[2020] UKFTT 0064 (TC)

TC07560

INCOME TAX – interaction of TMA and ITA – HMRC's powers of enquiry – extensive – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2018/03931

BETWEEN

CHRISTOPHER J GRINYER **Appellant**

-and-

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

TRIBUNAL: JUDGE ANNE SCOTT
MEMBER JOHN WOODMAN

Sitting in public at Edinburgh on Tuesday 21 January 2020

Philip Simpson, QC, instructed by MHA Henderson Loggie, for the Appellant

Elizabeth Roxburgh of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

INTRODUCTION

1. The appeal is against a Closure Notice ("the Closure Notice") issued by the Respondents ("HMRC") on 20 October 2017 pursuant to Section 28A of the Taxes Management Act 1970 ("TMA") which concluded an enquiry into the Appellant's self-assessment tax return ("the Tax Return") for the tax year 2010/11.

2. The Closure Notice had the effect of removing:

   (i) The Appellant's claim for share loss relief of £401,362 in respect of shares held by the Appellant in a company with which this appeal is no longer concerned,

   (ii) The Appellant's claim for a share of a loss incurred by Elysian Fuels 3 LLP ("the LLP") a limited liability partnership of which the Appellant was a member,

   (iii) The Appellant's claim that £25,000 be set off against other income (or capital gains) for the 2010/11 tax year, and

   (iv) The Appellant's claim to carry forward the balance of the loss of £397,312.

3. As a result of the amendments made by the Closure Notice, the Closure Notice resulted in an increase of tax of £209,539.70.

4. The appeal to the Tribunal was set down for one reading day and three days for hearing. It was allocated as a complex case in terms of Rule 23 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ("the Rules").

5. In the course of the week before the hearing, the Appellant intimated that various Grounds of Appeal had been withdrawn and that the only Ground of Appeal on which the Appellant relies at this hearing is that it was not open to HMRC to amend the Tax Return by removing the entries by which the Appellant:

   (i) claimed £25,000 sideways loss relief against general income, and

   (ii) carried forward £397,312 of trade losses to subsequent tax years.

6. HMRC's grounds for removing those entries were that:

   (a) the LLP was not carrying on a trade, and, in the alternative

   (b) the LLP's trade was not carried on commercially.

7. Neither party advanced any argument, or adduced any evidence, on the trade, or not, of the LLP. We had no witness evidence.

8. By agreement the only issue before the Tribunal was whether the claim for loss relief (and carry forward of losses) could be refused in the absence of an enquiry into the LLP's partnership tax return ("the PTR").

9. In essence the Appellant argues that although the enquiry into the Tax Return was validly opened the only route whereby HMRC could raise those issues about the LLP's trade was by an enquiry into the PTR. HMRC disagree.

10. The parties lodged with the Tribunal a Statement of Agreed Facts to which was attached an Appendix including copies of the redacted PTR, the Tax Return, the letter opening the enquiry into the Tax Return and the Closure Notice.

The agreed facts

11. It is not disputed that:-

(1) In 2010/11 the Appellant was a member of the LLP.

(2) Pursuant to Sections 12AA and 12AB TMA the LLP submitted to HMRC a tax return including a partnership statement for the tax year 2010/11.

(3) That return recorded that the LLP had made a trading loss in the tax year 2010/11.

(4) In the partnership statement within the PTR the LLP recorded that the Appellant's share of that trading loss was £422,312 (in fact the PTR stated £422,314).

(5) Pursuant to Section 8 TMA the Appellant submitted the Tax Return for the tax year 2010/11 and that return included partnership pages relating to the LLP.

(6) HMRC did not open an enquiry into the PTR.

(7) HMRC did open an enquiry into the Tax Return on 3 August 2012.

(8) HMRC closed the enquiry by the Closure Notice dated 12 October 2017.

12. We do not know why there is a £2 difference between the partnership statement in the PTR and the Tax Return but it is not material.

13. There is no dispute between the parties that the maximum extent to which, if any, the Appellant could claim loss relief against general income in the tax year 2010/11 was £25,000. That is because in that year he had not been an active partner and had worked for less than 10 hours per week.

The relevant entries in the Tax Return

14. We observe that the uncontested entries in the Tax Return are:

(1) At Box 7 of the Partnership pages relating to the LLP, the Tax Return recorded that the Appellant's share of the LLP's trading loss for the tax year 2010/11 was £422,312,

(2) At Box 19 that the Appellant's adjusted loss was £422,312 as there were no adjustments to be made,

(3) At Box 20 the Appellant claimed loss relief of £25,000 against general income in the tax year 2010/11, and

(4) At Box 22 he carried forward the balance of £397,312 of unused trade losses to future tax years.

The Legislation

15. Although an LLP is a "body corporate" (Section 1(2) Limited Liability Partnership Act 2000 ("LLPA")) Section 863 of the Income Tax (Trading and Other Income) Act 2005 ("ITTOIA") provides that, for income tax purposes, an LLP carrying on a trade or business with a view to profit is treated as if it was a partnership.

16. A partnership does not have a separate legal personality for income tax purposes (Section 848 ITTOIA). For partnerships that are comprised of UK resident individual partners, Section 849 ITTOIA provides that the partnership profits are calculated as if the firm were a UK resident individual with the partnership's profits allocated to the partners in accordance with the partnership's profit sharing arrangements (Section 850 ITTOIA). Partnership trading

(including professions) profits must be computed in accordance with generally accepted accounting practice (Section 25 ITTOIA). In each tax year that the partnership trades, each partner's share of trading profits or losses is treated as profits or losses of a trade carried on by the partner alone (Section 852 ITTOIA).

Insofar as it is relevant to this appeal Section 8 TMA provides:

"**8 Personal return**

(1) For the purpose of establishing the amounts in which a person is chargeable to income tax and capital gains tax for a year of assessment, and the amount payable by him by way of income tax for that year, he may be required by a notice given to him by an officer of the Board—

(a) to make and deliver to the officer, on or before the day mentioned in subsection (1A) below, a return containing such information as may reasonably be required in pursuance of the notice, and

(b) to deliver with the return such accounts, statements and documents, relating to information contained in the return, as may reasonably be so required.

(1A) The day referred to in subsection (1) above is—

(a) the 31st January next following the year of assessment, or

(b) where the notice under this section is given after the 31st October next following the year, the last day of the period of three months beginning with the day on which the notice is given.

(1AA) For the purposes of subsection (1) above—

(a) the amounts in which a person is chargeable to income tax and capital gains tax are net amounts, that is to say, amounts which take into account any relief or allowance a claim for which is included in the return; and

(b) the amount payable by a person by way of income tax is the difference between the amount in which he is chargeable to income tax and the aggregate amount of any income tax deducted at source and any tax credits to which section 397(1) or 397A(1) of ITTOIA 2005 applies.

(1B) In the case of a person who carries on a trade, profession, or business in partnership with one or more other persons, a return under this section shall include each amount which, in any relevant statement, is stated to be equal to his share of any income, loss, tax, credit or charge for the period in respect of which the statement is made.

(1C) In subsection (1B) above "relevant statement" means a statement which, as respects the partnership, falls to be made under section 12AB of this Act for a period which includes, or includes any part of, the year of assessment or its basis period.

…

(2) Every return under this section shall include a declaration by the person making the return to the effect that the return is to the best of his knowledge correct and complete.

…".

17. Section 9 TMA provides that returns submitted under Section 8 TMA must contain a self-assessment of the amounts in respect of which an individual is chargeable to income tax and capital gains tax.

18. HMRC have the power to enquire into a tax return under Section 9A TMA. Section 9A(3) reads: "A return which has been the subject matter of one notice of enquiry may not be the subject of another, except one … under section 9ZA of this Act".

19. Section 9A(4) reads:

"An enquiry extends to-

(a) anything contained in the return, or required to be contained in the return, including any claim or election included in the return….".

20. Such an enquiry is completed by the issue of a Closure Notice under Section 28A TMA which provides, so far as relevant:

"**28A Completion of enquiry into personal or trustee return**

(1) An enquiry under section 9A(1) of this Act is completed when an officer of the Board by notice (a 'closure notice') informs the taxpayer that he has completed his enquiries and states his conclusions.

In this section 'the taxpayer' means the person to whom notice of enquiry was given.

(2) A closure notice must either—

(a) state that in the officer's opinion no amendment of the return is required, or

(b) make the amendments of the return required to give effect to his conclusions.

(3) A closure notice takes effect when it is issued."

21. Under Section 12AA TMA an officer of HMRC may issue a notice to a partner (the recipient being one identified in accordance with the rules accompanying the notice) requiring the submission of a partnership return. The partnership return must contain a partnership statement setting out the profits of the partnership as well as the amount of profits allocated to each partner (Section 12AB TMA).

22. HMRC may enquire into the partnership return under Section 12AC TMA.

23. Section 12AC(3) reads: "A return which has been the subject matter of one notice of enquiry may not be the subject of another, except one … under section 12ABA of this Act".

24. Section 12AC(4) reads: "An enquiry extends to anything contained in the return, or required to be contained in the return, including any claim or election included in the return….".

25. Section 12AC(6) reads:

"(6) The giving of notice of enquiry under subsection (1) above at any time shall be deemed to include the giving of notice of enquiry—

(a) under section 9A(1) of this Act to each partner who at that time has made a return under sections 8 or 8A of this Act or at any subsequent time makes such a return, or

(b) under paragraph 24 of Schedule 18 to the Finance Act 1998 to each partner who at that time has made a company tax return or at any subsequent time makes such a return."

26. Such an enquiry may be closed under Section 28B TMA which provides:

"**28B Completion of enquiry into partnership return**

(1) An enquiry under section 12AC(1) of this Act is completed when an officer of the Board by notice (a 'closure notice') informs the taxpayer that he has completed his enquiries and states his conclusions.

In this section 'the taxpayer' means the person to whom notice of enquiry was given or his successor.

(2) A closure notice must either—

(a) state that in the officer's opinion no amendment of the return is required, or

(b) make the amendments of the return required to give effect to his conclusions.

(3) A closure notice takes effect when it is issued.

(4) Where a partnership return is amended under subsection (2) above, the officer shall by notice to each of the partners amend—

(a) the partner's return under sections 8 or 8A of this Act, or

(b) the partner's company tax return,

so as to give effect to the amendments of the partnership return."

27. Insofar as they are relevant to this appeal Sections 64 and 66 of the Income Tax Act 2007 ("ITA") read:

> "**64 Deduction of losses from general income**
>
> (1) A person may make a claim for trade loss relief against general income if the person—
>
> (a) carries on a trade in a tax year, and
>
> (b) makes a loss in the trade in the tax year ('the loss-making year').
>
> …
>
> (8) …
>
> (b) sections 66 to 70 (restrictions on the relief), …
>
> **66 Restriction on relief unless trade is commercial**
>
> (1) Trade loss relief against general income for a loss made in a trade in a tax year is not available unless the trade is commercial.
>
> (2) The trade is commercial if it is carried on throughout the basis period for the tax year—
>
> (a) on a commercial basis, and
>
> (b) with a view to the realisation of profits of the trade.
>
> (3) If at any time a trade is carried on so as to afford a reasonable expectation of profit, it is treated as carried on at that time with a view to the realisation of profits."

General observations

28. It was indubitably incumbent on the Appellant to return the figure of £422,314 in Box 7 of the Tax Return. That does not fall to be amended in the circumstances of this appeal. Since that loss was not adjusted the same figure should be found in Box 19.

29. The issue then is whether or not any part of that loss can be claimed and/or carried forward.

30. In order to claim loss relief against general income (and put an entry in Box 20) a taxpayer must satisfy the criteria set out in Sections 64 and 66 ITA.

31. After calculation of that loss, if any, then the balance of losses is inserted in Box 22.

32. If an enquiry is opened into either an individual's return or a partnership return, as can be seen, the provisions of Sections 9A(4) and 12AC(4) both provide that "An enquiry extends to **anything** contained in the return". It is we who have highlighted the word "anything" in bold. We agree with HMRC that that is very wide.

Overview of the Appellant's arguments

33. Mr Simpson very properly concedes that HMRC can open an enquiry into any entry in a return. However, he argues that it is the scope of that enquiry that is limited in that they cannot do so on the basis of certain types of challenge.

34. In summary, the Appellant's key point is that it is when the PTR is completed that the trading profit or loss is calculated. That is done by identifying the source of the income and the appropriate basis for calculation. Therefore the entry in the Tax Return presupposes that that figure is correct (hence Section 8(1B) TMA). Furthermore, since an LLP should be trading with a view to a profit[1] it must be on a commercial basis.

[1] Section 2 LLPA

35. It is only by opening an enquiry into the LLP that HMRC can open questions as to whether or not the LLP is in fact trading with a view to a profit. Since an enquiry into a partnership automatically opens an enquiry into the returns of the individual partners that is the appropriate route to adopt.

36. In the absence of an enquiry into the PTR, in respect of the Tax Return, HMRC is limited to identifying whether the entry at Box 7 (and in this case at Box 19) is indeed the amount identified in the partnership return. It cannot encompass the issues underlying that entry, such as whether or not the partnership was carrying on a trade. That would lead to incoherence between the PTR and the Tax Return.

37. The logical extension of that is that since the trading profit or loss has been quantified, the figures for losses and carried forward losses cannot be queried on the basis that there is no trade. The reality is that if one is trading then it is both commercial and with a view to a profit.

38. It is argued that there are good policy reasons for that approach not least as there would only be an enquiry into one return with consequent savings in time and expense.

39. Section 9A(3) TMA (one enquiry only) cannot be read literally in isolation because of the provisions of Sections 12AC and 28B TMA. The Appellant's Skeleton Argument referred to *Reid v HMRC*[2] ("Reid") but did not cite a particular passage.

Overview of HMRC's arguments

40. HMRC maintain that it is not necessary to undertake an enquiry in relation to a partnership in order to undertake an enquiry into the affairs of a partner in that partnership.

41. Amendments to an individual self-assessment tax return which denies interest relief or sideways loss relief can be made either:

(a) By closing a partnership enquiry; or

(b) By closing the individual enquiry under Section 28A(1) and (2) TMA.

42. There is nothing in Section 9A TMA to suggest that Parliament intended that an enquiry under that section could not consider an individual's right to set partnership losses against his other income. Section 9A(4) TMA is very wide in its terms.

43. It is for the Appellant to prove that he is entitled to claim the share of losses against general income and the burden of proof lies with him to establish that the requirements of Sections 64 and 66 ITA are met. Those sections would be otiose if the entry in the PTR, transposed into the Tax Return, was the beginning and end of the matter.

44. HMRC argue that there is nothing in TMA to support the restriction sought by the Appellant. The Appellant is conflating two issues, namely, how a partner's share of partnership profit and losses is determined, and when, and whether, a partner is entitled to set his share of partnership losses against general income.

Discussion

45. Rather than narrate our views on an enquiry into a partnership return, we prefer to adopt the reasoning of Judge Aleksander at paragraph 56 *et seq* in *Reid*[3] with which we agree and which reads:

> "56. As regards enquiries into partnership tax returns, a notice under s12AC opens the enquiry. It is a notice delivered to the nominated partner only. Notice is not given to the other partners, nor do those other partners

[2] 2018 UKFTT 236 (TC)
[3] [2018] UKFTT 236 (TC)

have any statutory right to be informed of the enquiry. A closure notice under s28B(1) closes the enquiry. This is delivered to the nominated partner only. Only if the self-assessment returns of the individual partners are amended is notice served on them – under s28B(4). This notice is not a closure notice – and cannot be construed as such. Its only effect is to address consequential amendments that need to be made to the individual's self-assessment tax return as a result of the closure of the partnership enquiry – and nothing more.

57. This interpretation is supported by the fact that individual partners have no right to be informed when an enquiry is opened into a partnership's tax return, nor are they necessarily notified of its closure (they will only be notified under s28B(4) if there are consequential amendments that need to be made to their individual self-assessment tax returns).

58. I also disagree with the Appellants' submissions that a deemed enquiry under s12AC(6) opens enquiries into all aspects of the tax returns of the partners for that year. I agree with HMRC that the deeming provision in s12A(6) is administrative convenience avoiding the need for actual notices of enquiry to be given to each of the individual partners – the deemed enquiry is effected solely for the purpose of allowing consequential amendments to be made to the partners' self-assessment tax returns arising out of the closure of the partnership enquiry.

59. I also disagree with the Appellants' submission that the existence of a deemed enquiry under s12AC(4) gives rise to a breach of s9A(3). This is because the deemed notice is not an actual notice of enquiry into the individual's return (the actual notice of enquiry was into the partnership's return). s9A(3) must be interpreted as referring only to actual enquires and not to deemed enquiries. To interpret these provisions otherwise would lead to absurd results. Consider, for example, an individual who is a partner of two different partnerships. If the Appellants' interpretation is correct, it would lead to the absurd situation that if HMRC opened an enquiry into one of the partnerships' returns, they would be precluded from opening an enquiry into the returns of the other.

60. Mr Sherry asked the question as to how the deemed enquiry opened under s12AC(6) was closed. The answer is that the actual enquiry into the partnership's return is closed by its own closure notice – but that there is no requirement for the partnership closure notice to be served on the individual partners. And there is a certain logic to this – as the individual partners are not served with the notice opening the enquiry into the partnership's return, they are not served with the partnership's closure notice. If there needs to be amendments to the self-assessment tax returns of the individual partners in consequence of the partnership enquiry, then those amendments are given effect by a notice under s28B(4)."

46. As can be seen, Sections 9A(3) and 12AC(3) are expressed in identical terms. In our view it would be equally absurd if an enquiry into the PTR were to be precluded simply because there was a valid enquiry into the Tax Return.

47. In this instance HMRC wished to enquire into other aspects of the Appellant's tax affairs and therefore an enquiry under Section 9A had to be opened.

48. Ms Roxburgh very pertinently pointed to the wording in Section 8(1B) which requires only that the figure to be returned is the "amount…stated" in the PTR. There is nothing to suggest that that figure is to be taken to be correct. Indeed, as can be seen from *Morgan v HMRC*[4] and *King v HMRC*[5] partners can and do challenge the accuracy of the figures in partnership returns.

49. Lord Hodge in *R(De Silva) v HMRC*[6] at paragraph 30 made it crystal clear that:

"HMRC may inquire into a return under section 8 or 8A if an officer gives notice of his intention to do so (section 9A(1)) and that enquiry may extend to anything contained in the return, or required to be contained in the return, including any claim: section 9A(4)."

[4] [2009] SFTD 160
[5] [2016] UKFTT 409 (TC)
[6] [2017] UKSC 74

We agree with HMRC that that means that although they cannot go beyond checking the accuracy of the figure in Boxes 7 and 19, since that figure must comply with the provisions of Section 8(1B), they can enquire into literally anything else including a claim for loss relief.

50. We were not referred to the case but we observe that Lord Carnworth in *R(Derry) v HMRC*[7] stated at paragraph 20: "TMA, as its title implies, is concerned principally with the management of the tax rather than fixing liability." In going on look closely at the relevant provisions of ITA he went on to say:

> "36. Having taken such care to walk the taxpayer through the process of giving effect to his entitlement as part of his tax liability for the year specified by him, it would seem extraordinary for that to be taken away, without any direct reference or signpost, by a provision in a relatively obscure Schedule of another statute concerned principally, not with liability, but with management of the tax….
>
> 37. Turning to the TMA, it is true that words of Schedule 1B taken on their own would be apt to apply to a claim under sections 132-133. However, I do not regard that as enough to displace the clear provisions of the ITA in respect of liability. I do not see this as turning so much on whether one set of provisions is more specific than the other, but rather on the fact that the ITA is in principle the governing statute in respect of tax liability, and as such should take precedence in the absence of any indication to the contrary."

51. It seems to us that that is absolutely in point in this instance.

52. The terms of Sections 64 and 66 ITA are crystal clear in their terms. If he seeks to utilise and carry forward losses it is indeed incumbent on the Appellant to establish that the trade that he is deemed to have carried on was indeed a trade on a commercial basis with a view to realisation of profit.

53. The administrative provisions of TMA cannot restrict or negate that. Indeed Parliament's intention when passing that legislation (and its predecessor provisions) was to make it clear precisely what was required in terms of establishing the right to loss relief.

54. We are not bound by Judge Jones at paragraphs 252 to 256 of *Martin v HMRC*[8] where he stated*:*

> "*(iii) Whether enquiry into GM LLP's return is a prerequisite for enquiry into the Appellant's 12/13 Return*
>
> 252. The Appellant asserts that the Enquiry Notice was invalid because HMRC failed to open an enquiry into the partnership return. This assertion is incorrect and is rejected.
>
> 253. An enquiry into GM LLP's 2012/13 tax return was not a prerequisite of opening an enquiry into the Appellant's 12/13 Return and making amendments denying his claim for relief arising from partnership losses pursuant to section 28A TMA 1970. This is for the simple reason that on a straightforward construction of the legislation, TMA 1970 sets out separate provisions for HMRC to enquire into, on the one hand, a personal tax return (section 9A TMA 1970), and, on the other hand, a partnership return (section 12AC TMA 1970).
>
> 254. This is not surprising. HMRC may take issue with a partner's return, but not with that of the partnership, for example because the claimed losses of the partnership are not in dispute, whereas HMRC wishes to enquire into the partner's entitlement to claim relief in respect of those losses. The fact that there may have been no enquiry into the partnership return of GM LLP may have been through mistake does not deprive HMRC of enquiring into the personal tax return.
>
> 255. Depending on the factual circumstances, it may of course make it harder for HMRC to resist a substantive challenge to any amendments to the personal tax return. It may be to the advantage of an appellant in an appeal against amendments to their personal return if sufficient evidence has not been acquired by HMRC to defend the basis to disallow losses through their lack of any partnership enquiry.

[7] [2019] UKSC 19
[8] [2019] UKFTT 710 (TC)

> 256. However, the Appellant did not seek to take advantage of this potential benefit in this appeal (until during the middle of the hearing at which time the Tribunal ruled he could not do so for the reasons set out above)."

55. Mr Simpson argued that that case could be distinguished on the basis that the taxpayer was unrepresented and the point was not fully argued. We disagree. Judge Jones clearly looked at and considered the legislation. We agree with his analysis.

56. Furthermore, we have heard full argument by experienced counsel and come to the same conclusion for the reasons that we have set out above.

Decision

57. For all these reasons the appeal is dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

58. 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.

ANNE SCOTT
TRIBUNAL JUDGE

RELEASE DATE: 03 FEBRUARY 2020