[2019] UKFTT 489 (TC)

TC07292

Appeal number: TC/2015/05875
TC/2015/05814
TC/2016/00419

INCOME TAX – IT contractor employed by offshore company – loans made to taxpayer from employee benefits trust set up by employer – whether or not payments by employer to EBT were taxable earnings – accepted by appellant – whether or not HMRC entitled to raise discovery assessments under s29 TMA 1970 – held yes – whether or not HMRC entitled to exercise discretion under s 684(7A) ITEPA 2003 to disapply PAYE regulations – held yes – whether or not taxpayer alternatively subject to taxation under the transfer of assets abroad legislation – held yes, subject to the amount of the income of the person abroad – whether or not EU law principle of free movement of capital prevents application of TOAA legislation – held no because discrimination is justified by tax avoidance purpose of TOAA legislation

FIRST-TIER TRIBUNAL
TAX CHAMBER

STEPHEN HOEY — **Appellant**

- and -

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

TRIBUNAL: JUDGE PHILIP GILLETT

Sitting in public at Taylor House, London on 1 to 9 July 2019

Rory Mullan, counsel, instructed by Reynolds Porter Chamberlain LLP, for the Appellant

Aparna Nathan QC and Marika Lemos, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. This was an appeal against:

(1) a decision of HMRC to raise two discovery assessments under s29 Taxes Management Act 1970 ("TMA") ("the Assessments"):

(a) One dated 18 February 2013 in respect of 2008-09, in the amount of £40,437.15, and

(b) One dated 5 March 2014 in respect of 2009-10, in the amount of £2,334.20.

(2) The conclusions stated in, and the amendments by, a closure notice issued on 22 December 2015 ("the Closure Notice") in respect of the 2010-11 year of assessment in the amount of £36,810.20.

2. In outline, the appellant, Mr Hoey, participated in various iterations of a marketed tax avoidance scheme, the aim of which was to avoid tax on earnings by providing loans to users of the scheme, instead of earnings.

3. The arrangements under consideration in this appeal were:

(1) A scheme involving Penfolds, a company resident in the Isle of Man, as the employer ("the Penfolds Scheme") which had 3,014 users, and

(2) A scheme involving Hamilton Trust, a company resident in Guernsey, as the employer ("the Hamilton Trust Scheme") which had 3,152 users.

4. The Hamilton Trust Scheme was modified in response to the anti-forestalling provisions and the Hamilton Trust Anti-Forestalling "loan cleansing" scheme, as it was termed, ("the Loan Cleansing Scheme") was disclosed to HMRC on 15 August 2011 by RSM Tenon Group Plc. This scheme fell outside the tax years which are under appeal in this case.

RULE 18 DIRECTION

5. This appeal was one of two cases which were designated lead cases pursuant to Rule 18 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 in relation to a number of other appellants who were employed by the same employers under the same terms. The appellant in the other lead case, Mr Stephen Vaughan Jones, withdrew his appeal on 17 June 2019. There were originally 43 other cases joined to this appeal under Rule 18, although nine of these have withdrawn their appeals, leaving 34 still covered under the Rule 18 procedure.

The Issues

6. The issues as originally agreed between the parties, as they are set out in the Rule 18 Direction, were as follows:

> (1) Can an assessment pursuant to s29 TMA 1970 be raised on a taxpayer in respect of income which is PAYE income?
>
> (2) Were the assessments validly made in accordance with s29 TMA 1970?
>
> (3) Were monies received by Penfolds and/or the Hamilton Trust in respect of the services provided by [their employees] earnings [of their employees] within the meaning of s62 Income Tax (Earnings and Pensions) Act 2003 ("ITEPA")? If so, how is the amount of those earnings to be determined?
>
> (4) Were loans made to [the employees] from the Penfolds Employee Benefits Trust and/or the Hamilton Employee Benefits Trust earnings within the meaning of s62 ITEPA? If so, how is the amount of those earnings to be determined?
>
> (5) In the event that the answer to the first question in (3) and (4) above is negative, did [the employees] obtain a financial benefit from the loan made by the Penfolds EBT and/or the Hamilton EBT? If so, how is the value of that financial benefit to be taxed?
>
> (6) Were the loans made by the Penfolds EBT and/or the Hamilton EBT released and/or written off after they were made by the Penfolds EBT and/or the Hamilton EBT so that s188 ITEPA 2003 is engaged?
>
> (7) Does a charge to tax on the [employees] arise under the provisions of Chapter 2, Part 13, Income Tax Act 2007 ("ITA"), the Transfer of Assets Abroad legislation ("the TOAA legislation")? If so how is that income identified?
>
> (8) Does the use of the Penfolds/Hamilton arrangements by [the employees] engage Article 63 of the Treaty on the Functioning of the European Union ("TFEU")?
>
> (9) Does the use of the Penfolds/Hamilton arrangements engage section 815AZA ICTA 1988? (This issue was not argued before me.)

7. In advance of the appeal, on 12 June 2019, Reynolds Porter Chamberlain LLP, Mr Hoey's representatives, wrote to HMRC to say that Mr Hoey had considered HMRC's arguments as to the application of the decision of the Supreme Court in *RFC 2012 (in liquidation) v Advocate General for Scotland* [2017] 1 WLR 2767 to these arrangements, and accepted that the reasoning adopted by Lord Hodge in that case would apply to the facts of this appeal. The consequence of that is that the sums which were paid to the Trusts with a view to an onward loan to Mr Hoey were properly to be taxed as earnings of Mr Hoey.

The Remaining Issues

8. Mr Hoey's acceptance of HMRC's argument that payments to the Trusts are to be taxed as his employment income disposes of some, but not all, of the issues listed above. Mr Mullan argued that his client's concession on this point should also dispose of HMRC's alternative argument on the application of the TOAA legislation, but Ms Nathan, on behalf of HMRC, submitted that I should also consider this argument because it would provide an alternative head of charge should I find against HMRC on some of the other issues listed above or should this decision be appealed to higher courts.

9. The remaining issues therefore are:

(1) Do the discovery assessments for 2008-09 and 2009-10 meet the conditions for a valid assessment under s29 TMA 1970? In particular:

(a) Have HMRC shown that a valid discovery was made? (s29(1)).

(b) Was Mr Hoey's tax return submitted in line with the practice generally prevailing at the time as regards the submission of individual tax returns? (s29(2)).

(c) Should the information disclosed by Mr Hoey in his tax returns for the years in question have alerted a hypothetical reasonably competent inspector of taxes that there was an insufficiency of tax? (s29(5)).

(2) HMRC state that they have exercised a general discretion available to them under s684(7A) ITEPA 2003 to disapply the PAYE Regulation in cases where they consider it appropriate, thus transferring the effective burden of paying the tax from the ultimate users of Mr Hoey's services to Mr Hoey himself. The questions therefore arise as to:

(a) whether or not HMRC do possess this general discretion, and

(b) whether or not HMRC had exercised this alleged discretion legally.

(3) Do the provisions of the TOAA legislation apply to the amounts received by Mr Hoey? In particular:

(a) Does the creation of the employment contracts between Mr Hoey and Penfolds/Hamilton constitute the transfer of an asset by Mr Hoey, a UK resident, to Penfolds/Hamilton, who were not resident in the UK, to a person abroad?

(b) If so what is the measure of the "income" which has been transferred to the person abroad?

(c) Can Mr Hoey claim the benefit of the motive test to avoid any charge under this legislation?

(d) Is the application of the TOAA legislation in contravention of EU law, particularly does it infringe one or more of the four fundamental freedoms?

(e) If it does infringe one of these freedoms is there justification for the infringement on the basis that it is a proportionate response to the objective of the arrangements?

THE FACTS

10. I received witness statements and oral evidence from Mr Hoey, Andrew Parr, a Director of Hansard Limited, a company based in Guernsey, Matthew Hall, formerly an employee of RSM Tenon, the firm which devised the Penfolds arrangements, and now tax adviser to the claimants in this appeal, Andy Finch, a retired officer of HMRC, and Lesley Stopp, also a retired officer of HMRC. I also received a witness statement from Scott MacFarlane, an officer of HMRC, but he was not called to give oral evidence, and his witness statement was not challenged.

11. A number of the witnesses had difficulty in remembering precise details from many years ago but I found all of them to be fundamentally honest and credible witnesses.

12. On the basis of these witness statements, the oral evidence and the bundle of documents provided to me, I find the following as matters of fact.

Outline Facts

13. Mr Hoey is an IT specialist and, as was common in that sector at that time, the ultimate users of Mr Hoey's services ("End Users") did not wish to take on additional employees to work on relatively short term contracts, of the order of one to two years. In order to obtain work therefore, Mr Hoey had to provide his services either as an independent consultant or through a company, either his own personal service company or a third party provider employing a number of such contractors, which was referred to as an umbrella company.

14. Mr Finch estimated that approximately 1.7million individuals had provided their services to End Users as contractors during this period and that, of those, approximately 15,000 had engaged in similar arrangements to those used by Mr Hoey. The vast majority of contractors had therefore provided their services to End Users by more conventional means.

15. Mr Hoey had previously, in around 2004, supplied his services to End Users via a personal service company but had found the complexities of running his own company too much for him to deal with. He had therefore engaged the services of an intermediary, Dynamic Management Solutions Ltd ("DMS"), and, in 2007-08, they had introduced him to Penfolds, at which time he entered into employment with Penfolds. In September 2009 Penfolds suggested he should transfer his employment to Hamilton Trust, a Guernsey based trust company, which he duly did.

16. DMS, and a subsequent intermediary, Cascade, were Mr Hoey's prime points of contact throughout this process. He trusted them totally. If they recommended a course of action then he believed that that course of action would be in his best interests. He submitted his time sheets to them and they in turn submitted invoices to

the End Users. Mr Hoey had very little to do with the other parties to the arrangements although he clearly signed the various documents which were sent to him.

17. Various publicity material which had been produced by Penfolds and Hamilton, and which described the benefits of these schemes, was presented to the tribunal. Mr Hoey could not remember if he had read this material thoroughly but if he had he did not understand the implications of what was being suggested to him.

18. His motivation in entering into these schemes was solely to avoid the complexities of running his own company or his own business. When considering whether or not to enter the schemes he simply compared the post-tax cash he would receive under his existing arrangements, via a UK umbrella company, and the post-tax cash he would receive under the Penfolds arrangement. The cash which he would receive under the Penfolds arrangement was slightly better than he was currently receiving but Mr Hoey did not really understand that this was because he would be paid in a way which was designed to avoid paying UK tax on a large part of his earnings.

19. Importantly I note that Mr Hoey did not receive the full benefit of the absence of UK tax on his earnings because the fees chargeable by the various intermediaries were between 10% and 18% of his income, compared to the 1% which might be charged by a simple UK based umbrella company. A substantial part of the hoped for benefit of avoiding UK tax was therefore absorbed by the fees being charged by the promoters and facilitators of the scheme.

20. In Mr Hoey's case the End Users were Axa Investment Managers Ltd, Aviva Investors and Threadneedle Investments. These were all entities based in the UK.

21. Mr Hoey and his fellow employees ("the Contractors") were paid a basic wage for their work for Penfolds/Hamilton ("the Employers") and tax was paid in full on those earnings. This was deducted at source under the PAYE Regulations and paid over to HMRC even though the Employees were both non-UK resident and therefore not strictly within the ambit of the PAYE Regulations.

22. In addition, each Employer then made substantial contributions to a trust which it had established for the benefit of its employees (referred to as "the Trusts"). The trustees of the Trusts ("the Trustees") provided benefits to the Contractors, in their capacity as beneficiaries of the Trusts, by making interest-free loans ("the loans") to the Contractors. The loans were stated to be repayable on demand but the Contractors did not expect to be required to repay the loans at any time. Of the many users of these schemes, Mr Hall said that he was aware of only three who had actually repaid their loans, although there was some confusion as to whether or not HMRC had required the loans to be forgiven or repaid in the cases where Contractors had settled their tax liabilities with HMRC.

23. The loans were treated by the Contractors as employment related loans under Chapter 7, Part 3 Income Tax (Earnings and Pensions) Act 2003 ("ITEPA") and were disclosed to HMRC and taxed as such in their tax returns.

24. Both the Penfolds and the Hamilton schemes had been disclosed to HMRC under the DOTAS legislation and both had been allocated a Scheme Reference Number. Both Scheme Reference Numbers were disclosed on Mr Hoey's tax return for 2009-10 but not on his return for 2008-09.

25. On 23 March 2011, Karen Gough of RSM Tenon wrote to Mr Hoey, stating:

> "We have been in discussions with your employer ("Hamilton Trust") about your possible resignation as an employee… We understand that Hamilton Trust has made an offer for you not to have to work your notice period if you make the decision to resign. Should you make this decision, we would propose, without incurring any legal obligation to do so, to make you an ex gratia payment equal to the amount of the loans you have received from the EBT since December 9th 2010 but subject to a maximum of £29,250. This figure has been calculated by reference to funds at our disposal, the length of your contract with our end client remaining post 6 April and various other factors. It is our intention to set off the ex gratia payment pound for pound against the loans we have made to you since 9th December 2010, subject to a maximum of £29,250. Any balance above this amount and any loans made to you prior to 9th December 2010 will not be considered for set off and will remain outstanding and repayable on demand. This offer is made on the bass that you accept it prior to 2 April 2011…."

26. Mr Hoey could not remember any details of this and could not remember whether or not he had actually resigned from his employment with Hamilton. It seems to have been an attempt to reduce the amount of the loan outstanding in a way which would not attract tax, by making a termination payment, the first £30,000 of which would be free of tax. This £29,250 "payment" was offset against part of his loan from the Hamilton EBT and was shown on Mr Hoey's tax return for the year as a termination payment but I had no other evidence of what had happened such as a resignation letter or any documentation concerning Mr Hoey's subsequent employment.

Detailed Scheme Arrangements

The Penfolds Arrangements

27. The Penfolds arrangements were allocated DOTAS scheme reference number 71676485.

28. The arrangements involved the Contractor entering into a contract of employment with Penfolds.

29. The Contractor would provide services to a company ("the End User").

30. Typically, this would be through a third party UK based company (an “Intermediary”). In some cases, the Intermediary would contract with the End User through an agent (an "Agency").

31. Penfolds would agree with the Intermediary to provide the Contractor’s services.

32. The Agency or Intermediary would then contract with the End User as appropriate for the onward supply of the Contractor.

33. The Contractor would provide timesheets to the Agency or Intermediary which enabled it to invoice the End User.

34. The End User would pay the Intermediary either directly or through the Agency.

35. The Intermediary would pay Penfolds subject to its fee or commission.

36. Penfolds would pay a salary to the Contractor, which marketing literature suggested would be 20-25% of the annual gross estimated billed time.

37. Penfolds would contribute monies to the Penfolds EBT.

38. Loans would be made to Contractors from the Penfolds EBT based on recommendations made by the directors of Penfolds.

39. A series of loans were made throughout the period of employment and were paid into the Contractors’ personal bank accounts. Loans were typically made on terms that they would be interest free, unsecured and repayable on demand.

The Hamilton Arrangements

40. The Hamilton arrangements were allocated DOTAS scheme reference number 23237278.

41. The arrangements involved the Contractor entering into a contract of employment with the Hamilton Trust, which was a trust company which had been set up by Hansard Limited, a company based in Guernsey.

42. The Contractor would provide services to a company (“the End User”). Typically, this would be through a third party UK based company (an “Intermediary”). In some cases, the Intermediary would contract with the End User through an agent ("an Agency").

43. The Hamilton Trust would agree with the Intermediary to provide the Contractor’s services.

44. The Agency or Intermediary would then contract with the End User as appropriate for the onward supply of the Contractor.

45. The Contractor would provide timesheets to the Agency or Intermediary which enabled it to invoice the End User.

46. The End User would pay the Intermediary either directly or through the Agency.

47. The Intermediary would pay the Hamilton Trust subject to its fee or commission.

48. The Hamilton Trust would pay a salary to the Contractor.

49. The Hamilton Trust would contribute monies to the Hamilton EBT.

50. Loans would be made to Contractors from the Hamilton EBT based on recommendations made by the Hamilton Foundation, an organisation based in Panama, which was the Enforcer of the Hamilton EBT.

51. A series of loans were made throughout the period of employment which were paid into the Contractors' personal bank accounts. Loans were typically made on terms that they would be interest free, unsecured and repayable on demand.

The Hamilton Loan Cleansing Arrangements

52. These arrangements were allocated DOTAS scheme reference number 45921195.

53. From 10 December 2010 loans made by the Hamilton EBT were subject to a condition that they were repayable on 30 March 2012.

54. In November 2011, the Hamilton Trust offered all former employees a loan ("the new loan") to be used to repay any outstanding loans made by the Hamilton EBT since 9 December 2010. The new loan agreement specified that the new loan would be paid directly to the Hamilton EBT in settlement of such loans. Contractors who did not take up this offer were advised that loans made by the Hamilton EBT since 9 December 2010 were to be repaid by 30 March 2012.

55. In November and December 2011 the Hamilton Trust made loans to Contractors which were used to repay loans made to those Contractors from the Hamilton EBT.

56. On or after 5 December 2011, the Hamilton Trust sold the loans (at face value) to the Hamilton EBT, which paid cash for them. The loans were assigned to the EBT under the terms of that sale.

The Tax Returns

57. Mr Hoey's tax returns for the years under appeal were all filed within the normal statutory time limits. They were prepared by Mr Hoey's accountants, which had been Global Tax Services Limited in the first year and then Kingston Smith in the subsequent years. Again Mr Hoey had not really paid much attention to the detail as to what was said in the returns and had trusted his professional advisers totally.

58. The tax return for 2008-09 showed the amount Mr Hoey had been paid as salary by Penfolds, £24,458, as taxable income, plus the taxable benefit of the interest free loans, which was calculated as £8,570. In the "white space" area of the form, box 19, it stated:

> "The figures in box 15 of the employment page relates to interest free sterling loans provided by the Penfolds (IOM) Limited Employee Benefit Trust. The loans are repayable on demand."

59. The tax return for 2009-10 showed the amount Mr Hoey had been paid as salary by Penfolds and Hamilton, totalling £12,187, as taxable income, plus the taxable benefit of the interest free loans, which was calculated as £5,246. In box 14 it stated two scheme reference numbers for tax avoidance schemes, 23237278 and 71676485, being the scheme reference numbers for the Hamilton and Penfolds schemes respectively. In the "white space" area of the form, box 19, it stated:

> "Penfolds – 961/ZA02563
>
> The figure shown in box 15 of the Employment Supplementary Page E1 is in relation to interest free loans from the Penfolds Employee Benefit Trust. These loans are repayable on demand."

There was no reference in box 19 to any loans from the Hamilton EBT.

60. The tax return for 2010-11 showed the amount Mr Hoey had been paid as salary by Hamilton, £10,699, as taxable income, plus the taxable benefit of the interest free loans, which was calculated as £1,864. In box 18 it stated a scheme reference number for a tax avoidance scheme, 23237278, being the scheme reference number for the Hamilton scheme. No additional information was given in the "white space" area of the form but the figure for the taxable benefit of the interest free loan was shown on a separate schedule to the return. The return also contained a figure for Redundancy and other lump sums and compensation payments of £29,250.

The Discovery and the Issue of Assessments

61. Mr Finch was a senior officer of HMRC at the time the discovery assessments were made and had been working on the contractor loan schemes for a number of years. He had come to the conclusion, working with other senior officials and specialists within HMRC, that the schemes could be defeated using the TOAA legislation.

62. In order to take this work forward, in late 2012, Mr Finch was provided with the services of a personal tax compliance team, based in Bedford, under the leadership of Miss Stopp. Mr Finch met Miss Stopps and her team on 19 November 2012 and provided them with the initial training on the work which they would be undertaking.

63. The presentation which Mr Finch gave to the team indicated that there were 17 schemes and approximately 15,000 individuals using these schemes. The tax potentially recoverable was estimated at £445m. Mr Finch emphasised that, in the

grand scheme of things, this was not an enormous amount of tax. What was more concerning for HMRC was the number of individuals involved, and HMRC considered that having so many people avoiding tax in this way would set a bad precedent and encourage others to seek to reduce their tax liabilities in this way.

64. The teams involved with this work were eventually trained to the level at which they could satisfactorily handle telephone calls from the taxpayers affected.

65. While Miss Stopps' team was preparing to work on the earlier years it also commenced work on opening up enquiries into approximately 3,500 returns for 2010-11, which were still in time for HMRC to open enquiries in the normal manner under s9A TMA.

66. At this time HMRC had the tax returns from the individual contractors and the P11Ds and P35s which had been provided by the Employers, which set out the amount of the loans. HMRC did therefore have a list of all scheme participants and the loans which were made to them for all years up to 2010-11. These had been compiled by specialist analysts within HMRC from the various Employers' and individual returns in HMRC's possession.

67. HMRC had written to the Isle of Man authorities requesting a great deal of information in 2008, but it was not clear what if anything had been received from the Isle of Man authorities in response to that letter.

68. Mr Finch said that by 7 May 2013, when he met Mr Hall for an initial discussion of these issues, he had not received anything from the Isle of Man authorities at that time but that the contents of what he referred to as "57 boxes" were received in CD form not long after the meeting with Mr Hall. This was, he said, a response to another letter to the Isle of Man authorities which he had sent much later. I received no further evidence as to this information and I therefore accept Mr Finch's version of events as factually correct.

69. It rapidly became apparent that further resources would be required in addition to the 11 caseworkers in Miss Stopps' team, and a second team was allocated to the task. In addition a Personal Tax Operations team was also brought on board. This further team was not as experienced in discovery assessments and therefore worked alongside the existing Bedford teams to ensure that the appropriate level of supervision and training could be provided.

70. Further teams in Blackburn, Wrexham and Cambridge subsequently became involved.

71. Miss Stopps, along with Mr Finch and other senior officers, developed a methodology for processing the information to ensure consistency of approach on the part of all members of the teams. These were initially in the form of simple word documents, which were referred to as working instruction documents ("WIDs") and these WIDs were subsequently adapted and improved and became known as standard working instructions ("SWIs"). This change was primarily to bring the terminology into line with that used in similar situations throughout HMRC. As the work

progressed the SWIs were update to improve their efficiency and usability based on experience of using them.

72. The process was divided into three stages, SWI 1, SWI 2 and SWI 3:

(1) SWI 1 established the loan figure,

(2) SWI 2 calculated the amount of any insufficiency of tax, and

(3) SWI 3 covered the making of the discovery assessment.

73. The "discovery" for the purposes of s29 was therefore made by the officer handling the SWI 2 process because this is the point at which a calculation showed an insufficiency of tax in respect of the individual taxpayer. This officer then referred the case to another officer to handle the actual mechanics of raising an assessment using the SWI 3, although sometimes it was the same officer handling both the SWI 2 process and the SWI 3 process.

74. There was an internal team practice rule which dictated that step 3 of the process had to be completed on the same day as step 2 to ensure that mistakes were avoided. This does not seem to have been followed precisely in the case of Mr Hoey in that:

(1) As regards 2008-09, the SWI 2 calculation was made on 11 February 2013 and the Assessment was issued 2 days later, on 13 February 2013.

(2) As regards 2009-10, the SWI 2 calculation was made on 5 March 2014 and the Assessment was issued on the same day.

75. By design, there was no element of discretion in the process and the only decision making had to be done in accordance with the processes set out in the SWIs.

76. I note at this stage that the discovery assessments raised on Mr Hoey for 2008-09 and 2009-10 appear to include not only a tax charge on the loans which were being assessed as additional earnings, but also included the charge to tax on the benefit of receiving interest free loans which had been included on Mr Hoey's original tax return. It is clear that an individual in these circumstance should not be assessed to tax on both the benefit of having an interest free loan as well as being taxed on the receipt of the loan as if it were earnings. Miss Stopp acknowledged that this was an error, and indeed the SWIs contained a specific instruction that this element of double taxation should be removed. This instruction clearly had not been followed in Mr Hoey's case.

77. The assessment letters were all signed "for Miss LJ Stopp". Miss Stopp did not actually look at every single assessment but considered that if the complete SWI process had been followed then the assessment would be valid and for the correct amount.

78. The officers working on the SWI 1 process were often relatively junior but those working on SWI 1 and SWI 2 were experienced officers of Administrative Officer grade and were properly authorised to issue assessments. As stated above,

they were also trained so as to be able to handle telephone calls from taxpayers on the discovery assessments which were being issued.

79. Under the PAYE Regulations the normal process in these circumstances would be that the tax would be paid by the End Users. However, Mr Finch made the decision not to pursue the End Users for the tax outstanding because he considered that they knew nothing about the tax avoidance arrangements and therefore considered it inappropriate for them to pay. He therefore exercised the discretion which he believed was available to HMRC under s684(7A) ITEPA not to require the End Users to pay the tax. He explained that HMRC internal procedures required this decision to be taken by an officer of Grade 7 or above, and he was a Grade 6. He was not required to consult with any one further up the hierarchy within HMRC.

THE LAW

80. The legislation in this case is very extensive and I will not therefore set it out in full. The key provisions are however set out below.

81. The provisions regarding discovery are contained in s29 TMA which provides, as far as is relevant, as follows:

> **"29 Assessment where loss of tax discovered**
>
> (1) If an officer of the Board or the Board discover, as regards any person (the taxpayer) and a year of assessment—
>
> > (a) that any income which ought to have been assessed to income tax, or chargeable gains which ought to have been assessed to capital gains tax, have not been assessed, or
> >
> > (b) that an assessment to tax is or has become insufficient, or
> >
> > (c) that any relief which has been given is or has become excessive,
>
> the officer or, as the case may be, the Board may, subject to subsections (2) and (3) below, make an assessment in the amount, or the further amount, which ought in his or their opinion to be charged in order to make good to the Crown the loss of tax.
>
> (2) Where—
>
> > (a) the taxpayer has made and delivered a return under section 8 or 8A of this Act in respect of the relevant year of assessment, and
> >
> > (b) the situation mentioned in subsection (1) above is attributable to an error or mistake in the return as to the basis on which his liability ought to have been computed,
>
> the taxpayer shall not be assessed under that subsection in respect of the year of assessment there mentioned if the return was in fact made on the basis or in accordance with the practice generally prevailing at the time when it was made (or, where the error or mistake is in an end of period statement forming part of

the return, if that statement was provided on the basis of or in accordance with the practice generally prevailing at the time when it was provided).

(3) Where the taxpayer has made and delivered a return under section 8 or 8A of this Act in respect of the relevant year of assessment, he shall not be assessed under subsection (1) above—

(a) in respect of the year of assessment mentioned in that subsection; and

(b) in the same capacity as that in which he made and delivered the return,

unless one of the two conditions mentioned below is fulfilled.

(4) The first condition is that the situation mentioned in subsection (1) above was brought about carelessly or deliberately by the taxpayer or a person acting on his behalf.

(5) The second condition is that at the time when an officer of the Board—

(a) ceased to be entitled to give notice of his intention to enquire into the taxpayer's return under section 8 or 8A of this Act in respect of the relevant year of assessment; or

(b) informed the taxpayer that he had completed his enquiries into that return,

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 subsection (1) above.

(6) For the purposes of subsection (5) above, information is made available to an officer of the Board if—

(a) it is contained in the taxpayer's return under section 8 or 8A of this Act in respect of the relevant year of assessment (the return), or in any accounts, statements or documents accompanying the return;

(b) it is contained in any claim made as regards the relevant year of assessment by the taxpayer acting in the same capacity as that in which he made the return, or in any accounts, statements or documents accompanying any such claim;

(c) it is contained in any documents, accounts or particulars which, for the purposes of any enquiries into the return or any such claim by an officer of the Board, are produced or furnished by the taxpayer to the officer; or

(d) it is information the existence of which, and the relevance of which as regards the situation mentioned in subsection (1) above—

(i) could reasonably be expected to be inferred by an officer of the Board from information falling within paragraphs (a) to (c) above; or

(ii) are notified in writing by the taxpayer to an officer of the Board."

82. The provisions regarding the PAYE Regulations are contained in s684 ITEPA 2003 and this, as far as is relevant, is set out below:

"684 PAYE regulations

(1) The Commissioners for Her Majesty's Revenue and Customs must make regulations ("PAYE regulations") with respect to the assessment, charge, collection and recovery of income tax in respect of all PAYE income.

(2) PAYE regulations may, in particular, include any such provision as is set out in the following list.

List of Provisions

…

4A Provision authorising the recovery from the payee rather than the payer of any amount that an officer of Revenue and Customs considers should have been deducted by the payer.

…

(3) The deductions of income tax required to be made by PAYE regulations under item 1 in the above list may be required to be made at the basic rate or other rates in such cases or classes of case as may be provided by the regulations.

(4) Interest required to be paid by PAYE regulations under item 6 or 7 in the above list must be paid without any deduction of income tax and may not be taken into account in computing any income, profits or losses for any tax purposes.

(5) PAYE regulations must not affect any right of appeal to the General or Special Commissioners which a person would have apart from the regulations.

(6) It does not matter for the purposes of PAYE regulations that income is wholly or partly income for a tax year other than that in which the payment is made.

(7) PAYE regulations have effect despite anything in the Income Tax Acts.

(7A) Nothing in PAYE regulations may be read—

(a) as preventing the making of arrangements for the collection of tax in such manner as may be agreed by, or on behalf of, the payer and an officer of Revenue and Customs, or

(b) as requiring the payer to comply with the regulations in circumstances in which an officer of Revenue and Customs is satisfied that it is unnecessary or not appropriate for the payer to do so.

(7B) References in this section and section 685 to income tax in respect of PAYE income are references to income tax in respect of that income if reasonable assumptions are (when necessary) made about other income.

(7C) In this section and section 685—"payer" means any person paying PAYE income and "payee" means any person in receipt of such income;
"specified" means specified in PAYE regulations.

(8) In this Act and any other enactment (whenever passed) "PAYE regulations" means regulations under this section."

83. The TOAA legislation is contained in Chapter 2, Part 13, Income Tax Act 2007 ("ITA"), the key provisions of which are as follows.

84. Section 720 ITA is the basic charging provision and provides:

"**720 Charge to tax on income treated as arising under section 721**

(1) The charge under this section applies for the purpose of preventing the avoiding of liability to income tax by individuals who are ordinarily UK resident by means of relevant transfers.

(2) Income tax is charged on income treated as arising to such an individual under section 721 (individuals with power to enjoy income as a result of relevant transactions).

(3) Tax is charged under this section on the amount of income treated as arising in the tax year.

(4) ...

(5) The person liable for any tax charged under this section is the individual to whom the income is treated as arising.

(6) ...

(7) For exemptions from the charge under this section, see sections 736 to 742 (exemptions where no tax avoidance purpose or genuine commercial transaction)."

85. Section 721 ITA then provides (so far as is relevant):

"**721 Individuals with power to enjoy income as a result of relevant transactions**

(1) Income is treated as arising to such an individual as is mentioned in section 720(1) in a tax year for income tax purposes if conditions A and B are met.

(2) Condition A is that the individual has power in the tax year to enjoy income of a person abroad as a result of—

(a) a relevant transfer ,

(b) one or more associated operations , or

(c) a relevant transfer and one or more associated operations.

(3) Condition B is that the income would be chargeable to income tax if it were the individual's and received by the individual in the United Kingdom.

(4) For the purposes of subsection (2), it does not matter whether the income may be enjoyed immediately or only later.

(5) It does not matter for the purposes of this section—

(a) whether the income would be chargeable to income tax apart from section 720,

(b) whether the individual is ordinarily UK resident at the time when the relevant transfer is made, or

(c) whether the avoiding of liability to income tax is a purpose for which the transfer is effected.

(6) For the circumstances in which an individual is treated as having the power to enjoy income for the purposes of this section, see section 722."

86. This means that where an individual resident in the UK transfers assets to a person abroad, and that individual has the power to enjoy the income of that person abroad, then the individual is chargeable to tax in respect of that income.

87. Section 727 ITA provides (so far as relevant):

"**727 Charge to tax on income treated as arising under section 728**

(1) The charge under this section applies for the purpose of preventing the avoiding of liability to income tax by individuals who are ordinarily UK resident by means of relevant transfers.

(2) Income tax is charged on income treated as arising to such an individual under section 728 (individuals receiving capital sums as a result of relevant transactions).

(3) Tax is charged under this section on the amount of income treated as arising in the tax year.

(4) ...

(5) The person liable for any tax charged under this section is the individual to whom the income is treated as arising.

(6) For exemptions from the charge under this section, see sections 736 to 742 (exemptions where no tax avoidance purpose or genuine commercial transaction).

(7) For rules about the availability of deductions and reliefs where income is charged under this section, see section 746 (deductions and reliefs where individual charged under section 720 or this section)."

88. Section 728 ITA provides, (so far as is relevant):

"**728 Individuals receiving capital sums as a result of relevant transactions**

(1) Income is treated as arising to such an individual as is referred to in section 727(1) in a tax year for income tax purposes if—

(a) income has become the income of a person abroad as a result of—

(i) a relevant transfer,

(ii) one or more associated operations, or

(iii) a relevant transfer and one or more associated operations, and

(b) the capital receipt conditions are met in respect of the individual in the tax year (see section 729)."

89. Section 729 ITA provides:

"**729 The capital receipt conditions**

(1) For the purposes of section 728(1), the capital receipt conditions are met in respect of the individual in a tax year ("the relevant year") if—

(a) either—

(i) in the relevant year the individual receives or is entitled to receive any capital sum, whether before or after the relevant transfer, or

(ii) in any earlier tax year the individual has received any capital sum, whether before or after the relevant transfer, and

(b) the payment of that sum is (or, in the case of an entitlement, would be) in any way connected with any relevant transaction.

(2) But subsection (1)(a)(ii) does not apply merely because of the receipt of a sum by way of loan if the loan is wholly repaid before the relevant year begins.

(3) In subsection (1) "capital sum" means—

(a) any sum paid or payable by way of loan or repayment of a loan, and

(b) any other sum paid or payable—

(i) otherwise than as income, and

(ii) not for full consideration in money or money's worth.

(4) For the purposes of subsection (1), a sum is treated as a capital sum which the individual ("A") receives or is entitled to receive if another person receives or is entitled to receive it—

(a) at A's direction, or

(b) as a result of the assignment by A of A's right to receive it."

90. The transfer of assets provisions are disapplied if the motive defence applies. Given that all the relevant transactions were effected after 5 December 2005, the relevant motive defence is set out in s737 ITA:

> "**737 Exemption: all relevant transactions post-4 December 2005 transactions**
>
> (1) This section applies if all the relevant transactions are post-4 December 2005 transactions.
>
> (2) An individual is not liable to income tax under this Chapter for the tax year by reference to the relevant transactions if the individual satisfies an officer of Revenue and Customs—
>
> > (a) that Condition A is met, or
> >
> > (b) in a case where Condition A is not met, that Condition B is met.
>
> (3) Condition A is that it would not be reasonable to draw the conclusion, from all the circumstances of the case, that the purpose of avoiding liability to taxation was the purpose, or one of the purposes, for which the relevant transactions or any of them were effected.
>
> (4) Condition B is that—
>
> > (a) all the relevant transactions were genuine commercial transactions (see section 738), and
> >
> > (b) it would not be reasonable to draw the conclusion, from all the circumstances of the case, that any one or more of those transactions was more than incidentally designed for the purpose of avoiding liability to taxation.
>
> (5) In determining the purposes for which the relevant transactions or any of them were effected, the intentions and purposes of any person within subsection (6) are to be taken into account.
>
> (6) A person is within this subsection if, whether or not for consideration, the person—
>
> > (a) designs or effects, or
> >
> > (b) provides advice in relation to,
>
> the relevant transactions or any of them.
>
> (7) In this section—
>
> > "revenue" includes taxes, duties and national insurance contributions,
> >
> > "taxation" includes any revenue for whose collection and management the Commissioners for Her Majesty's Revenue and Customs are responsible.
>
> (8) If—

(a) apart from this subsection, an associated operation would not be taken into account for the purposes of this section, and

(b) the conditions in subsections (2) to (4) are not met if it is taken into account, because of—

(i) the associated operation, or

(ii) the associated operation taken together with any other relevant transactions, it must be taken into account for those purposes."

DISCUSSION

91. As set out above, the issues in this case fall into three discrete areas:

(1) The discovery provision contained in s29 TMA 1970,

(2) The exercise of the discretion under s684(7A) ITEPA 203, a subset of which is whether or not I have the jurisdiction to consider if HMRC exercised that discretion legally, and indeed whether or not I have the jurisdiction to consider the application of the PAYR Regulations in any case, and

(3) Whether or not the provisions of the TOAA legislation apply to the amounts received by Mr Hoey.

I will therefore address these in turn.

Discovery

92. The issue as to whether or not HMRC are able to issue discovery assessments under s29 TMA also falls into three separate parts:

(1) Was there a valid discovery "that an assessment to tax is or has become insufficient", and, if so, was it acted on within a reasonable timeframe such that the discovery did not become "stale",

(2) Were Mr Hoey's returns "in fact made on the basis or in accordance with the practice generally prevailing at the time when it was made", and

(3) Could the officer "have been reasonably expected, on the basis of the information made available to him before [he ceased to be entitled to give notice of his intention to enquire into the taxpayer's return], to be aware of the situation", ie the insufficiency of tax.

Was there a valid discovery?

93. As set out above, I have found as a matter of fact that:

(1) As regards 2008-09, a "discovery" of an insufficiency of tax was made on 11 February 2013, and the assessment was issued 2 days later, on 13 February 2013, and

(2) As regards 2009-10, a "discovery" of an insufficiency of tax was made on 5 March 2014, and the assessment was issued on the same day.

94. The "discovery" of an insufficiency of tax was made by an HMRC officer working through the SWI 2 process. The officer concerned was at least of Administrative Officer grade and was therefore authorised to issue an assessment. That officer then passed the file onto another officer, also of at least Administrative Officer grade, to carry out the SWI 3 process and issue the actual assessment.

95. The question however is whether or not this was a valid discovery for the purposes of s29(1). There is much judicial guidance on this but the most helpful in my view is that contained in the judgement of the Upper Tribunal in *Charlton and others v HMRC* [2012] UKFTT 770 (TCC) at [37]:

> "In our judgment, no new information, of fact or law, is required for there to be a discovery. All that is required is that it has newly appeared to an officer, acting honestly and reasonably, that there is an insufficiency in an assessment. That can be for any reason, including a change of view, change of opinion, or correction of an oversight. The requirement for newness does not relate to the reason for the conclusion reached by the officer, but to the conclusion itself."

96. In my view it is clear that the officer carrying out the SWI 2 process in this case made a discovery failing within these words. There was perhaps no new information, of fact or law, the relevant information was already in the possession of HMRC, but there was the need for a precise calculation to identify that there was an insufficiency of tax in the particular case of the Contractor concerned. Miss Stopps noted that in some, a very few, cases the Contractor had actually returned the loans as income. As such there was no insufficiency of tax, and without carrying out a detailed calculation this fact would not have been known. A satisfactory discovery was therefore, in my view, properly made.

97. Mr Mullan raised a number of objections to the use of a process by HMRC. He suggested that in fact the discovery was not made by an officer but was discovered as a result of the application of a mechanical process which did not permit any element of discretion or judgement by the officers involved, and was not therefore a valid discovery. In support of this argument he put forward the words of the Court of Appeal in *Burford v Durkin (Inspector of Taxes)* [1991] STC 7:

> "Counsel for the Crown advanced a general proposition of law to the following effect. Where a statute confers a power on an official to exercise his discretion, only that official can exercise it. But once he has exercised that discretion he may delegate purely ministerial tasks which flow from the exercise of that discretion to another. If he does so, he has still properly exercised his statutory power; the carrying out of the ministerial task is treated in law as being his."

98. In my view, in spite of the inevitable constraints of a semi-mechanised process, which was essential to ensure consistent treatment between taxpayers in similar

circumstances, I find that the officer carrying out the SWI 2 process did genuinely make the discovery that there was an actual insufficiency of tax in Mr Hoey's case. It is hard to understand how an officer can make such a discovery without carrying out a detailed calculation of the tax due and comparing that with the tax already paid or deducted at source. The fact that the calculation process in question has been devised by another officer and applied to a large number of taxpayers in a similar position cannot in my view render that discovery null and void.

99. I do not therefore agree that the officer carrying out the SWI 2 process somehow failed to meet the requirements of making a discovery within the terms of s29(1). In my view, this constituted a valid discovery of an insufficiency of tax within the terms of s29(1).

100. Having made the discovery, the officer carrying out the SWI 2 process then passed the file onto the officer dealing with the SWI 3 process, or in some cases carried out the SWI 3 process themselves, leading to the issue of the assessments, in accordance with the SWI 3 process. To me this seems to fall clearly within the words of the Court of Appeal in *Burford*:

> "… once he has exercised that discretion he may delegate purely ministerial tasks which flow from the exercise of that discretion to another."

101. I therefore find nothing wrong with the discovery process.

102. It is also obvious that since the assessments were issued within two days of the discovery, or on the same day in the case of 2009-10, there is no question of any staleness.

Generally Prevailing Practice

103. A defence against a discovery assessment is available under s29(2) to a taxpayer who has filed a tax return and has done so in accordance with generally prevailing practice.

104. For Mr Hoey, Mr Mullan accepted that HMRC were correct in asserting that this ground can only succeed if the only basis of raising the discovery assessment is that *RFC 2012* applies. In other words, if the only basis for HMRC raising the discovery assessments is the decision in *RFC 2012*, that the redirection of payments from the Employers to the Trusts constituted taxable emoluments, then Mr Hoey's returns were made in line with the practice as regards this element before the decision in *RFC 2012* was made. That decision was issued by the Supreme Court on 5 July 2017 and was of course preceded by the decision of the Court of Session in *AG for Scotland v Murray Group Holdings Ltd and others* [2015] CSIH 77, in what was effectively the same case. That decision was issued on 4 November 2015. Since Mr Hoey's returns were made before these decisions then they cannot be said to affect what was the generally prevailing practice at the time the returns were made.

105. However it is also quite clear that the discovery assessments were not made, and cannot have been made, only on the basis of the decision in *RFC 2012*. The discovery

assessments were made on 13 February 2013 and 5 March 2014, ie, well before the decision of the Court of Session in *Murray Group Holdings*. Mr Finch's evidence, which I have accepted as factually correct, is that the discovery assessments were raised on the basis that HMRC could tax the amounts of the loans under the TOAA legislation.

106. Since Mr Mullan has conceded that this ground of appeal can only succeed if the decision in *RFC 2012* was the only basis on which the discovery assessments were issued, then this ground must fail.

Section 29(5) TMA

107. The issue as regards s29(5) is whether or not "the officer could have been reasonably expected, on the basis of the information made available to him before [he ceased to be entitled to give notice of his intention to enquire into the taxpayer's return], to be aware of the situation", ie the insufficiency of tax.

108. In *Sanderson v Revenue and Customs Commissioners* [2016] EWCA 19, in the Court of Appeal, Patten LJ set out, at [17], the principles established by the earlier cases:

> "17. It is clear as a matter of authority:
>
> (1) that the officer is not the actual officer who made the assessment (for example Mr Thackeray in this case) but a hypothetical officer;
>
> (2) that the officer has the characteristics of an officer of general competence, knowledge or skill which include a reasonable knowledge and understanding of the law: see *HMRC v Lansdowne Partners LLP* [2012] STC 544;
>
> (3) that where the law is complex even adequate disclosure by the taxpayer may not make it reasonable for the officer to have discovered the insufficiency on the basis of the information disclosed at the time: see *Lansdowne* at [69];
>
> (4) that what the hypothetical officer must have been reasonably expected to be aware of is an actual insufficiency: see *Langham v Veltema* [2004] STC 544 per Auld LJ at [33]-[34]:
>
>> "33. More particularly, it is plain from the wording of the statutory test in section 29(5) that it is concerned, not with what an Inspector could reasonably have been expected to do, but with what he could have been reasonably expected to be aware of. It speaks of an Inspector's objective awareness, from the information made available to him by the taxpayer, of "the situation" mentioned in section 29(1), namely an actual insufficiency in the assessment, not an objective awareness that he should do something to check whether there is such an insufficiency, as suggested by Park J. If he is uneasy about the sufficiency of the assessment, he can exercise his power of enquiry under section 9A and is given plenty of time in which to complete it before the discovery provisions of section 29 take effect.

> 34. In my view, that plain construction of the provision is not overcome by Mr. Sherry's argument that it is implicit in the words in section 29(5) "on the basis of the information made available to him" (my emphasis) and also in the provision in section 29(6)(d) for information, the existence and relevance of which could reasonably be inferred from information falling within section 29(6) (a) to (c), that the information itself may fall short of information as to actual insufficiency. Such provision for awareness of insufficiency "on the basis" of the specified information or from information that could reasonably be expected to be inferred therefrom does not, in my view, denote an objective awareness of something less than insufficiency. It is a mark of the way in which the subsection provides an objective test of awareness of insufficiency, expressed as a negative condition in the form that an officer "could not have been reasonably expected … to be aware of the" insufficiency. It also allows, as section 29(6) expressly does, for constructive awareness of insufficiency, that is, for something less than an awareness of an insufficiency, in the form of an inference of insufficiency."

(5) that the assessment of whether the officer could reasonably have been expected to be aware of the insufficiency falls to be determined on the basis of the types of available information specified in s.29(6). These are the only sources of information to be taken into account for that purpose: see *Langham v Veltema* at [36]:

> "The answer to the second issue– as to the source of the information for the purpose of section 29(5) - though distinct from, may throw some light on, the answer to the first issue. It seems to me that the key to the scheme is that the Inspector is to be shut out from making a discovery assessment under the section only when the taxpayer or his representatives, in making an honest and accurate return or in responding to a section 9A enquiry, have clearly alerted him to the insufficiency of the assessment, not where the Inspector may have some other information, not normally part of his checks, that may put the sufficiency of the assessment in question. If that other information when seen by the Inspector does cause him to question the assessment, he has the option of making a section 9A enquiry before the discovery provisions of section 29(5) come into play. That scheme is clearly supported by the express identification in section 29(6) only of categories of information emanating from the taxpayer. It does not help, it seems to me, to consider how else the draftsman might have dealt with the matter. It is true, as Mr. Sherry suggested, he might have expressed the relevant passage in section 29(5) as "on the basis only of information made available to him", and the passage in section 29(6) as "For the purposes of subsection (5) above, information is made available to an officer of the Board if, but only if," it fell within the specified categories. However, if he had intended that the categories of information specified in section 29(6) should not be an exhaustive list, he could have expressed its opening words in an inclusive form, for example, "For the purposes of

subsection (5) above, information … made available to an officer of the Board … includes any of the following".”””

109. Patten LJ then continued at [22]:

> “22. It is important to emphasise that the decision in *Lansdowne* did not involve any qualification of what Auld LJ in *Langham v Veltema* identified as the question posed by the second s.29(5) condition. The hypothetical officer must, on an objective analysis, be made aware of an actual insufficiency in the assessment by the matters disclosed in the s.29(6) information. This is made clear by the Chancellor at [55] of his judgment in *Lansdowne*. The sole dispute in that case was whether the disclosures made by the taxpayer’s accountants were sufficient to cause the hypothetical officer to conclude that there was an insufficiency.”

110. He then noted at [25] that:

> “25. I do not accept that ss.29(1) and (5) import the same test and that the Revenue’s power to raise an assessment is therefore directly dependent on the level of awareness which the notional officer would have based on the s.29(6) information. The exercise of the s.29(1) power is made by a real officer who is required to come to a conclusion about a possible insufficiency based on all the available information at the time when the discovery assessment is made. Section 29(5) operates to place a restriction on the exercise of that power by reference to a hypothetical officer who is required to carry out an evaluation of the adequacy of the return at a fixed and different point in time on the basis of a fixed and limited class of information. The purpose of the condition is to test the adequacy of the taxpayer’s disclosure, not to prescribe the circumstances which would justify the real officer in exercising the s.29(1) power. Although there will inevitably be points of contact between the real and the hypothetical exercises which ss.29(1) and (5) involve, the tests are not the same.”

111. Mr Mullan, for Mr Hoey, suggested that the information available to the hypothetical officer, or which could reasonably be inferred, from Mr Hoey’s tax returns included:

(1) The existence of a loan which was interest free and repayable on demand.

(2) The P11D disclosing details of the loan.

(3) The existence of an employee benefit trust (the EBT).

(4) The fact the employment was with an Isle of Man company.

(5) The fact that the amount loaned from the EBT in the year was significantly in excess of Mr Hoey’s earnings from his employment.

(6) For 2009-10 he should also have been aware of the DOTAS disclosures

112. Mr Mullan also argued that the knowledge of the hypothetical officer should include the HMRC internal note “Spotlight 5: PAYE and National Insurance

contributions, Corporation Tax and Inheritance Tax: using trusts and similar entities to reward employees" which was issued on 5 August 2010. This stated:

> "HMRC believe that at the time the funds are allocated to the employee or their beneficiaries, those funds become earnings on which PAYE and NICs are due and should be accounted for by the employer".

113. As Mr Finch explained in evidence this was something made available throughout HMRC via the intranet. This was perhaps therefore the sort of thing which the hypothetical inspector would have been aware of, or would have been expected to make himself aware of once the EBT was mentioned.

114. Mr Mullan therefore argued that the combination of the existence of the SRNs, at least in the 2009-10 return, and Spotlight 5, indicating HMRC's concerns with loans made via a trust, should have been sufficient to alert the hypothetical officer to a possible insufficiency of tax. However, according to Patten LJ in *Sanderson*:

> "The purpose of the condition is to test the adequacy of the taxpayer's disclosure, not to prescribe the circumstances which would justify the real officer in exercising the s.29(1) power."

115. These are all factors which indicate that something might be wrong and that perhaps the hypothetical officer should make further enquiries but, as Auld LJ said in *Langham v Veltema*:

> "… it is plain from the wording of the statutory test in section 29(5) that it is concerned, not with what an Inspector could reasonably have been expected to do, but with what he could have been reasonably expected to be aware of."

116. The mere inference that the officer should perhaps carry out further enquiries is not therefore sufficient. Something more is required to alert the hypothetical officer to the insufficiency of tax. I do not therefore consider that the level of disclosure in Mr Hoey's tax returns, even when combined with the information contained in Spotlight 5, is sufficient to prevent HMRC from raising a discovery assessment.

Summary re s29

117. In my view therefore:

> (1) HMRC made a valid discovery within the meaning of s29(1),
>
> (2) Mr Hoey did not complete his tax return in a manner in accordance with generally prevailing practice at that time, as required by s29(2),
>
> (3) The information provided in Mr Hoey's tax returns was not sufficient to alert the hypothetical reasonably competent officer to an insufficiency of tax so as to prohibit the making of an assessment under s29.

118. I therefore find that the assessments issued under s29 TMA in respect of 2008-09 and 2009-10 were validly made.

The PAYE Regulations

119. Ms Nathan, for HMRC, submitted that the FTT simply did not have any jurisdiction as regards the operation of the PAYE Regulations. She argued that the PAYE Regulations provide for a collection mechanism, but that liability to tax on employment income is fixed at an earlier stage, by different provisions, ss6, 7, 9, 11 and 13 ITEPA. In line with these provisions therefore, the "person liable" in respect of employment income is the employee and, in the view of HMRC, nothing in any other provision changes that incidence of the liability.

120. In support of this argument Ms Nathan referred me to *McCarthy v McCarthy & Stone plc* [2007] EWCA Civ 664, per the Chancellor at [42]:

> "42. As is well known the PAYE system is designed to recover tax due on income of an employee from its source, that is the employer, and in anticipation of the liability which arises at the end of the year of assessment in which it is paid. Accordingly it is hardly surprising that the PAYE regulations do not impose any liability on the employee. That is done by the primary legislation, namely ITEPA, to which I have referred, and the general machinery for collection contained in the Taxes Management Act 1970 ("TMA"), to which I now turn.
>
> 43. Part VI of TMA deals with "Payment of Tax". S.59A deals with payments on account of tax. It imposes the now familiar requirement to pay tax on 31st January and 31st July, the first of which is payable during the relevant year of assessment and the second only three months after its conclusion. It applies if in the previous year of assessment the tax on the income of the taxpayer from all sources exceeded the amount of tax deducted at source by a fraction to be prescribed by regulations. Thus a liability is imposed on a taxpayer in respect of his income in excess of that from which tax has been deducted at source. This section was referred to by Peter Smith J in paragraph 72 of his judgment as reinforcing the position that the Claimant "is liable to pay tax on his own earnings if it is not deducted".
>
> 44. The matter is put beyond doubt by the provisions of s.59B. That provides that the amount shown in a taxpayer's self-assessment under s.9 TMA for any year of assessment less (1) the aggregate of payments on account made by him under s.59A or otherwise in respect of that year and (2) any income tax deducted at source "shall be payable by him as mentioned in subsections (3) or (4) below". Those subsections deal with the time of payment by reference to notices given under ss. 7 or 8 TMA. But all of them recognise that the sums "payable by" the taxpayer are recoverable by the normal assessment procedures.
>
> 45. Counsel for the Claimant seeks to avoid what appear to me to be the obvious consequences of the legislative provisions to which I have referred on the grounds that s.59B is concerned with the mechanics of calculation of the liability, not its imposition. In one sense, of course, it is. It provides the mechanics for recovering the sums due in respect of the liabilities imposed by

> ITEPA in the provisions to which I have already referred. What it does not show is that an employee is not liable for tax on his employment income, including gains arising from the exercise of share options."

121. Mr Mullan, for Mr Hoey, contended that if the PAYE Regulations were operated in their normal manner, and HMRC had pursued the End Users for the PAYE which should have been deducted from Mr Hoey's earnings, then he would have been entitled to a tax "credit" in accordance with Regulation 185 of the PAYE Regulations.

122. However, Regulation 185 is expressed only to apply to ss59A and 59B. Regulation 185(6) provides for amounts which should have been deducted or accounted for to be "treated as deducted" for the purposes of ss59A(1) and 59B(1). This is apparent from the title of the provision and from Regulations 185(1)(a) and (b). Accordingly, Regulation 185 does not apply for the purposes of sections 8 and 9 TMA.

123. Section 59B is concerned with "payments of income tax/capital gains tax" in the case of assessments. This includes self-assessments. The difference between the figures at s59B(1)(a) and (b) is said to be "payable". Ms Nathan argued that this therefore was the amount to be paid, which she contrasted with the amount "chargeable" and the amount "payable" as those terms are described in s8(1AA) and s9(1) TMA.

124. She also emphasised the importance of the definition of "tax payable under the assessment" in Regulation 188(7), which expressly excludes deductions from, or credits against, the amount payable under the assessment.

125. She submitted that the "liability" and the amount "to be paid" are different concepts, which is confirmed by section 684(5) ITEPA, which preserves the employee's right of appeal to the tribunal, regardless of any provision under the PAYE Regulations. This, she says, reflects the fact that the PAYE Regulations do not disturb the liability to tax of the employee, imposed by the earlier provisions of ITEPA.

126. Not surprisingly this issue has been the subject of earlier judicial guidance and I was referred to *HMRC v Walker* [2016] UKUT 32 (TCC) at [39]:

> "It is, of course, correct that section 59B is not justiciable before the FTT, being concerned with matters of collection and enforcement."

127. Mr Mullan, however, referred me to a passage from the Upper Tribunal judgement in *R & J Birkett v HMRC* [2017] UKUT 89 (TCC). The relevant principles as to when public law issues might fall within the jurisdiction of the FTT are summarised at [30]:

> "(1) The FTT is a creature of statute. It was created by s3 of the Tribunals, Courts and Enforcement Act 2007 ("TCEA") "for the purpose of exercising the functions conferred on it under or by virtue of this Act or any other Act". Its

jurisdiction is therefore entirely statutory: *Hok* at [36], *Noor* at [25], *BT Trustees* at [133].

(2) The FTT has no judicial review jurisdiction. It has no inherent jurisdiction equivalent to that of the High Court, and no statutory jurisdiction equivalent to that of the UT (which has a limited jurisdiction to deal with certain judicial review claims under ss15 and 18 TCEA): *Hok* at [41]-[43], *Noor* at [25]-[29] and [33], *BT Trustees* at [143].

(3) But this does not mean that the FTT never has any jurisdiction to consider public law questions. A court or tribunal that has no judicial review jurisdiction may nevertheless have to decide questions of public law in the course of exercising the jurisdiction which it does have. In *Oxfam* at [68] Sales J gave as examples county courts, magistrates' courts and employment tribunals, none of which has a judicial review jurisdiction. In *Hok* at [52] the UT accepted that in certain cases where there was an issue whether a public body's actions had had the effect for which it argued – such as whether rent had been validly increased (*Wandsworth LBC v Winder* [1985] AC 461), or whether a compulsory purchase order had been vitiated (*Rhondda Cynon Taff BC v Watkins* [2003] 1 WLR 1864) – such issues could give rise to questions of public law for which judicial review was not the only remedy. In *Noor* at [73] the UT, similarly constituted, accepted that the tribunal (formerly the VAT Tribunal, now the FTT) would sometimes have to apply public law concepts, but characterised the cases that Sales J had referred to as those where a court had to determine a public law point either in the context of an issue which fell within its jurisdiction and had to be decided before that jurisdiction could be properly exercised, or in the context of whether it had jurisdiction in the first place.

(4) In each case therefore when assessing whether a particular public law point is one that the FTT can consider, it is necessary to consider the specific jurisdiction that the FTT is exercising, and whether the particular point that is sought to be raised is one that falls to the FTT to consider in either exercising that jurisdiction, or deciding whether it has jurisdiction.

(5) Since the FTT's jurisdiction is statutory, this is ultimately a question of statutory construction."

128. Having considered these submissions carefully I have come to the conclusion that not only does the FTT not have a general jurisdiction to consider matters of public law, and, in particular, the operation of the PAYE Regulations, but also that this is not a case where it is necessary for me to consider public law points in order to enable me to consider those issues which are properly within my jurisdiction. I cannot therefore venture into the question as to whether or not HMRC exercised any discretion they might have under s684(7A) correctly, legally or reasonably.

129. I am not however sure that this means that I cannot consider whether or not the discretion which HMRC claim to have exercised is genuinely what they say it is and,

given the importance this provision has in the context of this case, I believe I should address this point.

130. The PAYE Regulations contain a number of very specific provisions, notably Regulation 72 and Regulation 81, which permit HMRC to collect the tax due from the employee rather than the employer, but only in very specific circumstances. This does not therefore sit easily with s684(7A), which, reading the plain words, gives HMRC a very wide ranging discretion to disapply the PAYE Regulations in circumstances where they consider it "unnecessary or not appropriate" to pursue the employer.

131. Mr Mullan submitted that the general rule of construction was that the specific should over-ride the specific and that therefore s684(7A) should be given a much narrower interpretation than that argued for by HMRC. In support of this he referred me to the words of Lord Bingham in *R v Liverpool City Council, Ex p Baby Products Association* [1999] EWHC 832 (Admin), where he said that:

> "... power conferred in very general terms plainly cannot be relied on to defeat the intention of clear and particular statutory provision."

132. This statement is very clear. However, I am not considering here a situation in which the general power is designed "to defeat the intention of [a] clear and particular statutory provision." In this case the two provisions are overlapping. There is no conflict between them.

133. Mr Mullan also referred me to the words of Lord Wilberforce in *Vestey v IRC (Nos 1 and 2)* [1980] AC 1148 at 1172E-F:

> "Taxes are imposed upon subjects by Parliament. A citizen cannot be taxed unless he is designated in clear terms by a taxing Act as a taxpayer and the amount of his liability is clearly defined.
>
> A proposition that whether a subject is to be taxed or not, or, if he is, the amount of his liability, is to be decided (even though within a limit) by an administrative body represents a radical departure from constitutional principle. It may be that the revenue could persuade Parliament to enact such a proposition in such terms that the courts would have to give effect to it: but, unless it has done so, the courts, acting on constitutional principles, not only should not, but cannot, validate it."

134. Mr Mullan therefore argued that it was unconstitutional for the legislation to give such a wide ranging discretion to HMRC.

135. However, the situation in *Vestey* was very different. In that case the legislation lead to the conclusion that a number of people could be taxed on the same income, seemingly at the discretion of the Inland Revenue, which their Lordships rightly considered unconstitutional. This is not therefore, in my view, comparable to the situation in the current appeal. There is no question of double taxation in the current

appeal, there is simply the question as to who should pay an amount of tax which is properly chargeable. I do not therefore find *Vestey* directly helpful.

136. The position is further muddied by the wording of HMRC's Compliance Operational Guidance manual para [915255], which states:

> "The *Demibourne* case confirmed that:
>
> Where an employment relationship exists, the employer is responsible for deducting tax from payments made to the employee in accordance with the PAYE Regulations.
>
> **Prior to the amendment to the PAYE Regulations, HMRC did not have the discretion to choose whether to collect tax from the employer or the employee unless there had been a Direction to transfer PAYE to the employee under either Regulation 72 or Regulation 81 of the PAYE regulations**.
>
> An employee is entitled under Regulation 185 of the PAYE Regulations, to treat as deducted any tax that the employer was liable to deduct whether or not that tax was actually deducted. However the Regulation 185(5) credit is restricted so that an employee is not repaid any amount they didn't actually pay or have deducted.
>
> Unless there had been a direction to remove the PAYE obligation from the employer under either Regulation 72 or Regulation 81 of the PAYE Regulations, the employee was entitled to recover tax paid through SA, subject to time limits and HMRC could not refuse to repay on the grounds they had not recovered the tax from the employer.
>
> Regulations 72E to G were introduced following *Demibourne* to extend the circumstances where HMRC could make a direction to remove a PAYE liability from an employer and prevent an employee claiming credit for tax the employer failed to deduct."

137. When questioned as to the implications of this, Mr Finch said that he could not recall seeing this and in any case **it was wrong**. It was suggested by Ms Nathan that the reference to "Prior to the amendment to the PAYE Regulations …" also meant "Prior to the amendments to s684 …" which were introduced by the same legislation, and it was this reference which was wrong.

138. However, whatever the explanation of the wording of the HMRC Compliance Operational Guidance manual, I cannot escape the fact that the wording of s684(7A) seems to give a very wide discretion to HMRC and effectively renders Regulations 72 and 81 otiose. It may have been intended to provide additional discretion in situations which were not covered by Regs 72 and 81, and Mr Mullan did indeed suggest certain circumstances where this might be appropriate, but I can find nothing in the legislation which restricts the use of this discretion in this way.

139. I must therefore find that s684(7A) ITEPA does indeed give HMRC the discretion which they say it does and that I do not have the jurisdiction to interfere with whether or not that discretion was properly exercised.

The Transfer of Assets Abroad

140. Having decided in HMRC's favour as regards the discovery assessments and the operations of the PAYE Regulations, it is not strictly necessary for me to address whether or not Mr Hoey is also taxable under the TOAA legislation. However Ms Nathan encouraged me to do so on the basis that this might have wider application should my decision be appealed to the higher courts. I will therefore do so.

141. Ms Nathan submitted that Mr Hoey's entry into the employment contract with Penfolds and later Hamilton Trust constituted a transfer of assets by Mr Hoey to Penfolds/Hamilton.

142. The word "assets" is defined widely and, she argued, includes cash, property and rights. Therefore, by virtue of the entry into the employment contract under which the services of Mr Hoey were provided to the End Users, income in the form of fees from the End Users arose to Penfolds/Hamilton Trust (each of which was 'a person abroad' within the meaning of s.718 ITA), such that there was a relevant transfer within the meaning of s.716 ITA.

143. I cannot disagree with this basic analysis, and neither did Mr Mullan.

144. The questions to be addressed therefore are:

(1) Can Mr Hoey claim the protection of the motive defence, contained in s737 ITTOIA?

(2) What is the measure of the income of the person abroad which Mr Hoey might be said to enjoy?

(3) Does the EU Principle of the Right to Free Movement of Capital render the TOAA legislation inapplicable to the current appeal?

The Motive Defence

145. The legislation covering the motive defence is set out in s737 ITTOIA as above. The key provisions as regards this appeal are:

"(2) An individual is not liable to income tax under this Chapter for the tax year by reference to the relevant transactions if the individual satisfies an officer of Revenue and Customs—

(a) that Condition A is met, or

(b) in a case where Condition A is not met, that Condition B is met.

(2) Condition A is that it would not be reasonable to draw the conclusion, from all the circumstances of the case, that the purpose of avoiding liability to

taxation was the purpose, or one of the purposes, for which the relevant transactions or any of them were effected.

(3) Condition B is that—

(a) all the relevant transactions were genuine commercial transactions (see section 738), and

(b) it would not be reasonable to draw the conclusion, from all the circumstances of the case, that any one or more of those transactions was more than incidentally designed for the purpose of avoiding liability to taxation.

(4) In determining the purposes for which the relevant transactions or any of them were effected, the intentions and purposes of any person within subsection (6) are to be taken into account.

(5) A person is within this subsection if, whether or not for consideration, the person—

(a) designs or effects, or

(b) provides advice in relation to,

the relevant transactions or any of them."

146. Before I can address s737 therefore I need to address the meaning of tax avoidance. The most widely accepted definition of this controversial issue is perhaps that set out in *IRC v Willoughby* [1997] STC 995 by Lord Nolan:

> "The hallmark of tax avoidance is that the taxpayer reduces his liability to tax without incurring the economic consequences that Parliament intended to be suffered by any taxpayer qualifying for such reduction in his tax liability … Where the taxpayer's chosen course is seen upon examination to involve tax avoidance (as opposed to tax mitigation), it follows that tax avoidance must be at least one of the taxpayer's purposes in adopting that course, whether or not the taxpayer has formed the subjective motive of avoiding tax.
>
> My Lords, I am content for my part to adopt these propositions as a generally helpful approach to the elusive concept of 'tax avoidance', the more so since they owe much to the speeches of Lord Templeman and Lord Goff of Chieveley in Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes) … respectively …"

147. It was clear from Mr Hoey's evidence that **his** motive was purely the avoidance of the complexities of running his own company or his own consultancy. He had no idea that the arrangements involved tax avoidance or anything untoward. He had been put in touch with Penfolds by his intermediary, DMS, whom he trusted implicitly, and I cannot therefore conclude that **his** motivation was related to tax avoidance.

148. However, subsection (5) demands that I also need to examine the motives of anyone who "designs or effects or provides advice in relation to the relevant

transactions or any of them." This casts the net much wider, so I therefore need to address whether any of the arrangements fall within the definition of tax avoidance.

149. It is well established that there is no requirement for anyone to organise his commercial affairs so as to maximise his tax burden. It is therefore perfectly legitimate to organise commercial transactions in a way which minimises the tax burden. This was made clear by the House of Lords in *IRC v Brebner* [1967] 2 WLR 1001 where Lord Upjohn said:

> "My Lords, I would only conclude my judgment by saying, when the question of carrying out a genuine commercial transaction, as this was, is considered, the fact that there are two ways of carrying it out - one by paying the maximum amount of tax, the other by paying no, or much less, tax - it would be quite wrong as a necessary consequence to draw the inference that in adopting the latter course one of the main objects is, for the purposes of the section, avoidance of tax. No commercial man in his senses is going to carry out commercial transactions except upon the footing of paying the smallest amount of tax involved."

150. In my mind therefore, the question arises as to whether or not all the transactions were normal commercial transactions and whether all that was being done was the taxpayer, or at least his advisers, taking advantage of the opportunity to reduce tax in a way that **Parliament had intended**.

151. However, the intentions of Parliament are sometimes very difficult to discern. Indeed, the vast majority of modern tax avoidance practice involves taking advantage of the opportunities which the **wording** of the legislation affords, whether or not Parliament actually intended that outcome in the circumstances in question. I am therefore required to interpret the statutory provisions by reference to their intended purpose, although this still presents difficulties because it is not always clear what Parliament intended.

152. However, in this case, I cannot believe that Parliament intended that taxpayers should be able to set up off-shore employers who would make contributions to a trust which would then make loans to the employee, who did not expect to be required to repay the loans, and who would then be taxed on the notional benefit of receiving an interest-free loan rather than on the benefit of receiving the moneys in a form which was taxable as income.

153. I therefore regard the basic structure, of Contractors being employed by an umbrella company which then provides their services to the End Users, as being a perfectly reasonable commercial transaction. However, I regard the insertion of additional transactions, being the setting up of an umbrella company offshore, which makes payments to a trust, which then makes interest free loans to the Contractors, with the expectation that those loans are never repaid, as constituting tax avoidance.

154. I am not required to ignore those transactions in my analysis but, using a purposive analysis, I find that their purpose was the avoidance of tax in a way which Parliament did not intend.

155. Looking again at the provisions of s737(2) and (3) these subsections set out two conditions, which I will paraphrase for the sake of clarity:

> "(2) Condition A is that it would not be reasonable to draw the conclusion, that the purpose of avoiding liability to taxation was the purpose, or one of the purposes, for which the relevant transactions or any of them were effected.
>
> (3) Condition B is that—
>
> (a) all the relevant transactions were genuine commercial transactions (see section 738), and
>
> (b) it would not be reasonable to draw the conclusion, from all the circumstances of the case, that any one or more of those transactions was more than incidentally designed for the purpose of avoiding liability to taxation."

156. In my view, the transactions fail Condition A because I believe that the purpose of the interposed steps was indeed to avoid taxation in a way which Parliament did not intend. Therefore "one of the purposes" for which the relevant transaction were effected was the avoiding of a liability to taxation.

157. If Condition A is failed then I must examine Condition B.

158. Genuine Commercial Transactions is defined in s738 ITA as follows:

> **"738 Meaning of "commercial transaction"**
>
> (1) For the purposes of section 737, a relevant transaction is a commercial transaction only if it meets the conditions in subsections (2) and (3).
>
> (2) It must be effected—
>
> (a) in the course of a trade or business and for its purposes, or
>
> (b) with a view to setting up and commencing a trade or business and for its purposes.
>
> (3) It must not—
>
> (a) be on terms other than those that would have been made between persons not connected with each other dealing at arm's length, or
>
> (b) be a transaction that would not have been entered into between such persons so dealing.
>
> (4) For the purposes of subsection (2), making investments, managing them or making and managing them is a trade or business only so far as—
>
> (a) the person by whom it is done, and

(b) the person for whom it is done, are persons not connected with each other and are dealing at arm's length."

159. The transactions in question were indeed effected in the course of a trade being carried on by Penfolds/Hamilton, and were in my view transactions which were transactions which might have been entered into between persons not connected with each other, since they were in fact entered into between unconnected parties.

160. However, if I turn to Condition B(b) I must come to the conclusion that some of those transactions, specifically the interposition of a non-resident employer, a trust, and the making of loans from the trust, were "more than incidentally designed for the purpose of avoiding liability to taxation."

161. I therefore find that Mr Hoey cannot take advantage of the motive defence in s737.

Measurement of the Income of the Person Abroad

162. It was agreed between the parties that "income" for these purposes was the profits of the "person abroad", ie, Penfolds and Hamilton. I was however given no evidence as to the profits of either Penfolds or Hamilton, such as profit and loss accounts.

163. The evidence I was given suggests that the profit and loss account of Penfolds/Hamilton consisted of the receipt of fees from the intermediary in respect of Mr Hoey's services, which, according to the agreed statement of common facts, were received from DMS/Cascade net of the fees payable to the promotors and other facilitators, less the payments of salary to the Contractors and the funds contributed to the trusts.

164. Ms Nathan suggested that I should consider the fees payable to the promotors as being payments made by Penfolds/Hamilton, the deductibility of which might be in doubt because there was a duality of purpose. However, the agreed statement of common facts stated that these fees were deducted by DMS/Cascade before the Contractor fees were paid on to Penfolds/Hamilton. DMS/Cascade then presumably distributed the fees to the relevant parties. No arguments were advanced to me as to who actually paid these fees from the perspective of strict legal construction and my working assumption is that the fees were in fact paid, as a matter of legal construction, by Mr Hoey. The question of their deductibility from the point of view of Penfolds/Hamilton does not therefore arise.

165. From the information I have therefore the Profit and Loss account of Penfolds/Hamilton consists of the net fees received from DMS/Cascade less the salaries and the payments into the Trusts. There may have been a small amount of residual profit remaining in Penfolds/Hamilton but I have no evidence as to its existence or amount.

166. In arriving at the profits of Penfolds/Hamilton, I think it is not in dispute that the amounts paid by way of salary to the Contractors are valid deductions. The payments

into the Trusts are however potentially more controversial. I must therefore look to the judgement of Lord Hodge, in *RFC 2012*, which might indicate their true nature.

167. In *RFC 2012*, Lord Hodge, at [59], said:

> "Parliament in enacting legislation for the taxation of emoluments or earnings from employment has sought to tax remuneration paid in money or money's worth. No persuasive rationale has been advanced for excluding from the scope of this tax charge remuneration in the form of money which the employee agrees should be paid to a third party, or where he arranges or acquiesces in a transaction to that effect."

168. It is clear from these words that the payments made into the Trusts were nothing more or less than additional payments of salary. They therefore properly fall to be deducted in arriving at the "income" of Penfolds and Hamilton for the purposes of s721 ITA.

169. I therefore find that the income of Penfolds and Hamilton for these purposes was nil.

Application of EU Law

170. Again, as a consequence of my above findings, it is not strictly necessary for me to consider whether or not the TOAA legislation impinges on one of the four basic freedoms set out in the TFEU, such that its application might be considered incompatible with EU law.

171. Article 63 TFEU, which defines the concept of the free movement of capital, provides:

> "1. Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.
>
> 2. Within the framework of the provisions set out in this Chapter, all restrictions on payments between Member States and between Member States and third countries shall be prohibited."

I note that for these purposes the Isle of Man and Guernsey are third countries.

172. The other fundamental freedoms do not cover transfers to or from third countries and there was therefore some discussion as to which of the fundamental freedoms might be in point in this case. Ms Nathan argued that I should consider the TOAA legislation in the context of the free movement of labour or the freedom of establishment.

173. Any restrictions imposed by the TOAA legislation do not however place any restriction on where Mr Hoey might actually work, and therefore, the TOAA

provisions cannot in my view constitute an infringement of the free movement of labour.

174. The TOAA might be a restriction on the freedom of establishment, limiting where Penfolds or Hamilton might be set up, but in my view we are here concerned primarily with the transfer of assets to a person abroad, which I consider is properly a matter which falls into the ambit of the free movement of capital. Transfers to and from a third country are therefore in point.

175. I was referred to the case of *Fisher v HMRC* [2014] SFTD 1341 at [642-673] where the First-tier Tribunal considered the compatibility of the TOAA code with the provisions of the TFEU on freedom of establishment and free movement of capital. They concluded, at [673]:

> "673 Our conclusion is that the TOAA charge does restrict Anne Fisher's freedom of establishment (and by extension her free movement of capital) and that it breaches those freedoms in a way which lacks justification. Even if the breach of those freedoms were justified it is not proportionate to any legitimate justification of fighting tax avoidance as that concept is understood in European law."

176. This was of course a decision of the FTT and is not therefore binding on me but I find it very helpful.

177. My understanding of the approach to be adopted when considering the compatibility of UK law with a potential infringement of one of the four basic freedoms is:

> (1) To establish whether or not there is any discrimination inherent in the relevant UK law such as might restrict one of the four fundamental freedoms,
>
> (2) To ask if that discrimination is justified and proportionate, and, if not,
>
> (3) To ask if the EU law is applicable to the facts of the case in question.

178. It is clear that there is inherent discrimination in the provisions of the TOAA legislation. Had Mr Hoey transferred his employment to a company resident in the UK then this would not have triggered the provisions of the TOAA legislation, whereas, because he transferred his employment to a company or companies based in third countries, it did trigger the TOAA provisions. This was clearly a restriction on Mr Hoey's freedom to transfer his capital, in this context, his contract of employment.

179. The question then arises as to whether that discrimination is justified.

180. The declared aim of the TOAA legislation is that it is an anti-avoidance provision designed to prevent the transfer of UK taxable income abroad by transferring the asset which gives rise to that income.

181. Mr Mullan submitted that in considering whether or not the TOAA legislation was proportionate because it was designed to tackle tax avoidance, I should have

regard to the EU concept of tax avoidance, which was concerned with wholly artificial arrangements, not with the type of transaction under consideration in this case. However, Ms Nathan referred me to the case of *X Gmbh v Finanzamt Stuttgart – Korperschaften* (Case C-135/17), 26 February 2019, in which the CJEU held as follows:

> "[84] … in the context of the free movement of capital, the concept of 'wholly artificial arrangements' cannot necessarily be limited to merely the indications referred to in paragraphs 67 and 68 of the judgment of 12 September 2006, *Cadbury Schweppes and Cadbury Schweppes Overseas* (C-196/04, EU:C:544), that the establishment of a company does not reflect economic reality, since the artificial creation of the conditions required in order to escape taxation in a Member State improperly or enjoy a tax advantage in that Member State improperly can take several forms as regards cross-border movements of capital. Indeed, those indications may also amount to evidence of the existence of a wholly artificial arrangement for the purposes of applying the rules on the free movement of capital, in particular when it proves necessary to assess the commercial justification of acquiring shares in a company that does not pursue any economic activities of its own. **However, that concept is also capable of covering, in the context of the free movement of capital, any scheme which has as its primary objective or one of its primary objectives the artificial transfer of profits made by way of activities carried out in the territory of a Member State to third countries with a low tax rate.**"

182. It seems to me, therefore, in the context of this very recent case, that "the artificial transfer of profits made by way of activities carried out in the [UK] to third countries with a low tax rate" is very much the sort of anti-avoidance objective which the CJEU might have in mind.

183. In summary, I find that, although the TOAA legislation does infringe the principle of the free movement of capital, the TOAA legislation is a reasonable and proportionate response to achieve its objectives of preventing the transfer of income abroad from the UK. The principle of free movement of capital does not therefore, in my view, prevent the application of the TOAA legislation.

DECISION

184. In summary, I find that:

(1) The discovery assessments for 2008-09 and 2009-10 meet the conditions for a valid assessment under s29 TMA 1970. In particular:

(a) HMRC have shown that a valid discovery was made. (s29(1)).

(b) Mr Hoey's tax return was not submitted in line with the practice generally prevailing at the time as regards the submission of individual tax returns. (s29(2)).

(c) The information disclosed by Mr Hoey in his tax returns for the years in question was not sufficient to have alerted a hypothetical

reasonably competent inspector of taxes that there was an insufficiency of tax. (s29(5)).

(2) As regards the general discretion available to HMRC under s684(7A) ITEPA 2003 to disapply the PAYE Regulation:

(a) HMRC do possess this general discretion, and

(b) This tribunal does not have the jurisdiction to consider further the application of the PAYE Regulations or whether HMRC exercised their discretion under s684(7A) legally and properly.

(3) The provisions of the TOAA legislation do potentially apply to the amounts received by Mr Hoey. Specifically:

(a) The creation of the employment contracts between Mr Hoey and Penfolds/Hamilton constitute the transfer of an asset by Mr Hoey, a UK resident, to Penfolds/Hamilton, who were not resident in the UK, and therefore persons abroad.

(b) However, the amount of the "income" of Penfolds and Hamilton which was transferred to the person abroad was nil.

(c) Mr Hoey cannot claim the benefit of the motive test to avoid any charge under this legislation.

(d) The application of the TOAA legislation is potentially in contravention of EU law, in that it infringes the principle of the free movement of capital, but

(e) There is justification for the infringement on the basis that it is a proportionate response to the tax avoidance objective of the arrangements.

185. Therefore, subject to the amendment of the figures to remove any element of taxation of the benefit of receiving employer related interest free loans, this appeal is DISMISSED.

186. 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.

PHILIP GILLETT

TRIBUNAL JUDGE
RELEASE DATE: 29 JULY 2019