Checking the power

Management of taxes

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Ross Birkbeck considers the effect of recent cases on Accelerated Payment Notices

Key Points

What is the issue?

The recent Court of Appeal decision in R(Rowe and others) v HMRC considered the conditions under which HMRC can issue APNs.

What does it mean to me?

The APN scheme gives HMRC substantial powers to demand a taxpayer's money before any legal determination that it is due. HMRC had taken a hard line on the matter, insisting that when a DOTAS registered scheme was involved there was virtually no procedural limitation on this power.

What can I take away?

The Court has substantially raised the bar that HMRC must meet before demanding payment of disputed tax up front. It will still be hard to resist an APN, but HMRC will no longer be able to be quite so dismissive of an attempt to do so.

The Court of Appeal's decision in *R (on the application of Rowe and Others) v HMRC* [2017] EWCA Civ 2105 finally offers some reassurance that the Revenue does not have completely free rein to demand a taxpayer's money before a dispute is resolved.

The taxpayer has spent a few years wondering if there was anything they could do. Since the Finance Act 2014 introduced the Accelerated Payment Notice (APN) scheme the Revenue has been able to demand, when certain conditions are met, the payment of disputed tax up front. The measures have often been called draconian on the basis that they appear to allow the government to demand payment in the absence of any legal determination that the payment is due.

Unsurprisingly the legislation was quickly challenged in court, where arguments were put that its application breaches fundamental principles of natural justice and human rights. Nonetheless, in 2015 and 2016, numerous High Court decisions have stated that the Revenue's powers to issue APN's were limited only by the express provisions of the scheme. It appeared that there was very little the taxpayer could do in the face of a notice.

Inevitably the issue has made its way to the Court of Appeal, which on 12 December 2017 handed down judgement in the joined appeal from the cases of *Rowe* and *Vital Nut*. Although the appeals were dismissed, the Court importantly rejected some

significant aspects of the High Court's interpretation of the APN scheme. It confirmed that officers of the Revenue have to show that any notices issued are properly considered and reasonable, and that the taxpayer must be given a meaningful opportunity to make representations before the notices are issued.

For the first time this establishes that taxpayers' rights go beyond the strict wording of the statutory scheme.

The APN regime

The stated aim of the APN regime, and its sibling the PPN (Partner Payment Notice) regime (which was actually the legislation in issue in *Rowe*) is to counter the economic advantage to taxpayers who take part in tax schemes that are later determined to fail. Absent the regime, a taxpayer mostly has the right to postpone paying disputed tax. So even in appeals that HMRC go on to win (some 80% of cases in 2010 to 2013 according to the *Budget 2014: policy costings (March 2014, HM Treasury)* report), they could gain a cash flow advantage from withholding tax during the often lengthy process of appeal to the First Tier Tribunal.

By issuing an APN the Revenue can demand that the cash is paid up front. Crucially, there is no right of appeal against it being so, and there are penalties for late payment. So where the gateway conditions are satisfied the taxpayer is firmly in the Revenue's hands.

The shifting of the financial burden in a dispute is not unique to the APN scheme. It is also seen, for example, in the interim payment, injunction, and security for costs regimes in CPR 25, all of which have the effect of saying to one of the parties in a dispute something along the lines of 'sorry, even though this case hasn't been proved against you, in the interests of balancing the prejudice to both parties you will have to pay this money now – don't worry we'll make it up to you when the case is resolved.'

Those regimes, however, are based on very broad criteria for the exercise of judicial discretion and a consideration of all the circumstances. And they are applied by the court, a neutral third party to the dispute. The APN system, on the other hand, appears to not only set a very low bar for the payment on account – a box ticking exercise, really – but to put the decision into the hands of one of the parties to the dispute: HMRC themselves.

And the Revenue clearly consider DOTAS registered schemes to be low hanging fruit when it comes to APNs. As the Court of Appeal noted in *Rowe*, HMRC took a policy decision to issue APNs/PPNs in all cases where the taxpayers had implemented a scheme on the DOTAS list. Given that the DOTAS regime was deliberately drafted widely to require disclosure it is not obviously an appropriate gatekeeper to powers targeting avoidance. At the heart of Rowe was a dispute as to whether such an un-questioning attitude by HMRC to the correlation between DOTAS and APNs was acceptable.

Rowe and *Vital Nut*

Rowe and *Vital Nut* were both lead cases, and in both APNs were issued on the back of DOTAS disclosures. *Rowe* involved film production investments that produced large losses in the first year, which could then be written off against other tax liabilities. *Vital Nut* considered corporations who had claimed for a deduction in corporation tax in relation to employer financed retirement benefit schemes.
Both claimants sought judicial review of the decisions to issue the notices. The decision of Mrs Justice Simler in *Rowe* was handed down in July 2015, dismissing the claims. In July the following year Mr Justice Charles followed suit, and Simler J's judgment, in *Vital Nut*. The claimants appealed.

In the Court of Appeal

In the joined appeals the Appellants between them argued essentially (as they had below) that HMRC should not be allowed to issue APNs/PPNs as a formality, nor in relation to schemes entered before the legislation came into effect; that issuing APN's was a substantive interference with their rights and that the Revenue could not make such a determination without good grounds; and that the Revenue's powers under the APN/PPN scheme needed to be interpreted restrictively as otherwise the provisions themselves were a breach of the claimant's right to justice.

The meat of the decision therefore concerned the interpretation of the provisions in regard to (i) their retrospectivity, (ii) the triggers activating the Revenue's power to issue notices, and (iii) the exercise of the Revenue's discretion in applying that power.

Purpose, interpretation, and retrospectivity

Looking at the essence of the legislation itself, Lady Justice Arden concluded emphatically that its purpose is not only to deter avoidance but also to shift the balance of power in tax disputes and deter taxpayers from dragging out disputes (despite it often being HMRC who do the dragging, as Charles J accepted it was in *Vital Nut*). Accordingly, it was not outside of the purpose of the legislation to effect schemes entered into before the legislation was passed. However it would be outside the purpose of the legislation – and an abuse of power – if HMRC were to use APNs/PPNs as an alternative to properly pursuing enquiries because they don't have the resources, time or inclination to properly deal with a dispute (see para 55).

Grounds for issuing

In *Vital Nut*, in the High Court, Charles J had found that when issuing an APN the officer had to conclude that he was not satisfied that the scheme was effective. At the appeal, the Revenue adopted this position, arguing that no positive view of the effectiveness of the scheme was required, and that their admitted procedure of issuing notices to all taxpayers engaged in a DOTAS registered scheme unless there was a 'slam dunk' case against doing so was legitimate.

The appellants argued that such a test reversed the burden of proof against the taxpayer, and that in order to issue an APN or PPN the Revenue needed a positive case for doing so.

Arden LJ agreed, concluding that the Charles J's test was 'more generous to the revenue than the statutory language permits' and that the designated officer must be 'positively satisfied on the information that he then has that the scheme is not effective' (para 62). As a result there must be a determination of the effectiveness of a scheme, based on evidence possessed by the Revenue, before an APN or PPN can be issued. Lord Justice McCombe concurred: there is a 'requirement for the designated officer to be positively satisfied that the scheme under consideration is not effective in the manner claimed by the taxpayer' (para 220).

Unfortunately for the taxpayers, the Court went on to decide that HMRC do in fact take sufficient steps to satisfy themselves of the ineffectiveness of any scheme before proceeding to issue APNs/PPNs. Arden LJ accepted that the multi-stage process which HMRC used to decide if a notice should be issued was sufficient and noted that there was no suggestion that it was not followed in this instance. Accordingly, she found that HMRC had formed a sufficiently positive view of the

scheme.

But whilst the Appellants were not successful on the facts, this new statement of the obligation on the Revenue, requiring them to form a positive view of the underlying case, is a substantive raising of the bar for issuing APNs. There now appears to be an opportunity to dispute the issuing of an APN if the multi-stage test is not substantively followed, or a positive conclusion that the scheme in question was ineffective is not reached.

Breach of natural justice

The Appellants also attacked the APN and PPN legislation on the grounds that it did not offer the taxpayer a chance to satisfy the designated officer as to the case being made against them, and was therefore a breach of the principles of natural justice. The existence of such a right (to fair trial) was not denied. The issue in dispute was the precise content of that right in the context of APNs and PPNs: was the taxpayer denied a real chance to argue that their scheme was effective (and so no notice should be issued)?

In the High Court in *Rowe*, Simler J appeared to endorse the Revenue's practice of only considering representations from the receivers of APNs that addressed either the issue of whether or not one of the gateway conditions for issuing a notice is met or the amount requested for payment.

Arden LJ disagreed. She concluded that there was a right to make representations regarding the effectiveness of the underlying scheme, and a right to know the grounds on which the taxpayer was considered liable (see para 111). Again she declined to decide that those rights were breached in this instance, since the taxpayers in fact knew the basis of their liability.

Nonetheless, this is potentially a highly important gloss on the legislation: it indicates that the Revenue has an obligation to engage fairly with a taxpayer regarding its case for issuing an APN before it does so, and that it will not be able to ignore submissions as to the broader case. Taken to its logical conclusion this could make treating APNs as a formality for DOTAS schemes a thing of the past, at least for proactive taxpayers willing to contend the issue by making substantive representations.

Human rights

Although McCombe LJ's consideration of the ECHR issues is lengthy his conclusions are short: the APN/PPN regime is a proportionate interference with a taxpayer's property, it is sufficiently clear, accessible and foreseeable in effect, and the reliance on the officer of the Revenue's discretion does not render the scheme arbitrary (even if, in accordance with Arden LJ's conclusions, the application of that discretion in any particular case does so).

Similarly, the Revenue were correct in their contention that the availability of a procedure for the making of representations against the issue of notices, backed by judicial review of any decision made, is sufficient to satisfy the requirements of ECHR Article 6.

So the Court was (unsurprisingly) not prepared to undermine the legitimacy of the legislation itself.

The designated officer

A final point dealt with by McCombe LJ related to the effect of an officer failing to reach a view of whether or not the scheme was effective. In *Vital Nut*, it was found that this was the case: the officer handling the dispute could not confidently be said to 'have reached the required independent view' that the scheme had failed. It might be assumed, therefore, that the APN was not properly issued. Unfortunately for the Appellants, the 2015 amendment to s 31 of the Senior Courts Act 1981 came to the rescue of the Revenue. Relying on subsection (2A), McCombe LJ considered that, if the designated officer had acted properly he would have come to the same conclusion. So this ground of appeal too was dismissed.

This point highlights the danger for the taxpayer of relying on the failures of individuals at HMRC as a defence against their conclusions when bringing a case in judicial review (although note that s31 does not apply to the tax tribunals).

Conclusions

Whilst not the outcome the Appellants were hoping for, or a repudiation of the APN/PPN scheme itself, the Court of Appeal has supplemented the statutory scheme in a way that means HMRC must meet further conditions when issuing an APN/PPN.

Most particularly, in addition to the express statutory requirements, the Revenue must:

- come to a conclusion, on the information available to HMRC, that the scheme in question is likely to be ineffective;
- consider representations, if made, regarding the substantive tax position of the taxpayer;
- not use APNs or PPNs as a replacement to making a proper assessment of tax due.

Although those conditions were met (or would have been) in these appeals, it by no means follows that this will be the case in relation to every APN. Where there is a suggestion that the Revenue has not properly considered the scheme in question, has ignored information provided, or has not followed its own processes properly, taxpayers have a right to require them do so. This may seem small comfort, but is significant nonetheless.