)).

The notice in para 12.6 states the category does not include the "services of lawyers, surveyors and consultants *where these directly relate to a specific piece of land or property*."

CONCLUSION

One must start with the assumption that all supplies are vatable at the positive rate.

That remains the position with regards to services directly related to UK land.

With regards to the giving of tax advice to a lay client who belongs outside the UK the supply is deemed to be made outside the UK (so no VAT is chargeable) but the input tax can be reclaimed under s26(2)(b) and Sched 4A para 16(2)(d). In the case of a supply to another taxable business person outside the UK the result is the same albeit the result is achieved by a different route (s26(2)(b) and s7A(2)(a)): thus no VAT charged but any input tax can be reclaimed.

The HMRC concession with regards to counsel's fees should be noted.

The zero rating head has little significance in this area (s30 and Schedule 8).

FOOTBALL AND PAYMENTS TO AGENTS

Patrick Way QC

Speed read

On 31st March 2021 HMRC announced their new practice in relation to payments by football clubs to agents acting for both club and player ("dual representation").

The old "50:50" split has gone and now detailed records will need to be kept to demonstrate the value of the benefit accruing to the club on the one hand and the footballer on the other. The footballer will (as before) be taxed on the deemed earnings he receives when the club pays the agent for services held to be provided to him.

The definition of earnings is found at ITEPA 2003 s.62 and it includes:

> "any gratuity or other profit or incidental benefit obtained by the employee if it is money or money's worth or anything else that constitutes an emolument of the employment."

As we all know, the definition of “money’s worth” means something that is of direct monetary value to the employee.

It can be seen therefore that when a football agent negotiates the transfer of a player to a club and is paid by the club, the services provided by the agent may be said to be both for the benefit of the club on the one hand and the player on the other.

Until 31st March 2021 HMRC, broadly speaking, accepted that in these circumstances the appropriate split was 50:50: the club and the player were each said to have received half the benefit of the agent’s services and the player was therefore obliged to pay tax as if he had received earnings equivalent to half the agent’s fee. This practice could be “ignored” in certain circumstances. For example, if it could be demonstrated that more than half of the benefit of the agent’s services accrued to the club, rather than the player, then it might be possible to reduce the 50% deemed earnings, accruing to the player, to a lower amount. This was unusual and relied on good evidence being supplied.

The new practice is found in the employment income manual at EIM01150 to EIM01152.

In a nutshell, in cases of dual representation (which, after all, is what we are talking about) the 50:50 split is replaced by a split which must be justified by reference to the actual services provided to each of the club and the player.

HMRC now require that the club should retain documentation to show the reasoning behind the split and they suggest that this should include meeting notes, e-mails, details of time spent and other documentation to substantiate its payments. In each case HMRC is looking for some sort of evidence and commercial justification for the split which is arrived at.

At EIM01152 HMRC suggest the sort of records that should be kept by the club, the agent and the player and these are as follows:-

> HMRC suggest that the club keeps records covering:
>
> - the specific reasons for engaging an agent for the specific transaction;
> - contemporaneous evidence of the engagement of the agent, the

instructions given, and the level of fee discussed;

- contemporaneous evidence of the work done for the club services;
- evidence to support any variation of the fees shown in the player/agent representation agreement and the subsequent tri-partite agreement.

As far as the agent is concerned the following records might be kept:

- contemporaneous evidence of their engagement by the club, the instructions given, and the level of fee discussed;
- contemporaneous evidence of the work done for the club;
- contemporaneous evidence of the work done for the player;
- evidence to support the basis of any split in the agent's fee paid between club and player services;

- evidence to support any variation of the fees shown in the player/agent representation agreement and the subsequent tri-partite agreement.

So far as the player is concerned the following records may be kept:

- discussions held with the agent during the transfer or contract negotiations;

- their understanding of any conversation resulting in their agent being engaged by the club as well as them.

One can see that this new practice is not without its difficulties. The two transfer windows in the summer and January are relatively small and an enormous number of transfers take place at the very last minute. So for detailed records of this nature to be kept may be difficult.

For what it is worth, HMRC's "new approach" would seem to me to be justified by reference to the legislation and the key is definitely going to be to decide at the outset for whom the agent is acting and to agree, on a commercial and sensible basis, how the agent's fees in each case should be split.

Given that an agent may typically take 5% to 10% of the player's salary, each year, by way of his fee and given the enormous increase in the amount that top footballers are paid one can see that footballers will need to be very carefully advised, before transfers are effected, as to the likely impact on their net remuneration. Equally, players who are paid relatively small amounts but "benefit" from large fees of an agent should be particularly careful: there are situations where the tax on the fee of the agent to which the player becomes liable may represent a very large proportion of their monthly income.

DISCOVERY ASSESSMENTS

The Level of Awareness

Peter Vaines

The Supreme Court in *HMRC v Tooth [2021] UKSC 13* provided some welcome clarity on the subject of discovery assessments where they confirmed that discovery assessments can never be regarded as stale if they are raised within the statutory time limit. Further definitive guidance would also be welcome because confusion exists with many other aspects of the legislation regarding discovery assessments.

One particularly difficult area is the amount of information which has to be provided to HMRC for them to be sufficiently aware of the possibility of an underpayment of tax. If the tax officer is provided with sufficient information, then the period for raising an assessment is strictly limited.

We have had two recent cases heard by the Upper Tribunal in which the level of awareness was examined.

The first case was *Good v HMRC [2021] UKUT 0281*, where the Upper Tribunal gave detailed consideration to section 29(5) TMA 1970. The precise words of section 29(5) are important:

> "The officer could not have been reasonably expected on the basis of the information made available to him before that time to be aware of the situation mentioned in sub-section 1 above". (*That is to say, an insufficiency of tax*).

This test is supplemented by sub-section 6 which includes:

> "It is information the existence of which and the relevance of which as regards the situation in sub-section 1 above could reasonably be expected to be **inferred** by an officer of the Board from information falling within paragraphs (a) to (c) above or

are notified in writing by the taxpayer to an officer of the board".

I have highlighted the reference to "inferred" for reasons which will become clear.

This ability to infer was considered by the Upper Tribunal in *HMRC v Charlton [2012] UK UT 770* where the taxpayer disclosed to HMRC the form AAG1 in his tax return setting out the detailed arrangements relating to a tax avoidance scheme. The Upper Tribunal said:

> "We are, however, in no doubt that first the existence of the form AAG1 could reasonably have been expected to have been inferred by the hypothetical officer and secondly, that the physical separation of the SRN [*Scheme Reference Number*] number from other relevant entries on the tax return would not have prevented an officer from making the necessary link

> between them so as reasonably to infer the relevance of the form AAG1 to the insufficiency.
>
> The circumstances of the form AAG1 in our view make it reasonable for its existence and relevance to be inferred.
>
> In our view the form AAG1 is just the sort of information the availability and relevance of which might reasonably be inferred from the inclusion of the SRN in a return which also discloses tax effects consistent with tax planning".

These extracts (there are more) make a pretty strong statement of the position when a form AAG1 is disclosed to HMRC with the tax return. It is therefore rather a surprise that the First Tier Tribunal in *Good* decided that a completed AAG1 form and the relevant DOTAS number which had been disclosed on the tax returns was not enough for the officer to reasonably aware of the insufficiency.

It is even more surprising that the Upper Tribunal concluded that the FTT made no error of law in its approach and did not misdirect itself as to the applicable principles.

The taxpayer argued that submission of the form AAG1 made it reasonable for the information and its relevance to be inferred by the officer (exactly as had been held in *Charlton*) but the Upper Tribunal rejected this argument.

It seems that the inference permitted by Section 29(6) and the significance of a form AAG1 may not as strong as suggested in *Charlton*. Maybe we have a new yardstick – or maybe we don't.

The second decision of the Upper Tribunal was the Stamp Duty Land Tax case of *Victoria Carter and Peter Kennedy v HMRC [2021] UKUT 0300*.

SDLT has its own legislative framework but the relevant element here is the same. For SDLT purposes, the power of HMRC to make a discovery assessment where a taxpayer has filed a timely return, is found in Schedule 10(30) Finance Act 2003. This provides (in very similar terms to section 29(5) TMA 1970) that an assessment can be made if at the relevant time:

> "[HMRC] could not have been reasonably expected on the basis of the information made available to them before that time, to be aware of the situation mentioned in paragraph 28…"

This case also raises some difficult issues.

It was common ground that the following principles applied:

(1) The issue was whether on the basis of the information provided, a hypothetical officer could not have been reasonably expected to be aware of the insufficiency.

(2) The general principle set out in *Langham v Veltema [2004] EWCA Civ 193* that HMRC is only to be prevented from making a discovery assessment where the taxpayer "in making an honest and accurate return…[has] clearly alerted

HMRC to the insufficiency of the assessment”.

(Pausing there for a moment, and recognizing that this is a decision of the Court of Appeal I would very respectfully suggest that this is an impossible test. If a taxpayer makes an honest and accurate return believing that his return is correct and accurate, he could not possibly be expected (indeed it would be absurd) for him to alert HMRC that his self-assessment is insufficient. The whole premise upon which he has submitted his honest and accurate return is that it is complete and accurate and not insufficient. So such a taxpayer could never be protected from the issue of a discovery assessment. In other words, HMRC is only to be prevented from making a discovery assessment where something happens which is impossible.

Conversely, if the taxpayer knows that his self-assessment is insufficient and fails to alert HMRC to that insufficiency, then HMRC do not need to worry about any of this; they have all the powers they need because this would be careless conduct and they would have six years in which to issue an assessment.

For these reasons, it is respectfully suggested that the test – or at least this phrase in the judgment of the Court of Appeal – should be interpreted in a different manner, or possibly restricted to a particular set of circumstances. As it stands, this formulation renders the information awareness test completely redundant).

(3) The information provided to the hypothetical officer must be sufficient to make him aware of the actual insufficiency at a level which would justify the making of an assessment. The information need not be sufficient to enable HMRC to prove its case.

(4) The hypothetical officer should be treated as being of general competence, knowledge or skill which includes a reasonable knowledge and understanding of the law. In determining the accuracy of the disclosure, it can be assumed that the hypothetical officer will apply his or her knowledge of the law to the facts disclosed and to form a view as to whether or not an insufficiency exists.

In the case of *Carter/ Kennedy*, the taxpayer entered into a tax scheme and provided details in a disclosure note. In the disclosure note the taxpayer explained the transaction, including the provisions upon which it relied, and also specified that they did not consider Section 75A FA 2003 applied to the transaction.

The FTT said that in considering the adequacy of the disclosure made by the taxpayer, an assessment has to be made of the conclusions that it is reasonable to expect HMRC officers to draw from that information. They accepted the evidence of the HMRC officer involved that before the relevant date "there was considerable debate within HMRC as to whether Section 75A FA 2003 could be applied to counteract these schemes". (This clearly acknowledges that HMRC were fully aware of the scheme).

The FTT went on to say that they would expect a hypothetical officer of general competence, knowledge or skill to be aware of Section 75A and its potential application to counteract tax avoidance scheme.

However, they said that until the officer (the real officer) had received advice from Counsel, neither he nor HMRC generally had come to a settled view about whether Section 75A could apply to counteract this type of transaction.

This brings in a whole new dimension to the awareness issue. The suggestion here is that even though HMRC may have all the information that they need to be aware of the transaction and its implications, they should not be regarded as being aware of a possible insufficiency until they had received Counsel's opinion on whether the scheme worked or not.

I would respectfully suggest that this must surely be the wrong test. As the FTT noted, the hypothetical officer is not required to resolve all issues or every question of law or to have enough to enable HMRC to prove that their view is right. The test is simply whether the information available would justify him in raising an assessment, even though the tax cannot be precisely quantified.

Many would feel that these circumstances justified the issue of a discovery assessment. Indeed, many will have had experience of discovery assessments being issued on much weaker grounds than this.

The whole point of the available awareness test is to see whether HMRC has been given sufficient information from which they can make the relevant judgment. If the rule is that HMRC are not considered to have had sufficient information until such time as they actually get round to making that judgment, then the time limit provided by Section 29(5) does not really exist. Can it really be right to say that if they fail to give adequate consideration to the matter before the expiration of the time limit, they are then allowed four years in which to do so.

The issue relating to Section 75A is also interesting. The taxpayer said they had considered Section 75A and had been advised that it did not apply. Section 75A is a complex anti-avoidance provision involving other hypothetical situations. The FTT criticised the disclosure note as not containing any indication that the transactions involved part of a pre-planned tax avoidance scheme and there was no technical explanation as to why Section 75A was considered not to apply

It is a harsh criticism of the taxpayer for failing to tell HMRC that they have entered into a tax avoidance scheme when the taxpayer specifically highlighted that they have considered section 75A (which is headed "anti avoidance") and had explained that in their view it does not apply. It is tempting to enquire whether it is necessary to specify (with grounds) all the provisions of the Tax Acts which the taxpayer considers do not apply. That would take a tree or two.

In conclusion, the Upper Tribunal decided that the FTT were entitled to reach their conclusions and the appeal was dismissed.

There may be many reasons why in this particular case HMRC may not have been sufficiently aware to enable them to raise a discovery assessment. However this is not an obvious conclusion when a tax avoidance scheme known to HMRC is flagged by the taxpayer in his tax return.

Section 29(5) TMA 1970 and Schedule 10 FA 2003 are an important part of the taxpayer's safeguards under self-assessment and the importance which is given to finality. If the reasoning in these cases remains unchallenged, they reveal that in reality, the legislation provides the taxpayer with precious few genuine safeguards against the issue of a discovery assessment outside the statutory time limit - and he (and we) might as well get used to it.

ONE HOUSE OR TWO? THE RELEVANCE OF CURTILAGE TO THE MAIN RESIDENCE EXEMPTION

Katherine Bullock

HMRC are demonstrating an increasing tendency to challenge taxpayers who submit their tax returns on the basis that a gain is covered by the main residence exemption. Challenge is even more likely where the part disposed of is a self-contained house in its own right. A single dwelling house may comprise a number of buildings just as a single building may contain a number of dwellings. However the plot thickens when a dwelling house comprises several buildings each of which can function as a separate dwelling. In this scenario of two fully functioning dwellings comprising a single dwelling-house, can one be sold tax-free? What exactly is part of a dwelling-house?

Roger Crippin v HMRC [2021] UKFTT 0351 (TC): **Whether or not a building is a dwelling-house used as a residence is a question of fact and degree. It is necessary to look at all the circumstances in the round.**

The First Tier Tribunal considered this question once again in the recent case of *Crippin*. In January 2013, Mr Crippin sold a property, Benko, to his partner, Ms McKean. Mr Crippin claimed that Benko was ancillary to the main house, Loaningdale, where he and Ms McKean lived with their four children. As a result, he argued, he was entitled to relief from CGT under s223 TCGA 1992 as he had made a part disposal of a dwelling-house occupied as his only or main residence. HMRC disagreed.

Mr Crippin acquired Loaningdale and Benko together as a family home. He constructed a double garage attached to Benko and remodelled the building to contain a three bedroom flat with a kitchen/living area. Access was via a separate entrance or a shared first floor balcony. The buildings were very close together and Benko did not have separate utilities (although the sales particulars suggested that it did). From its remodelling, Benko was occupied by friends of friends, who paid a contribution to the overheads of the accommodation. There was no formal tenancy arrangement and Mr Crippin and his family still had unrestricted access to Benko, stored their belongings there and used it for guest accommodation when the friends were away.

Benko was retrospectively recategorized as independent flatted accommodation as it could be distinguished from “the typical ‘granny flat’ or other types of ancillary accommodation that are commonly dependent on the main house for essential services”. Benko was a fully independent property and from construction to disposal was never available exclusively to the family for their use.

The issue under consideration by the FTT was whether Benko, which was appurtenant to and within the curtilage of Loaningdale, was part of the dwelling-house occupied as Mr Crippin’s main residence. Sadly the judgement does not set out why Benko was within the curtilage or appurtenant to Loaningdale. The FTT agreed that Benko was a dwelling-house in its own right and separate from Loaningdale, although the separate connection of utilities was not determinative. However this did not prevent it from being part of an entity that constituted Mr Crippin’s residence for the purposes of s.222. The FTT considered it particularly important that there was no formal arrangement with the friends, that Mr Crippin’s family continued to keep belongings there and had unfettered access and use to the property developed within the curtilage of the main residence.

So does this mean that if you develop a second property in close proximity to your main residence and let it informally, you can sell that property free of CGT? As always, it is a question of fact and degree.

TCGA 1992 s222: the disposal of part of a dwelling-house

TCGA 1992 section 223 provides that no part of a gain to which section 222 applies shall be subject to capital gains tax ("CGT"), if the dwelling-house or part of a dwelling-house has been the individual's only or main residence throughout the required period of ownership.

TCGA 1992 section 222 applies to a gain accruing to an individual so far as attributable to the disposal of, or of an interest in, a dwelling-house or part of a dwelling-house which is or, has at any time in the period of ownership been, the taxpayer's only or main residence.

Dwelling-house and residence are not defined in the legislation. Therefore, as HMRC wisely say in their guidance at CG64320, "when considering the question of what makes up the entity of the dwelling-house, we are guided by the principles laid down in case law”.

Batey v Wakefield **[1981] STC 521: A dwelling-house can consist of more than one building even if the other building itself constitutes a separate dwelling-house (the entity test).**

The taxpayer built a four bedroom house within 1.1 acres of land. As he worked away from home, he employed a caretaker and a housekeeper to look after the house. He also built a bungalow which they occupied, which had its own access and was the width of a tennis court from the main house, separated by an established yew hedge. He sold the bungalow with 0.15 acres of land and argued it was exempt from CGT as part of the dwelling house which he occupied as his main residence. The Commissioners, the Chancery Division and the Court of Appeal all agreed.

What has to be identified is the identity of the dwelling-house. Per Browne-Wilkinson J: “That dwelling-house may or may not be comprised in one physical building; it may comprise a number of different buildings. His dwelling-house and residence consists of all those buildings which are part and parcel of the whole. Each part being appurtenant to and occupied for the purpose of the residence.” The bungalow was occupied by the taxpayer through his employee, who was employed for the purpose of promoting the taxpayer’s reasonable enjoyment of his own residence. “In those circumstances, bearing in mind the fact that the buildings are very closely adjacent, it seems to me proper to find that the lodge was part of the residence of the taxpayer”

A dwelling-house can therefore include several buildings which are used as dwellings but still distinctly separated from each other eg one building with living accommodation and another with sleeping accommodation and bathroom facilities. It can include another person’s dwelling-house if the use of that person’s dwelling-house was to serve the main house as a residence eg staff accommodation.

How fine the line is in applying this test can be seen in *Green v IRC* [1982] BTC 378 where the Inner House of the Court of Session in Scotland held that two wings of a mansion closely adjacent and occupied for the purposes of main house, one wing by the gardener and the other mostly vacant as the house was too large for the taxpayer, were not part of the main house. The house and its wings were separate rateable units. Each had own entrance although connected at basement level. The court held that "where there are buildings, such as the mansion house and the wings here, within a common curtilage and single ownership, and capable of being regarded as separate to some extent, what has to be determined is the identity of the taxpayer's residence." This was a matter of degree.

***Lewis v Lady Rook* [1992] STC 171: no building can form part of a dwelling-house which includes a main house, unless that building is appurtenant to, and within the curtilage of, the main house (the curtilage test).**

Here the 10 acre estate included a semi-detached cottage 175m from the main house with its own road access. It was separately rated and occupied by the gardener. The cottage was sold and main residence relief claimed. In finding that the cottage was not part of the taxpayer's dwelling-house, the Court of Appeal held that although a dwelling house could consist of more than one building, even if the other was itself a separate dwelling-house, “what one is looking for is an entity which can be sensibly described as a dwelling-house though split up into different buildings performing different functions” (quoting with approval Vinelott J in *Williams v. Merrylees* ([1987] 60 TC 308). However, trying to identify the entity by identifying the taxpayer’s residence led to confusion as with a small estate it was easy to consider the estate the residence and all the buildings part of the residence. Accordingly, no building can form part of a dwelling-house which includes a main house, unless that building is appurtenant to, and within the curtilage of, the main house.

The right test was “Was the cottage within the curtilage of, and appurtenant to, [the main house] so as to be a part of the entity which together with [the main house] constituted the dwelling-house occupied by the taxpayer as her residence?” In Lady Rook’s case, the distance, degree of separation and size of estate meant that it was not.

***Methuen Campbell v. Walters* [1979] Q.B. 525: For one corporeal hereditament to fall**

within the curtilage of another, the former must be so intimately associated with the latter as to lead to the conclusion that the former in truth forms part and parcel of the latter.

Like dwelling-house and residence, there is no statutory definition of curtilage. The Shorter Oxford Dictionary defines curtilage as “a small court, yard or piece of ground attached to a dwelling house and forming one enclosure with it”. This definition was adopted in *Methuen-Campbell*, a Leasehold Reform Act case, cited with approval by the Court of Appeal in *Lady Rook* and again in *Dyer v Dorset County Council* [1989] 1QB 346, a leading non-tax case on meaning of curtilage. It was further held that more dispersed groups of buildings can be within a single curtilage if they are so intimately associated as to lead to the conclusion that one forms part and parcel of the other.

Curtilage therefore appears to require smallness of area, proximity and some form of attachment. HMRC’s view at CG6425 is that there should be no separation by a wall or fence. Similarly, a public road or stretch of tidal water will limit the curtilage of the building. Thus buildings standing around a courtyard together with the main house will be within the curtilage of the main house. Buildings which are within the curtilage and appurtenant to a main house will pass automatically on a conveyance of that house without having to be specifically mentioned, although it is worth noting that the conveyancing requirement is not one that is clear from the case law.

***Secretary of State for the Environment, Transport and the Regions v Skerritts of Nottingham Ltd* [2003] 3 WLR 511: It is not the case that the curtilage of a building must always be small or that the notion of smallness is inherent in the expression.**

This case, which was an appeal against a listed building enforcement notice and considered whether a stable block was part of the curtilage of the main house, was cited by the First Tier Tribunal in *Ritchie & Ritchie v HMRC*. In essence, Robert Walker LJ noted that small was relative to the type of building under consideration and the density of housing. Curtilage is not, in the judge's view, a term of art. It is a question of fact and degree.

In *R v Blackbushe Airport* [2021] EWCA 398, where the issue was whether an airfield, including runways, taxiways and a fuel depot, was within the curtilage of the airport terminal building, the relevant authorities, including *Methuen-Campbell,* were considered again by the Court of Appeal. The Court concluded that the correct test for deciding whether land was within the curtilage of a building was the *Methuen-Campbell* "part and parcel" test. The correct question is whether the land falls within the curtilage of the building, and not whether the land together with the building fall within, or comprise, a unit devoted to the same or equivalent function or purpose. Andrews LJ also noted that "although the size of the land will be a relevant consideration, the extent of the curtilage of a building may vary with the nature and size of the building. To refer to the area as 'small' (or conversely 'large') is not particularly helpful in a context where size is relative. What falls within the curtilage of a manor house, or a large industrial mill, or a factory, may not be the same as what falls within the curtilage of a dwelling house."

A similar point was made in *Markey v Sanders* [1987] STC 256 by Walton LJ: "what would be 'very closely adjacent' were one dealing with the sale of No. 7 Paradise Avenue, Hoxton, might very well be quite different from what those words would mean if one were considering the sale of Blenheim Palace."

Despite the need for caution, the development of non-tax case law in this area is clearly something to watch.

***Ritchie & Ritchie v HMRC* [2017] UKFTT 449 (TC): Where there is no identifiable main residence, curtilage cannot be the sole test as it would exclude from the exemption large numbers of properties.**

Here the taxpayers bought part of a dismantled train station with two buildings on it, a large shed and a small potting shed. The large shed was used for storage and the family rented a house nearby whilst they built a three storey house on the plot. In 2007 they sold the house and the sheds to a developer. The large shed was 85m from the new house. The FTT decided that, although binding authority, *Lady Rook* was irrelevant because there was no identifiable main residence. The FTT preferred the *Batey* test and disregarded size (which they considered only one factor) in favour of proximity and appurtenance. The evidence of the Ritchies, oral, written and photographic, showed that they extensively used and regularly accessed the shed as a garage, workshop and kitchen overflow and for the storage of sports equipment, that it was connected to the mains and was an intrinsic part of the family's residence. The FTT took "identifiable main house" to mean main house as opposed to another building which contains living accommodation, and probably though not certainly, occupied by an employee or similar.

CG64292 HMRC Concession: The curtilage test cannot be easily applied to a taxpayer who lives in a flat or small urban house.

HMRC concede that the curtilage test cannot be easily applied to flats and small urban houses because it is likely that the flat or house will have little or no curtilage beyond its walls or small garden. At CG64292 they state that in many cases the owner of a flat or urban house will own a separate garage which may be outside the curtilage of the dwelling-house or be separated from it by land and buildings not owned by the taxpayer. HMRC consider that in such circumstances if the garage is near to the flat or house and is bought and sold with the flat or house it can be considered to be part of the dwelling-house.

In *Honour v Norris* [1992] BTC 153 Vinelott J rejected as “an affront to common sense” the taxpayer’s claim that separate flats in different buildings in the same square occupied by the same family comprised a single dwelling. It was in his view the same as concluding that a house in a neighbouring village used for occasional personal use and for guests was part of the main dwelling-house. The flat disposed of was 60-80 yards from the other flats and provided accommodation for elder children, guests and occasionally for the taxpayer and his spouse. At CG64292 HMRC seem to suggest that the case is confined to its facts: “The High Court found that having regard to the particular facts of the case the two flats did not form a single dwelling-house, however the judge declined to set out any general guidelines on the question which could be applied to other cases.”

CG64305 concedes:

“There may be occasions where a group of flats can be considered to be one dwelling-house. This may be the case if they are

- All occupied by the owner and his or her family
- Within the same block
- Contiguous.

If the flats are in the same block but on different floors or are separated by other flats, relief should only be allowed in exceptional circumstances. The length of occupation and the use of the flats are important factors in deciding how flats should be treated and consideration should be given to all the relevant facts and circumstances. If the flats are in different blocks or are only connected via the street, then they should be treated as separate dwelling-houses."

Why the length of occupation should be a factor is a mystery. It is also unclear exactly what "near" might mean. In any event, practitioners would be wise to treat the availability of this treatment with caution except in the most straightforward cases.

Curtilage, garden and grounds

Curtilage determines the extent of a dwelling-house for the purposes of TCGA 1992 s.222(1)(a). It does not determine the extent of the permitted area of gardens and grounds for the purposes of s.222(1)(b). A building within the permitted area of garden and grounds will qualify for relief whether or not it is part of the dwelling-house, provided the other conditions for relief are met. Similarly what is included in the curtilage of a house will automatically qualify for relief as part of a dwelling-house, provided again that the other conditions are met. However, the importance of the curtilage test should not be overlooked in determining 'the size and character of the dwelling-house' and thus enabling a larger area of garden or grounds to qualify for relief.

Final thoughts

A taxpayer, such as Mr Crippin, faced with completing his tax return on the disposal of an annex or ancillary property, or a practitioner weighing up the consequences of failure to return a chargeable disposal, will empathise with the comments of Balcombe LJ in *Lady Rook* who said “I have to say that I do not find the current state of the authorities very satisfactory, and it is hardly surprising that different sets of General Commissioners have reached conclusions which are not always easy to understand.” Both may find their 60 days time limit for submission of their CGT return ticking away as they ponder the mesh of fine lines that they need to navigate.

However there are some practical measures that practitioners can look for that may help in determining the outcome on a part disposal of a dwelling house:

1. It is critical to retain records, written and photographic, that evidence a single dwelling, in case of dispute. In particular it is worth considering the statements made in planning applications and in estate agent's particulars.

2. In addition to proximity, buildings are more likely to be treated as a single dwelling house if they have shared utilities, common points of access, are not separately rated, are acquired and sold together and if one passes on the conveyance of the other under a single title number without being named.

3. The taxpayer should use all of the buildings in question so that together they form the whole of their residence (whether through family, friends or staff), with unrestricted access to all parts.

TAX 'AVOISION' – WHERE DO WE DRAW THE LINE?[1]

Dilpreet K. Dhanoa

With an Alternative Perspective & Commentary by Peter Vaines

"What you see and what you hear depends a great deal on where you are standing. It also depends on what sort of person you are."

These insightful words from the Chronicles of Narnia (The Magician's Nephew) by C. S. Lewis are equally as applicable to the magical world of childhood fantasy as they are to the spectrum of tax evasion and avoidance. That is 'avoision'. The Collins English Dictionary defines 'avoision' as "*the non-payment of tax which cannot be classified as either avoidance or evasion.*" This article argues that there is a line that

[1] This article was originally submitted for Taxation magazine's and the London Tax Society's Young Professionals Tax Writing Competition 2021. This is an amended version of the article which was the winning entry. This version published fpr the FCTC Digest includes an 'alternative perspective and commentary' section by Peter Vaines (ranked in Chambers & Partners 2021).

can be drawn, but not by drawing shifting lines in the sand as has happened to date; but rather, by having an enshrined set of guiding principles that assist in defining the parameters.

This article will argue that up until now where the line is drawn ultimately boils down to a matter of perspective, and the tax debate around 'morality' has added difficulties that pose a challenge for the executive, legislature and judiciary. Some 85 years ago, Lord Tomlinson in the infamous case of *IRC v Duke of Westminster*[2], adopted the view that *"*[e]*very man is entitled…to order his affairs so as that the tax attaching…is less that it would otherwise be."* It followed judgments advancing this position, and which divorced the moral (or any other) obligation from what the statutory wording permitted.[3] Lord Atkin viewed the function of the court as being only *"to determine the legal result of* [the taxpayer's] *dispositions so far as they affect tax."*[4] In other words, the taxpayer had a right to

2 (1936) AC 1.
3 See: *Ayrshire Pullman Motor Services v Ritchie v Inland Revenue Commissioners* (1929) 14 TC 754, *per* Lord Clyde.
4 *IRC v Duke of Westminster* (1936) AC 1, *per* Lord Atkin.

dispose of their capital and income in a manner which attracted the least amount of tax – provided they had a legal right to do so.

Approximately three decades later, the Institute of Economic Affairs published a lecture delivered by A. A. Shenfield: 'The Political Economy of Tax Avoidance'.[5] Shenfield condemned the approach of Lord Atkin, and described tax avoidance as a *"peculiar half-world"* – legally distinct from tax evasion; but morally, to the ordinary man, it was no different to evasion. He concluded by weighing up which was the worst 'evil' as between avoidance and anti-avoidance, coming to the view that the latter had gone far beyond what Parliament and the legislature had intended. The literature had by this point tied itself up in discussions of morality, ambivalence and the risks associated with it tax avoidance. It laid the groundwork for sentiments to be later expressed by the courts, such as Lord Reid in the Supreme Court6

5 Shenfield, A. A., 'The Political Economy of Tax Avoidance' (1968) Institute for Economic Affairs.

6 [2016] UKSC 13.

wherein he set out in the opening passage of his judgment:

> "In our society, a great deal of intellectual effort is devoted to tax avoidance. The most sophisticated attempts of the Houdini taxpayer to escape from the manacles of tax…generally take the form…[which] include elements which have been inserted without any business or commercial purpose but are intended to have the effect of removing the transaction from the scope of the charge."

When such an overlay of morality creeps in, it is inevitable that any objectivity in applying legal principles becomes an increasingly uphill battle. It has brought us no closer to determining the line that is to be drawn with respect to avoision. The spectrum of avoision simply continues the morality debate around avoidance, and without an over-arching set of guiding principles the task for the courts is made even more difficult.

Is there a Spectrum of Avoision or is it just a Question of Morality?

The problem with a term like 'avoision' is that like avoidance and evasion, it will be ultimately viewed through the lens of morality. It could be argued that the line should be drawn as close as possible to contain avoidance as much as possible, whilst continuing to keep evasion as an outlaw. Those who adopt this approach are likely to advance the case that anything on a spectrum of avoision should not be permissible. Inherently, 'avoision' is a conceptual anomaly. It is inconsistent, no matter how consistent the tools and methodology might be, because any application will be dependent on the context.

The starting point is the proposition that avoidance is considered legal, whilst evasion is illegal. There are two issues: first, the actual statutory wording which is interpreted and applied by taxpayers, the revenue authority and the courts (which aims to be objective); and, secondly, the vernacular around the ‘avoision’ spectrum more broadly (which is inherently subjective). Take, for example, the UK VAT Act 1994. Part IV deals with the administration, collection and enforcement of the tax. Section 58A sets out the disclosure requirements for what is to be done by the taxpayer in relation to schemes that result in VAT being avoided. Section 60 (which is largely repealed, but still applicable in some instances) applies in respect of dishonest conduct. Section 72 sets out the offences under the act, and the language lends itself to being interpreted as a person’s conduct that is either dishonest or fraudulent will give rise to a penalty. The inference being: there could be ‘honest evasion’. This is where the grey and nebulous term ‘avoision’ bites – or so the taxpayer might argue.

This gives rise to the second issue: the semantics surrounding avoision. Almost 17 years ago, Chris Tailby, the then Director of HMRC’s Anti-Avoidance Group stated:

> “It may be tempting to 'dress up' avoidance schemes in an attempt to give them a veneer of commerciality to disguise the real purpose. But this is a dangerous game and raises the stakes for the company and its adviser to what is a dangerous level. At its highest, we are talking about putting forward a false case to the Tribunal. This is no longer in the realm of avoidance, nor is it ‘avoision’ or any other fancy name advisers may want to invent, it is outright deception. And that carries unpleasant consequences.”

The debate around where to draw the line depends on which side you come from. At its core, there is a search for some kind of certainty in the uncertain terrain that the spectrum of avoision presents. The taxpayer will argue that there was a commercial driver that can support the position that resulted in a tax benefit to them, but how is that line to be determined? Effectively with the element of morality, the courts are being asked to consider not just the commerciality of a transaction but the taxpayer's *mens rea* (i.e. mental intention). Is the system inadvertently imputing criminal justice into its framework?

The Role of the Executive, the Legislature & the Judiciary: Separation of Principles?

Practically, the position that practitioners and taxpayers are having to grapple with is: what is successful and unsuccessful tax planning? The courts have sought to define the parameters, leading to a murky situation with little clarity. As noted by Professor Freedman, the development in the case law has not been impressive.[7] There is confusion in the courts over how terms should be defined in such a way as to give effect to Parliament's intention. Whilst applying the label of 'avoidance' to describe a range of activities may be *de rigeur*, it is questionable at best. Yet the alternative approach: *"appealing to fairness or morality to counter them may not be*

[7] Freedman J., 'Interpreting Tax Statutes: Tax Avoidance and the Intention of Parliament' (2007) 123 Law Quarterly Review, 53-90.

particularly helpful in reaching a practical solution.”[8]

Ramsay[9] is often identified as the ‘classic formulation’[10] of the tax avoidance principle. The House of Lords identified the court’s task as being that of identifying and ascertaining the legal nature of any transaction which results in a tax consequence (that is beneficial to the taxpayer). It is a task which stands in direct contradiction to *Duke of Westminster*. Despite not departing from the latter, the House of Lords adopted a purposive construction method to unravel the ‘true nature’ of the transactions entered into with the sole intention of avoiding one’s legitimate tax liability. *Ramsay* lurched the tax avoision debate forward, but it slowed down thereafter.

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8 Devereux, Freedman and Vella paper, ‘Avoidance’ (for the National Audit Office 2012), p.2.

9 *W. T. Ramsay Ltd v. Inland Revenue Commissioners, Eilbeck (Inspector of Taxes) v. Rawling*[1982] AC 300.

10 Andrew Roycroft, ‘A Welcome Decision’, Taxation (15 March 2001).

Cases that followed (including *Burmah Shell*[11] and *Furniss v Dawson*[12]) have sought to stretch and test the boundaries of the Ramsay principle. Yet no decision or judgment has made clear what the parameters are. As times change, the context in which tax law is made rapidly falls to be out of date. It can be argued that the methods and tools the judiciary has at its disposal include: consideration of the relevant legal facts; the fact that courts are not bound to respect sham transactions (even if a party may seek to argue privity of contract); and, the commercial versus the legality of the situation (applying Lord Hoffman's test in *MacNiven v Westmoreland Investments Ltd*[13]). Yet the case law continues to produce lines in the sand: a shifting set of principles. Tax legislation requires clearer definitions to be provided because uncertainty is wholly undesirable in any tax system, and the courts cannot impose an alternative will to that of Parliament's intention. The methods must be

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[11] *Inland Revenue Commissioners v. Burmah Oil Co. Ltd* [1982] S.T.C. 30, H.L. (Sc.).

[12] *Furniss (Inspector of Taxes) v. Dawsom D.E.R.* [1984] A.C. 474.

[13] [2001] UKHL 6.

questioned as to their effectiveness, and it becomes even harder to draw the line with respect to avoision.

Rules such as Targeted Anti-Avoidance Rules ('TAARs') are hundreds in number, but target only very specific scheme structures. The statutory scheme, despite its ever-increasing volume, still does not provide any further insight into where the line can be drawn with respect to avoision.

In turn, the legislature is influenced by public policy. One of the most significant voices being the tax authority. The tax legislation leaves much to be desired, and the shot-gun approach provides little to no clarity on what could be 'acceptable' versus 'unacceptable' avoision. The courts are then required to pick up where the legislature departs and leaves a lacuna in the law. The courts face a challenging task: to apply Parliament's will in circumstances where the judiciary is being forced (in the absence of any guiding principles) to apply a moral overlay.

An Alternative Approach?

Ultimately, a system needs to be in place which can counter-balance the range of tax avoidance that is engaged in, be that aggressive or otherwise. Neither the legislative nor the judiciary can separately undertake this task satisfactorily. The current mechanisms and methods in place, do not allow the judiciary to create a solid and reliable body of case law. Rather, value-based and moral standards are imposed dependent on the context of a case, whilst seeking to apply what a court may consider to be Parliament's intention. This can only lead to uncertainty and confusion at best.

An alternative approach would be to adopt a specific set of general anti-avoidance (or avoision) rules – a GAAR, but a GAAR which would provide both taxpayers and the revenue authorities with guidance based on sound principles covering common ground. These principles in turn would also assist the judiciary when applying the law to the facts of a case. The need to define boundaries is slowing down any progress that might be made in this area, and instead the focus should be identifying the common ground and how that can be protected.

Currently, there are no core principles that any of the stakeholders impacted or involved in tax avoision can turn to. It is demonstrative in the position taken by the courts. In the *UBS; DB Services* case, it is evident that the devisers of the share schemes exercised prudent planning arrangements. The Court of Appeal agreed, yet the Supreme Court – undoubtedly swayed by external factors and having no core guiding principles to turn to, decided against the taxpayer. It is a deeply unsatisfactory position for any legal system of taxation to be in.

Tax policies and the outcome of tax cases should be underpinned by guiding ethical principles developed as objectively as possible with the tax system in mind, reflecting accountability, transparency and consistency. A GAAR would allow for this. It would remove the burden from the court-room, and it would also remove the need for Parliament to legislate in an ad hoc and retrospective manner. It would instead place in the centre of an enshrined set of rules, with an objective test to assist the Courts and those seeking to engage in tax planning. It would reduce this 'cat and mouse' game, as it would be in the hands of those most experienced in devising such rules to close off unwanted loopholes, but to permit reasonable behaviour within the bounds of such tax planning.

<u>An Alternative Analysis & Perspective: Commentary by Peter Vaines</u>

I congratulate Dilpreet on her award for this excellent article which was clearly well deserved.

I would like to comment briefly on the position of the GAAR.

I share Dilpreet's view that a GAAR could be of a real benefit to the community - both HMRC and taxpayers. However, in my view, the GAAR that we actually have in the UK, is not.

I would strongly support a GAAR Panel to assist the community in dealing with tax disputes. The GAAR is made up of experienced tax professionals and their conclusions might be helpful to the taxpayer, explaining independently and authoritatively, why his claim is unlikely to succeed. They might also expose defects in the Revenue's case – and either of these outcomes would be a sensible way to avoid unnecessary litigation. That would be a very valuable and worthwhile service which I am sure would attract widespread support.

But it is not like this. The GAAR Panel expresses their view and to all intents and purposes, it lays down the law. That is the practical effect. If you challenge their view you risk a penalty of 60% of the tax. In other words you can be seriously penalised if you choose to disagree with them.

But it is not the law. The law says the taxpayer is right. The GAAR Panel says that even though you are complying with the law, we don't like it and you must do what we say.

It is Parliament who makes the law – not the GAAR Panel – and it must be offensive to society for such a body to act in a way which usurps the authority of Parliament. If Parliament says your course of action is lawful, you should not be the subject of a penalty imposed by anybody else. It's called the Rule of Law.