TC02323

Appeal number: TC/2009/16580

PROCEDURE – Application to set aside decision and reinstate appeal after withdrawal of appeal by Appellant – application refused – consequences of withdrawal of appeal under section 54(4) Taxes Management Act 1970 – original decision confirmed - whether agreement to settle appeal under section 54(1) Taxes Management Act 1970 – held no

FIRST-TIER TRIBUNAL
TAX CHAMBER

ORCHID PROPERTIES **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE GREG SINFIELD

Sitting in public at in London on 3 October 2012

Mr Bob Frenzel, managing partner of Orchid Properties, for the Appellant

Ms Kim Sukul, officer of HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This was an unusual application. The Respondents ("HMRC") applied to the Tribunal to set aside the withdrawal of an appeal by Orchid Properties ("Orchid"). Orchid opposed the application despite the fact that, by withdrawing its appeal, Orchid became liable to pay an amount of tax which Orchid maintains is not due. Orchid had withdrawn its appeal following receipt of an amended statement of case ("the Amended SoC") from HMRC which stated that the tax in dispute was much less than previously discussed between the parties. Orchid claims that, by virtue of section 54 of the Taxes Management Act 1970 ("TMA"), the amount of tax now payable to HMRC is the amount set out in the Amended SoC. HMRC disagree: they maintain that the disputed tax was understated in error and, if the appeal is not reinstated, Orchid is liable to pay the amount of tax which was originally subject to appeal.

Evidence

2. Each party provided a bundle of correspondence and other documentation. Mr Bob Frenzel, managing partner of Orchid Properties, did not give evidence at the hearing and was not subject to cross-examination but I accept what he told me as to the facts during his submissions. I also heard from Mr Colin Wash, formerly a partner with Baker Tilly who advised Orchid in relation to the dispute. On the basis of the documents and evidence given at the hearing, I find the facts material to the application to be as set out below.

Facts

3. Orchid is a partnership which, at the relevant time, consisted of six partners and carried on a property development business. In January 2005, HMRC opened an enquiry into the partnership's tax return for the year ended 5 April 2003. HMRC took the view that a property bought by Orchid in 1996 and sold in December 2002 was held as trading stock throughout and the profit should be subject to tax under Case I of Schedule D. In October 2006, HMRC amended Orchid's partnership tax return for the year ended 5 April 2003 to increase the partnership profits by £1,146,102. The parties entered into discussions in an attempt to resolve the matter.

4. In a letter dated 4 March 2009, HMRC advanced an alternative argument that if, as Orchid contended, the property was held as an investment and subject to capital gains tax on its disposal then it was not held as a business asset and taper relief under the Taxation of Capital Gains Act 1992 should be restricted. Around the same time in early 2009, Orchid offered to pay £30,000 to settle the matter but HMRC rejected the offer. Following that rejection, Mr Wash, on behalf of Orchid, had a conversation with an HMRC officer, Mr Andy Jones, about what figure would be acceptable to HMRC. As a result of that conversation, Mr Jones sent a letter dated 19 March 2009 to Baker Tilly enclosing HMRC's calculation of Orchid's gain based on the alternative argument. The calculation showed Orchid's original figure of a capital

gain for each partner of £35,903. The calculation also showed HMRC's view of what the gain should be as a result of restricting the taper relief. The gain per partner, on HMRC's view, was £110,069. For reasons that will become clear later in this decision, it is worth noting that the difference between the two figures is £74,166.

5. The parties were not able to agree any settlement figure. In a letter dated 29 October 2009 ("the Decision Letter"), HMRC confirmed the decision in the closure notice issued on 13 October 2006. The Decision Letter referred to both the primary argument and the secondary argument although no amounts of tax in dispute were specified.

6. On 25 November 2009, Baker Tilly, acting on behalf of Orchid, lodged a Notice of Appeal with the Tribunal against the Decision Letter. The grounds of appeal stated that:

> "HMRC initially proposed an increase to the partnership profits of £1,146,102 and have recently made a secondary claim for an increase to the original capital gain returned of £444,996 if their primary argument failed."

The amount of £444,996 is arrived at by multiplying £74,166 by six ie the number of partners in Orchid.

7. On 1 March 2010, HMRC lodged a statement of case ("the Original SoC") with the Tribunal. The Original SoC summarised both the primary and the alternative arguments.

8. Notwithstanding the fact that the appeal had been commenced, Orchid and its advisers still attempted to persuade HMRC that the decision was wrong. In an email dated 28 February 2011 to Baker Tilly, HMRC stated that they had accepted Orchid's argument that the property transaction gave rise to a capital gain although they maintained that taper relief should be restricted. In effect, the email stated that HMRC was no longer pursuing its primary argument. This was confirmed in an email dated 1 March 2011 from HMRC to the Tribunal, copied to Baker Tilly, which included draft directions that, among other things which are not relevant, required HMRC to produce an amended statement of case.

9. On 18 May 2011, HMRC lodged the Amended SoC with the Tribunal. The Amended SoC referred to the primary argument and the amendment to the return which increased the partnership profits by £1,146,102 and then stated:

> "Following further discussions between the parties, [HMRC] now accepts [Orchid's] position regarding the primary issue in the case and [HMRC] now contends that the profit should be increased by £74,166 based on an alternative argument which is still in dispute."

10. On 21 June 2011, Baker Tilly sent the following email to the Tribunal and copied it to HMRC:

> "WITHOUT PREJUDICE
>
> Please note that our client, the appellant, Orchid Properties, wish to withdraw their appeal against the contention by HM Revenue and Customs that the partnership profit should be increased by £74,166.
>
> Please note that the withdrawal of this appeal in no way is an acceptance of the arguments put forward by HM Revenue and Customs but is made as a practical decision to avoid any further costs in this matter.
>
> We would be grateful for your acknowledgement of our withdrawal of the appeal."

11. The email of 21 June was acknowledged by HMRC in an email the following day which stated that:

> "I note that your client has withdrawn his appeal and I have asked my Inspector to make the necessary tax adjustment."

12. On 29 June 2011, the Tribunal wrote a letter to HMRC enclosing a copy of the email withdrawing the appeal and stating that the file would be closed and any hearing dates cancelled. On the same day, the Tribunal also wrote to Baker Tilly in similar terms. That letter also stated:

> "Please note that you have 28 days from the date of your withdrawal to apply to the Tribunal if you wish the case to be reinstated."

13. On 1 September 2011, HMRC issued amended personal Self Assessment Tax Returns for the year ended 5 April 2003 to each of the six partners in Orchid for tax on an increase in taxable gain of £74,166 plus interest.

14. In a letter dated 30 May 2012, HMRC made an application under rule 38 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ("the Rules") to set aside a decision of the Tribunal which disposed of proceedings and that the appeal of Orchid should be reinstated. The application to set aside was made out of time and so HMRC also applied for an extension of time in which to make such application.

Submissions

15. At the hearing of the application, Ms Kim Sukul for HMRC submitted that the Amended SoC simply contained an error. It should have said that "the profit *per partner* should be increased by £74,166" or, alternatively, that the figure of £74,166 was a slip and should have been £444,996. HMRC contended that Orchid would have been aware of the error because they had referred to the alternative argument and the higher profit figure in their grounds of appeal. HMRC did not accept that the appeal had been determined by agreement under section 54 of the TMA as an error in a statement of case could not constitute a binding offer of settlement and they had never agreed to the figure suggested. Ms Sukul contended that the Tribunal made a decision, by its letter of 29 June 2011, which disposed of the proceedings. HMRC

now applied under Rule 38 of the Rules for Orchid's appeal to be reinstated. If the appeal was not reinstated then HMRC contended that the consequence of the withdrawal of the appeal was that the original determination of the amount of tax due was confirmed.

16. Mr Frenzel for Orchid submitted that the partners had spent time considering what to do after receiving the Amended SoC. He said that they never considered that the Amended SoC was not correct. They thought that, in the context of previous discussions, HMRC was open to a compromise and had decided to offer to settle for a figure that was at the upper end of what Orchid was prepared to pay. Mr Frenzel said that he relied on section 54(4) of the TMA as well as section 54(1).

Issues

17. This application raises several issues. The first is whether the appeal was withdrawn and, if so, then can HMRC apply to have it reinstated? If the appeal is reinstated then the position is restored to what it was before Orchid withdrew the appeal but if it is not reinstated then what are consequences of withdrawal? Additionally, there is the issue of whether the Amended SoC and the correspondence that followed it constituted an agreement under section 54(1) of the TMA.

Was there a withdrawal of the appeal?

18. Rule 17(1) of the Rules provides that a party may give notice of the withdrawal of its appeal by sending a written notice of withdrawal to the Tribunal at any time before a hearing to dispose of the proceedings. In my view, the email from Baker Tilly of 21 June clearly stated that Orchid wished to withdraw the appeal but it is arguable that it was made under a mistake of fact. The email stated that the appeal that was being withdrawn was against the contention by HMRC that the partnership profit should be increased by £74,166. This was an odd statement as there was no previous decision to that effect and Orchid had never appealed against any such decision. Orchid's notice of appeal referred to a primary claim for an increase in profit of £1,146,102 and a secondary claim for £444,996. The first time that, according to Orchid, HMRC had suggested that Orchid's profit should be increased by only £74,166 was in the Amended SoC. There was never any appeal against that amount.

19. At the hearing, Mr Frenzel said that he would not have withdrawn the appeal if he had thought that the amount of tax that would be payable was as much as £444,996. He argued that the Amended SoC should be seen as HMRC making an offer to settle in the context of the long running negotiations. I do not accept this. The Amended SoC was not part of the negotiations which had stopped by that time. There had never been any previous offer by HMRC to accept a figure that anything less than the amount under the alternative argument of £444,996 and the figure in the Amended SoC came out of the blue. Further, I find it very unlikely that Baker Tilly, who had computed the overall tax liability of £444,996 in the notice of appeal by multiplying HMRC's figure for the increase in profit per partner of £74,166 by the number of partners, did not realise that the amount of £74,166 in the Amended SoC

was a simple error rather than a proposal to settle. It seems to me, therefore, to be arguable that the withdrawal was made by Orchid on the basis of a mistake. The only alternative hypothesis is that Orchid was deliberately trying to take advantage of an obvious error in the Amended SoC which understated the tax in dispute.

20. Notwithstanding my view of the situation, both parties at the hearing accepted that Baker Tilly's email of 21 June 2011 was a valid withdrawal of Orchid's appeal. The Tribunal in its letter of 29 June clearly treated the appeal as withdrawn. Where an appeal is withdrawn, Rule 17(3) provides that:

> "(3) A party who has withdrawn their case may apply to the Tribunal for the case to be reinstated."

An application under Rule 17(3) must be made within 28 days of the date the Tribunal received the notice. It is clear from Rule 17(3) that only the party who has withdrawn the appeal can apply for it to be reinstated. HMRC cannot do so.

21. At the hearing, I suggested to Mr Frenzel that if the withdrawal had been made because of a mistake then he might like to consider whether to apply for the appeal to be reinstated. An application under Rule 17(3) must be made within 28 days of the date the Tribunal received the notice, ie by 19 July 2011 in this case, and so Orchid would also have to apply for an extension of time under rule 5(3)(a) of the Rules. I said that I would be prepared to consider granting an extension of time in order to enable him to do so and Ms Sukul said that HMRC would not oppose such an application. Mr Frenzel declined to make any application.

22. In conclusion on this issue, the language of Baker Tilly's email of 21 June 2011 withdrawing the appeal was clear and, as Orchid has not sought to argue that it withdrew the appeal as a consequence of any mistake or misunderstanding, the appeal should be regarded as having been withdrawn.

Application to set aside and reinstate

23. As I have already stated above, HMRC cannot apply under rule 17(3) of the Rules for an appeal that has been withdrawn to be reinstated. Ms Sukul anticipated this difficulty by applying under rule 38. Rule 38 of the Rules deals with "Setting aside a decision which disposes of proceedings". It reads as follows:

> "(1) The Tribunal may set aside a decision which disposes of proceedings or part of such a decision, and re-make the decision, or the relevant decision, if –
>
> (a) the Tribunal considers that it is in the interest of justice to do so; and
>
> (b) one or more of the conditions in paragraph (2) is satisfied
>
> (2) The conditions are –

(a) a document relating to the proceedings was not sent to, or was not received at an appropriate time by, a party or a party's representative;

(b) a document relating to the proceedings was not sent to the Tribunal at an appropriate time;

(c) there has been some other procedural irregularity in the proceedings; or

(d) a party, or a party's representative, was not present at a hearing related to the proceedings."

24. Rule 38(3) provides that an application to set aside a decision must be made by written application received by the Tribunal no later than 28 days after the date when the Tribunal sent the notice of the decision to the party. HMRC's application was made outside the time limit and so they also applied for an extension of time.

25. I do not need to consider whether to grant an extension of time because, in my view, rule 38 of the Rules cannot apply in this case. Rule 38 only applies to a decision which disposes of proceedings. HMRC submitted that the Tribunal's letter of 29 June 2011 was such a decision. In my view, the letter was not a decision within the Rules. The term "decision" is not defined in the Rules but it is clear from rule 35 that it requires findings of fact and reasons. The Tribunal's letter of 29 June 2011 did not contain or refer to any facts or reasons nor did it purport to communicate any decision. It was an administrative act following withdrawal of an appeal under rule 17. Such a withdrawal does not require any decision by the Tribunal and, indeed, the Tribunal cannot do anything other than accept a withdrawal if it is validly made. It follows that, in the absence of a decision, HMRC's application under rule 38 must be refused.

What are consequences of withdrawal?

26. Rule 17 of the FTT Rules does not provide for the consequences of a withdrawal although rule 10(4)(b) allows an application for costs to be made following withdrawal in suitable cases. Orchid made such an application on 4 July 2011 for an order that HMRC should pay Orchid's costs on the ground that HMRC had acted unreasonably in bringing and conducting the proceedings against Orchid.

27. Section 54(4) of the TMA provides for the consequences of a withdrawal by an appellant where HMRC do not object to the withdrawal within 30 days. The consequences are "as if, at the date of the appellant's notification, the appellant and the inspector … had come to an agreement, orally or in writing, as the case may be, that the assessment or decision under appeal should be upheld without variation". Mr Frenzel contended that the Amended SoC should be treated as the decision under appeal and the effect of section 54(4) is that Orchid should be required to pay tax on an overall increase in profit of £74,166. Ms Sukul submitted that the language of section 54(4) is clear and that the effect of the withdrawal is that the decision under appeal should be upheld without variation.

28. I agree with HMRC on this point. As I have already set out above, Orchid had never appealed against any decision that it should pay £74,166. Orchid appealed against HMRC's decision that the partnership's profit should be increased by £1,146,102 or, in the alternative, by £444,996. By the time of the withdrawal, HMRC had conceded its primary case and I consider that the decision under appeal was that the profit should be increased by £444,996. It follows that, under section 54(4), the consequence of Orchid's withdrawal of its appeal is that the decision that the partnership's profit should be increased by £444,996 is upheld without variation.

Was there a section 54(1) agreement?

29. Mr Frenzel also relied on section 54(1) of the TMA contending that the Amended SoC was an offer to settle on the basis of an overall liability of £74,166 which was accepted by Orchid in the email of 21 June 2011. Section 54 of the TMA deals with the settling of appeals by agreement. It provides that where, before an appeal is determined by the tribunal, an appellant and HMRC come to an agreement, whether in writing or otherwise, that the decision under appeal should be treated in a particular manner then the same consequences follow as if the tribunal had so determined the appeal.

30. I do not accept that the Amended SoC and the withdrawal of the appeal can be regarded as an agreement under section 54(1) of the TMA. In relation to this point, I adopt the same approach as the Court of Appeal in *Schuldenfrei v Hilton* [1999] STC 821. In *Schuldenfrei*, the tax inspector issued an amended notice of assessment which incorrectly showed the gains as nil. The taxpayer did not respond and, when the inspector sought to rectify the error, sought to argue that a section 54 agreement had been reached. This argument was rejected by the Court of Appeal. Jonathan Parker J, delivering the lead judgment, held:

> "44 To my mind, the notion of parties having 'come to' an agreement plainly implies not merely that they are of the same mind in relation to some particular matter, but also that their minds have met so as to form a mutual consensus; and that that meeting of minds, that mutual consensus, has resulted from a process in which each party has to some extent participated. On that footing it is, in my judgment, both legitimate and helpful (as both sides have accepted) to approach the question whether the Revenue and the taxpayer have made a section 54 agreement in the instant case by applying common law principles of offer and acceptance.
>
> 45 Adopting that approach, the first question which arises is whether the May 1993 notice contained an offer capable of acceptance by the taxpayer. I agree [with counsel for the taxpayer] that the mere fact that the adjustments to the original assessment referred to in the May 1993 notice had never validly been made does not directly affect that question, and that it is necessary to look at the May 1993 notice in order to see what, on its face, it said.

> 46 As I read the May 1993 notice, it purported to do no more and no less than notify the taxpayer that the revenue had adjusted the original assessment by reducing it to nil. It did not invite any response from the taxpayer, still less did it look to any 'acceptance' from him. Moreover, it came out of the blue, in the sense that it was not the product of any earlier discussion, still less negotiation, between the Revenue and the taxpayer. There had, of course, been lengthy negotiations as to the amount of the taxpayer's capital gains tax liability for the relevant year, but at no stage in those negotiations had the taxpayer suggested that his liability was nil. So the May 1993 notice cannot be set in the context of any earlier dealings between the Revenue and the taxpayer. In my judgment, to construe the May 1993 notice in these circumstances as containing an offer or proposal by the Revenue which, to become effective, invited or required 'acceptance' by the taxpayer would be to turn the May 1993 notice into something which, on its face, it manifestly was not.
>
> 47 In agreement with the judge, therefore, I conclude that the May 1993 notice did not contain any offer capable of acceptance by the taxpayer so as to result in a section 54 agreement."

31. In this case, it seems to me to be clear that the Amended SoC could not be construed as an offer by HMRC to settle the appeal on the basis of an increase in the partnership profits of £74,166. The Amended SoC was not expressed as an offer to settle. It was part of the pleadings in the appeal and did not invite any acceptance by Orchid but was predicated on the existence of a dispute between the parties. As in *Schuldenfrei*, the alleged offer came out of the blue, earlier discussions having come to nothing. Further, the letter of withdrawal, which Mr Frenzel contended was an acceptance of HMRC's offer, made no mention of section 54 or any agreement between the parties. In conclusion, I reject Orchid's submission that there was any agreement to dispose of the appeal under section 54(1) of the TMA.

Decision

32. My decision is that HMRC's application to have Orchid's appeal reinstated must be refused. I have also concluded that there was no agreement under section 54(1) of the TMA to settle the appeal. As a consequence of withdrawing the appeal in the absence of an agreement, Orchid has made itself liable to pay the tax due on the basis of HMRC's alternative argument with no opportunity to appeal against that decision.

33. As discussed above, Orchid declined to make an application to reinstate the appeal at the hearing. If, having considered this decision, Orchid now wishes to apply for reinstatement of its appeal (and an extension of time in which to do so) then I direct that it must do so within 14 days of the date of release of this decision.

34. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later

than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

GREG SINFIELD
TRIBUNAL JUDGE

RELEASE DATE: 19 October 2012