[2020] UKFTT 329 (TC)

TC07809

INCOME TAX – TERMINATION OF EMPLOYMENT – *Closure Notices — Errors - Validity - Compromise Agreement by which employment bonus retained – Whether a termination payment within Section 401 ITEPA 2003 – Correct year of earning - appeal dismissed*

Appeal number: TC/2019/05873 A/V

FIRST-TIER TRIBUNAL
TAX CHAMBER

Mr THIERRY LUCAS	**Appellant**
- and -	
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS	**Respondents**

TRIBUNAL: JUDGE JOHN MANUELL
Mrs SONIA GABLE

The hearing took place on 16 July 2020. The Tribunal heard the Appellant in person and Mr Max Simpson, Litigator, of HM Revenue and Customs' Solicitor's Office for the Respondents.

With the consent of the parties, the form of the hearing was by remote video link using the Tribunal video platform. The issues for the Tribunal were narrow and we decided a remote hearing was appropriate and so had granted the request. The documents to which we were referred consisted of the agreed bundle as prepared by HMRC in electronic form and served on the Appellant and the Tribunal.

The hearing was held in public and there was one observer.

DECISION

Introduction

1. The Appellant was employed by a large international bank between 1 November 2010 and 18 July 2012, when that employment was terminated by mutual agreement. This appeal concerns the tax treatment of the guaranteed bonus payment the Appellant received. He maintains that the payment falls to be treated as a termination payment. HMRC maintain that it falls to be taxed as income from his employment. HMRC's decisions, all dated 17 May 2019, which are under appeal are as follows:

Tax year	**Decision**	**Amount**
2014/15	Closure Notice	£1,864.40
2015/16	Closure Notice	£4,104.00
2016/17	Closure Notice	£7,799.20

2. HMRC accept that there are errors in the Closure Notices. They state that the Appellant's return showed that he was due to pay X and now shows that he is due to pay Y. In fact the Notices should state that the Appellant's return showed that he had *overpaid* X and now shows that he has *overpaid* Y. HMRC contend that the Notices are not rendered invalid by these mistakes, because section 114 of the Taxes Management Act 1970 ("TMA 1970") applies.

3. On 30 September 2015 HMRC wrote to the Appellant to notify him that an enquiry was being opened into his 2014 tax return. Correspondence and further enquiries followed and eventually the three Closure Notices under appeal were issued. It should be noted that the Appellant's personal tax affairs are complex and there have been various other matters in dispute between the Appellant and HMRC. Those other matters form no part of the present appeal.

The central issues

4. There were three main issues which required the Tribunal's decision, as follows:

(a) Whether the Closure Notices are valid despite their admitted errors.

(b) Whether the payments received by the Appellant are termination payments within section 401 Income Tax (Earnings and Pensions) Act 2003 ("ITEPA 2003") or are general earnings within section 62 ITEPA 2003.

(c) If the payments are general earnings under section 16 ITEPA 2003, whether they are for the year ending 5 April 2012, or for the year ending 5 April 2013.

The law

5. The main relevant legislation is ITEPA 2003:

Section 16 Meaning of earnings for a tax year

Section 62 Earnings

Section 401 Payments and Benefits on Termination of Employment

Section 413 Exception in certain cases of foreign service

TMA 1970 is also relevant:

Section 9A Notice of Enquiry

Section 29B Closure Notice

Section 50 Procedure

The key legislation is set out in the Appendix to this decision.

6. An appeal may be brought against any assessment which is not a self-assessment (section 31(1)(d) TMA 1970). If the appellant notifies the appeal to the Tribunal, the Tribunal is to decide the matter in question (section 49D TMA 1970).

The Appellant's case

7. The Appellant did not contend that his original SA returns were correct. His main contention was that the bonus payments received under the compromise agreement were termination payments within section 401 ITEPA 2003 and so qualify for full exemption under section 413 ITEPA 2003. The Appellant further contends that his entitlement to the payments stems from his signing the Compromise Agreement with his former employer on 23 April 2012.

The Respondent's case

8. HMRC contended, unsurprisingly, that the bonus payments were earnings from the Appellant's employment within section 62 ITEPA 2003. They were earned in October 2011, in accordance with his employment contract. Although the Appellant was initially informed by his employers that they intended to terminate his contract "for cause", subsequently agreement was reached that his employment would be terminated by mutual consent, as seen in the Compromise Agreement. That preserved the Appellant's bonus entitlement. The Compromise Agreement confirmed that the bonus earned in October 2011 would vest under the agreed schedule which did not alter its character as earnings from his employment. There was no new or additional payment as a result of the termination of the Appellant's employment. As the payments were of the bonus earned in October 2011, the payments are for the tax year ended 5 April 2012. As earnings, the payments qualify for Overseas Workday Relief ("OWR") to the extent that they related to duties performed overseas. The Appellant's workdays in that year should be used to calculate the level of OWR due.

9. The Closure Notices (as amended) were valid by reference to section 114 TMA 1970 and the appeal should be dismissed on all grounds.

Burden and standard of proof

10. The burden of proof lies on HMRC to show that the Closure Notices are valid. The standard of proof is the normal civil standard, the balance of probabilities. The burden of proof to show that the payments are termination payments within section 401 ITEPA 2003 lies on the Appellant to the same civil standard. It is also for the Appellant to show that the payments are for the year ended 5 April 2013, as he contended.

Evidence

11. A bundle of copy documents was served prior to the hearing by HMRC, incorporating the Appellant's documents, together with relevant authorities and legislation. The Tribunal will refer to specific documents as necessary below.

12. There was no dispute of fact as such and formal evidence was not required. The agreed facts are summarised at [1] to [3], above. The appeal turned on questions of law.

Submissions

13. Mr Simpson for HMRC relied on HMRC's Statement of Case, which has been summarised briefly above. The errors in the Closure Notices were not serious and had not prejudiced the Appellant in any way.

14. The Appellant relied on his Notice of Appeal and related correspondence.

Discussion

15. As noted above, the Appellant's income tax affairs are complex. He accepted that his 2013 return was erroneous. There was no suggestion of any dishonesty or carelessness on the Appellant's behalf. Some indication of the complexity of his tax affairs is seen in HMRC's difficulties in resolving the Appellant's tax liabilities and the time that process has taken.

16. The Appellant made no formal challenge to the validity of the three Closure Notices. Nevertheless the Tribunal has considered the validity issue independently as it is a fundamental point. The Tribunal finds that the Closure Notices are valid by virtue of the provisions of section 114 TMA 1970. HMRC's letter dated 16 May 2019 is strong evidence as it makes the correct tax calculations clear. The actual figures in the Closure Notices are correct: the mistake is limited to whether the sums are payments or repayments. Obviously, that is a significant difference and without HMRC's letter dated 16 May 2019 there would be much more doubt over the validity.

17. As to whether the payment falls within section 62 of ITEPA 2003, perhaps this issue need not be overcomplicated. The bonus, if it had been paid in the normal way in the course of the Appellant's continuing employment by the bank, would clearly and undoubtedly have been earnings from such employment. We find no merit in the Appellant's contention that a bonus is not "salary, wages or fee": ITEPA 2003 section 62(2)(a). If the bonus is not included in the term "salary", it certainly falls within section 62(2)(c) "anything else that constitutes an emolument of the employment".

18. Although the Appellant would have forfeited the valuable bonus if his employment had been terminated by the bank for cause, the plain fact is that the employment was not so terminated, because following brisk negotiations, the Appellant and his employer entered into the Compromise Agreement, which to an extent rewrote their recent history by mutual consent.

19. At the time the disciplinary action against him started, the Appellant had lost his entitlement to the bonus under paragraph 4.2.1 of the employment contract. However, he regained that entitlement by virtue of paragraph 2.3 of the Compromise Agreement. Paragraph 4.2.1 of the employment contract states that the guaranteed bonus is subject to "You not being subject to disciplinary action, including summary dismissal prior to the payment date". Possibly it is not entirely clear whether that paragraph would preclude payment of a bonus where there had been disciplinary action in the past, but such action had ceased. The punctuation suggests that the words "prior to the payment date" only apply to summary dismissal and not to the first part of the sentence, because there is no comma after "dismissal". But in any event, the Compromise Agreement is

effective to remove the “no disciplinary action” requirement, thus maintaining the Appellant’s previously accrued guaranteed bonus entitlement.

20. Because the Tribunal has found that the bonus payments fall squarely within section 62 of ITEPA 2003, there is no need for us to consider section 401.

21. The Tribunal does not consider that the fact that the Appellant in effect regained his entitlement to the bonus in the tax year 2012/13 means that the payments are for that year. The bonus was part of his remuneration for the year to October 2011 and a delay in payment and the risk of forfeiture do not change that. ITEPA 2003 section 16(2) puts that beyond doubt. The Appellant mentioned HMRC manual paragraph EIM40013. This sets out a view that HMRC took up to 2008, which was that earnings were for the year in which unfettered entitlement to them arose. The HMRC view now is set out from EIM40008 onwards. Earnings are assessed to tax in the tax year in which they are “received”. In this case the bonus was paid over a number of years and assessed to tax in those years. However the bonus was earned in October 2011 and so the payments were for the tax year ended 5 April 2012 and the OWR is to be applied accordingly.

22. The Appellant raised points about monetary value during submissions, but these do not assist his case because there is nothing for which monetary value has to be determined. He has perhaps become side-tracked by the term “money's worth” which appears in section 62(2)(b) ITEPA 2003, but the bonus payment does not fall to be taxed under that subsection. Here we are dealing with a fixed sum of £500,000. It was always contingent on certain conditions in the employment contract and the compensation plan being met. Latterly it was contingent on the signing of the Compromise Agreement, but the payment was always fully ascertainable, namely £500,000. The continued existence of a contingency, namely the Appellant not entering into employment with a competitor, did not create an occasion where a valuation was required. The existence of a condition does not make the payment unascertainable.

23. It is easy to see why the Appellant has regarded his Compromise Agreement with his former employer as a termination payment, because until the compromise was reached his bonus was lost. That is not, however, an interpretation the Tribunal is able to share. The Appellant himself accepted that he was paid nothing by way of compensation for loss of office. There is no such provision in the Compromise Agreement. Indeed, the correspondence from the negotiations disclosed by the Appellant states that in terms. The reality was that the Appellant was in a relatively weak position, and had to achieve the best deal he could, in which preserving his guaranteed employment bonus of £500,000 was an obvious objective.

24. Thus the Tribunal finds that HMRC has proved that the Closure Notices were valid despite the error (the first question) and that the Appellant has not proved his case on the other two questions.

25. The appeal is accordingly dismissed.

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.

TRIBUNAL JUDGE MANUELL

RELEASE DATE: 12 AUGUST 2020

APPENDIX

TMA 1970, Section 114

Want of form or errors not to invalidate assessments, etc.

(1) An assessment F1[or determination], warrant or other proceeding which purports to be made in pursuance of any provision of the Taxes Acts shall not be quashed, or deemed to be void or voidable, for want of form, or be affected by reason of a mistake, defect or omission therein, if the same is in substance and effect in conformity with or according to the intent and meaning of the Taxes Acts, and if the person or property charged or intended to be charged or affected thereby is designated therein according to common intent and understanding.

(2) An assessment F1[or determination] shall not be impeached or affected—

(a) by reason of a mistake therein as to—

(i) the name or surname of a person liable, or

(ii) the description of any profits or property, or

(iii) the amount of the tax charged, or

(b) by reason of any variance between the notice and the assessment F1[or determination].

ITEPA 2003, Section 62

Earnings

(1) This section explains what is meant by “earnings” in the employment income Parts.

(2) In those Parts “earnings”, in relation to an employment, means—

(a) any salary, wages or fee,

(b) any gratuity or other profit or incidental benefit of any kind obtained by the employee if it is money or money’s worth, or

(c) anything else that constitutes an emolument of the employment.

(3) For the purposes of subsection (2) “money’s worth” means something that is—

(a) of direct monetary value to the employee, or

(b) capable of being converted into money or something of direct monetary value to the employee.

(4) Subsection (1) does not affect the operation of statutory provisions that provide for amounts to be treated as earnings (and see section 721(7)).

ITEPA Section 401

Application of this Chapter

(1) This Chapter applies to payments and other benefits which are received directly or indirectly in consideration or in consequence of, or otherwise in connection with—

(a) the termination of a person’s employment,

(b) a change in the duties of a person’s employment, or

(c) a change in the earnings from a person’s employment,

by the person, or the person’s spouse [F1or civil partner], blood relative, dependant or personal representatives.

(2) Subsection (1) is subject to subsection (3) and sections 405 to [F2414A] (exceptions for certain payments and benefits).

(3) This Chapter does not apply to any payment or other benefit chargeable to income tax apart from this Chapter.

(4) For the purposes of this Chapter—

(a) a payment or other benefit which is provided on behalf of, or to the order of, the employee or former employee is treated as received by the employee or former employee, and

(b) in relation to a payment or other benefit—

(i) any reference to the employee or former employee is to the person mentioned in subsection (1), and

(ii) any reference to the employer or former employer is to be read accordingly.