TAX LAW AND THE SUPREME COURT

By Nicola Shaw QC

It can sometimes seem as though tax law is an isolated dominium of special rules to which neither common sense nor ordinary legal principles apply. However, in *R (Ingenious Media Holdings plc) v Comrs for HM Revenue and Customs*,[1] the UK Supreme Court ('the Court') welcomed the general body of taxpayers into the bosom of the common law in an action concerning the duty of confidentiality owed by HM Revenue and Customs ('HMRC'). In tax law, that duty is enshrined in s 18(1) of the Commissioners for Revenue and Customs Act 2005 ('the CRCA 2005') but it is subject to s 18(2), which permits the disclosure of information for various purposes, including where the disclosure 'is made for the purposes of a function of [HMRC]' under s 18(2)(a) of the 2005 Act. The primary question that arose was whether the disclosure of information relating to the tax activities of Ingenious Media Holdings plc by HMRC to The Times newspaper was permitted 'for the purposes of a function of [HMRC]' within s 18(2)(a) of the CRCA 2005. The information had been disclosed by the Permanent Secretary for Tax, David Hartnett, during an 'off the record' meeting with two financial journalists, and was subsequently included in two articles published by the newspaper a week later. The reason for disclosing the information was said to be to promote good relations with the financial press in order to disseminate HMRC's position in relation to elaborate tax avoidance schemes.

Although an action against HMRC had been brought by way of an application for judicial review, crucially, the Court held that HMRC (and public bodies in general) 'are not immune from the ordinary application of the common law, including in this case the law of confidentiality.'[2] Thus, the question of whether HMRC had breached their duty of confidentiality did not fall to be decided simply by reference to public law remedies and principles, as the courts below had thought.[3] The proper approach of the court was not limited to an assessment of the rationality of HMRC's behaviour. The proper approach was to consider whether the disclosure of information amounted to a breach of the duty of confidentiality, applying established principles of law to its own judgment of the facts.[4]

Allowing the appeal, the Court held that the information disclosed was confidential in nature and subject to the duty of confidentiality contained within s 18(1) of the CRCA 2005[5] and, more importantly, that its disclosure was not 'for the purposes of a function of [HMRC]' within s 18(2)(a) of the 2005 Act.[6] The words in s 18(2)(a) could not be interpreted as meaning 'anything which in the view of HMRC is necessary or expedient or incidental or conducive to or in connection with the exercise of the functions of the collection and management of revenue',[7] as HMRC suggested, because if that was right then a number of the specific permissions contained in s 18(2) of the CRCA 2005 would be otiose. Furthermore, the effect of such a construction would be to undermine the principle of legality whereby 'fundamental rights cannot be overridden by general or ambiguous words.'[8]

A taxpayer's right to confidentiality is *a fortiori* because 'the whole system […] involves that […] matters relating to income tax are between the commissioners and the taxpayer concerned' and that the 'total confidentiality of assessments and of negotiations between individuals and the revenue is a vital element in the working of the system'.[9] As such, the general wording of s 18(2)(a) of the 2005 Act could not be taken to override that fundamental right. Rather, the provision was to be narrowly interpreted as an exception permitting disclosure to the extent reasonably necessary for HMRC to fulfil its primary function, of revenue collection and management.[10]

Furthermore, the disclosure of confidential information in the present case could not be justified by the desire to promote good relations with the financial press[11] nor by its divulgence 'off the record': 'an impermissible disclosure of confidential information is no less impermissible just because the information is passed on in confidence'.[12]

Comrs for HM Revenue and Customs v Volkswagen Financial Services (UK) Ltd[13] concerned the second of two issues arising in the context of a claim for repayment of VAT on overhead costs incurred by Volkswagen Financial Services (UK) Ltd ('VWFS'), a finance provider within the Volkswagen Group. The overheads in question were attributable to VWFS's hire purchase business, a business which made both taxable supplies of cars and exempt supplies of finance. The substantive issue concerned whether a proportion of the overhead costs was recoverable as a 'cost component' of the taxable supplies of cars notwithstanding the fact that the overheads were not incorporated within the price of the car, but rather were incorporated solely within the price of the finance. That issue was referred by the Court to the CJEU on 27 March 2017.[14] The second issue was a jurisdictional question concerning the nature of the First-tier Tribunal's function on an appeal against a decision rejecting a partial exemption special method ('PESM'). The contention of HMRC was that in approving the PESM proposed by the taxpayer, the First-tier Tribunal was required to decide whether that method produced a fair and reasonable result and not simply to approve it by default, having rejected the PESM proposed by HMRC as a method which was not fair and reasonable. In rejecting HMRC's contention, the Court held that the First-tier Tribunal's role was flexible. It was entitled to adopt an inquisitorial role if appropriate. Equally, it was entitled to assume, especially in a case such as this involving substantial litigants represented by experienced counsel, that the issues for determination were restricted to those identified by the parties.[15]

Comrs for HM Revenue and Customs v Investment Trust Companies (in liq)[16] is the latest in a long line of cases concerning the intersection between claims for repayment of overpaid tax and the law of restitution.[17] The novelty in this case was that it concerned indirect claims, that is to say claims brought not by the taxpayers but by those who had ultimately borne the burden of the overpaid tax. The claims in question were brought by certain investment trust companies to recover amounts of Value Added Tax ('VAT') paid on the supply to them of investment management services and accounted for to HMRC by the investment managers after deducting any input tax chargeable on the investment managers' costs. As it transpired, the services ought to have been treated as exempt from VAT and the investment managers were entitled, by way of a claim under s 80 of the Value Added Tax Act 1994 ('VATA 1994'), to repayment from HMRC of the VAT accounted. Those claims were subject to two restrictions: first, the claims were subject to the limitation period of three years contained in s 80(4) of the VATA 1994; and secondly, the amount of overpaid VAT was to be offset by any input tax credited to the investment managers pursuant to s 80(2A) of the 1994 Act.[18] As a result, the Investment Trust Companies brought claims in restitution against HMRC for the VAT paid by them to the investment managers to the extent that such amounts had not already been recovered by the investment managers under the statutory scheme.

In a nutshell, the Court dismissed the claims on the basis that HMRC were not enriched at the expense of the investment trust companies.[19] It is impossible to capture the intricacy of the Court's reasoning in a case note of this nature, but a pithy outline of the plot is achievable. The starting point in the Court's analysis is to identify the extent of HMRC's enrichment as being the net amount of the VAT accounted for to them by the investment managers and not the amounts of input tax deducted by the investment managers. The amounts of input tax could not be regarded as amounts which enriched HMRC because the claims to recover those amounts proceeded on the basis that the supplies were exempt and, thus, there was no obligation on the part of HMRC to allow any credit for input tax.[20] As to whether that enrichment had been at the expense of the investment trust companies, the Court considered that 'usually', for the enrichment of a defendant to be at the expense of the claimant the parties will have dealt with each other directly,[21] although there are exceptions, such as where the agent of one of the parties is interposed between them or where the claimant discharges a debt owed by the defendant to a third party.[22] Outside of those situations, where the defendant does not receive a benefit directly from the claimant it will be difficult to maintain that the defendant has been enriched at the claimant's expense.[23] Furthermore, the Court rejected an approach to the question of whether there was enrichment at the expense of the claimant based on 'economic or commercial reality' as too 'fuzzy' a concept.[24] Thus, the transfers of value from the Investment Trust Companies to the investment managers and the transfers of value from the investment managers to HMRC could not be collapsed into a single transfer of value from the Investment Trust Companies to HMRC.[25] The Investment Trust Companies' right of action in restitution lay not against HMRC but against the investment managers.[26] In addition, the Court also held that s 80 of the VATA 1994 was inconsistent with a concurrent non-statutory obligation on the part of HMRC to repay amounts of overpaid VAT and, therefore, excludes the possibility of a common law claim in restitution by consumers, who ultimately bear the burden of VAT, against HMRC.[27] Finally, the Court held that the inability of the Investment Trust Companies to pursue a direct claim in restitution against HMRC was not incompatible with EU law because they had a common law right to restitution of the amounts against the investment managers, notwithstanding the fact that the investment managers would have had a defence of change of position for any amounts which they could no longer recover from HMRC because of the three-year time limit.[28]

Moving on, tax avoidance schemes are a perennially recurring subject matter in the Court, producing some of the most exciting jurisprudential developments in tax law. However, this year's example, *RFC 2012 Plc (in liq) v Advocate General for Scotland*,[29] is something of a disappointment in that regard. The scheme in question concerned payments made by Rangers Football Club ('the Club') to an employees' remuneration trust ('the Trust') on behalf of its players. On recruitment, the player's contract of employment would set out the terms of the employment and the salary which would be paid subject to 'pay as you earn' ('PAYE') and national insurance contributions ('NIC'). In addition, the player received a side-letter from the Club undertaking that it would recommend to the Trust that the player be included as protector of a sub-trust and to fund the sub-trust with the amounts agreed in the recruitment negotiations. The Trust then made loans to the players of the amounts contributed to it on behalf of the player which were repayable out of the player's estate on death. The aim of the scheme was to avoid the PAYE and NIC liabilities which would otherwise be due on payments of earnings by an employer. The issue identified by the Court was 'whether an employee's remuneration is taxable as his or her emoluments or earnings when it is paid to a third party in circumstances in which the employee had no prior entitlement to receive it himself or herself.'[30] Regrettably, the Court did not analyse the logically prior question as to whether the amounts contributed by the Club to the Trust constitute remuneration from the employment at all – the judgment simply proceeds on an assumption that they do.[31] Instead, the Court focused on whether it is necessary for an employee to receive the remuneration in order for it to constitute taxable emoluments[32] and it concludes, without much difficulty, that it is not, because neither the statutory provisions themselves nor the overarching purpose of the legislation suggest any such limitation.[33] It is, after all, elementary that the earnings from employment are no less earnings because the employee requests or agrees for them to be paid to a third party instead of to the employee.

Finally, in *Comrs for HM Revenue and Customs v BPP Holdings Ltd*,[34] the Court considered a case management decision of the First-tier Tribunal debarring HMRC from defending an appeal against a decision concerning the taxpayers' liability to VAT. The decision is ultimately unique to its facts but the Judgment of the Court is of general relevance in two respects. First, the Court held that an appellate court could interfere with such a case management decision only 'if it could be shown that irrelevant material was taken into account, relevant material was ignored […], there had been a failure to apply the right principles, or if the decision was one which no reasonable tribunal could have reached.'[35] Secondly, the Court held that all tribunals and appellate courts, particularly in the field of tax where the law is the same throughout the UK, should be wary of applying or relying on the procedural jurisprudence on the Civil Procedure Rules ('CPR') without also taking into account the relevant rules of the Scottish and Northern Irish courts.[36] However, in the present case, concerning the application of time limits and sanctions, neither the Upper Tribunal nor the Court of Appeal could find any justification for adopting a more relaxed attitude to that adopted by the English courts under the CPR and it was not for the Court to interfere with that guidance.[37]

Endnotes

1. [2016] UKSC 54, [2016] 1 WLR 4164.
2. ibid [28] (Lord Toulson (with whom Lady Hale, Lord Mance, Lord Kerr and Lord Reed agreed)).

3. cf *R (Ingenious Media Holdings plc) v HM Revenue and Customs* [2015] EWCA Civ 173, [2015] WLR 3183; *R (Ingenious Media Holdings plc) v HM Revenue and Customs* [2013] EWHC 3258 (Admin), [2014] STC 673.
4. *Ingenious Media* (n 1) [26] and [29] (Lord Toulson (with whom Lady Hale, Lord Mance, Lord Kerr and Lord Reed agreed)).
5. ibid [32].
6. ibid [36].
7. ibid [19].
8. ibid [19], quoting *R v Secretary of State for the Home Office, ex p Simms* [2000] 2 AC 115, 131 (Lord Hoffmann).
9. *Ingenious Media* (n 1) [17], quoting *R v Inland Revenue Comrs, ex p National Federation of Self-Employed and Small Businesses Ltd* [1982] AC 617, 633 (Lord Wilberforce).
10. ibid [19] and [23].
11. ibid [34].
12. ibid [30]-[31].
13. [2017] UKSC 26, [2017] STC 824.
14. Case C-153/17.
15. *Volkswagen* (n 14) [7] (Lord Carnwath (with whom Lord Neuberger, Lord Kerr, Lord Reed and Lord Gill agreed)).
16. [2017] UKSC 29, [2017] 2 WLR 1200.
17. See eg *Woolwich Equitable Building Society v Inland Revenue Comrs* [1993] AC 70. See generally Steven Elliott, Birke Häcker and Charles Mitchell (eds), *Restitution of Overpaid Tax* (Hart Publishing 2013).
18. *Investment Trust Companies* (n 17) [12]-[13] (Lord Reed (with whom Lord Neuberger, Lord Mance, Lord Carnwath and Lord Hodge agreed)).
19. ibid [32]-[74], see also [25]-[31] (in which the Court found that HMRC was not enriched to the extent of an additional, ‘notional’ amount).
20. ibid [30]-[31].
21. ibid [46].
22. ibid [48]-[49]
23. ibid [51].
24. ibid [59]-[60].
25. ibid [71].

26. ibid [73].
27. ibid [86]-[88].
28. ibid [93]-[94]. See Value Added Tax Act, s 80(4); cf Limitation Act 1980, s 32(1)(c).
29. [2017] UKSC 45, [2017] 1 WLR 2767.
30. ibid [1] (Lord Hodge (with whom Lord Neuberger, Lady Hale, Lord Reed and Lord Carnwath agreed)).
31. ibid [23] and [61].
32. ibid [36].
33. ibid [37]-[41].
34. [2017] UKSC 55, [2017] 1 WLR 2945.
35. ibid [21] (Lord Neuberger (with whom Lord Clarke, Lord Sumption, Lord Reed and Lord Hodge agreed)).
36. ibid [23].
37. ibid [26].

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