



TC06544

Appeal number: TC/17/5032 and TC/17/5140

PROCEDURE – whether there should be a preliminary issue to determine validity of discovery assessment – not in this appeal - whether two appeals by same taxpayer arising out of same transaction but involving largely discrete issues should be joined – yes in these appeals

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

ARUNVILL GLOBAL EQUITY TRADING LIMITED Appellant

- and -

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

TRIBUNAL: JUDGE BARBARA MOSEDALE

Sitting in public at Taylor House, Roseberry Avenue, London on 22 May 2018

Ms N Shaw QC, for the Appellant

Mr D Yates, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. On 15 June 2017, the appellant lodged two notices of appeal with this Tribunal.
5 One was against a discovery assessment of HMRC dated 25 November 2016 that assessed the appellant to £226,658 in corporation tax and denied losses of approximately £1million and the other was against decisions (in the alternative) of HMRC dated 29 November 2016 which in total charged the appellant to approximately £16.5 million in income tax (but it is accepted that as the assessments
10 are alternative, the maximum amount in dispute under this second appeal is only about £6.5 million). I will refer to the former as the corporation tax, or CT, appeal, and the latter as the manufactured dividend, or MD, appeal.

2. On 21 July 2017, the Tribunal directed that, subject to any objection from the parties within 14 days, the two appeals would be case managed and heard together.
15 The appellant objected within 14 days. Those directions are therefore not in force. At the same time as objecting, the appellant applied for a new direction that there be a preliminary hearing in the CT appeal.

3. HMRC maintained the position that the appeals should be consolidated or joined, which effectively put them in the position of making an application for
20 joinder/consolidation (the earlier direction no longer being in force). Nevertheless, Mr Yates indicated that he was happy for Ms Shaw to speak first. HMRC opposed the appellant's application for a preliminary hearing.

Background to the appeals

4. The two appeals concerned exactly the same set of transactions. In or around 5
25 November 2012, the appellant company ('A') entered into two transactions with another group company, which was non-UK resident ('G'). G gave a cash loan to A. A gave a stock loan to G. G was required to pay A 'manufactured' dividends under the stock loan, but was entitled to reduce the amount of these manufactured dividends (up to 98%) by offsetting them against A's obligation to repay its loan to G. G
30 exercised its rights of offset.

5. The question is the legal effect of these arrangements. HMRC taxed the appellant to corporation tax on the basis it had not made the claimed losses, and to income tax on what HMRC saw as the full amount of the manufactured dividend. The parties were agreed that the legal issues in the two appeals were quite separate
35 bar one issue. That issue was whether the reverse charge on the receipt of manufactured dividends which the appellant was due to pay under s 923 Income Tax Act 2007 was to be assessed on the amount of manufactured dividend received as manufactured dividend, or whether it was to be taxed on the value of the amount received as manufactured dividend *plus* the amount by which the loan repayment was
40 reduced.

6. S 794 Corporation Tax Act 2010 was relevant to the CT assessment on the appellant and therefore relevant to the CT appeal: liability under s 794 depended on

the amount of income tax payable under s 923 Income Tax Act. To this extent, therefore, the issues in the two appeals overlapped: it might not be possible to determine the CT appeal until the MD appeal was determined.

5 7. Otherwise, as HMRC appeared to accept, the issues in the two appeals were different. The CT appeal, in contrast to the MD appeal, would raise the following issues:

- (a) Was A carrying on a trade?
- (b) Were the transactions a part of that trade?
- 10 (c) Was the expense incurred wholly and exclusively for the purpose of the trade (if any) or for the avoidance of tax (or, alternatively whether certain other provisions including s 794 Corporation Tax Act 2010 would bring the entire manufactured dividend into account)?;
- (d) Were A's accounts UK GAAP compliant?
- (e) Was the loan waiver a release under s 358 CTA?
- 15 (f) Were the loan debits disallowed under s 441 CTA?
- (g) Were the discovery assessments valid?

8. Apart from the s 923 point, the only other issue which arose in the MD appeal was the question of quantum of the assessments (HMRC having asked the Tribunal to increase the quantum of the assessments).

20 9. Whether the two appeals should be joined had the potential to be influenced by the outcome of the appellant's application for a preliminary hearing in the CT appeals. If that application succeeded, it might indicate the appeals should remain separate as the MD appeal would be held up while the CT preliminary issue was heard and finally determined. So I consider the application for a preliminary issue first.

25 **Application for preliminary issue**

10. The CT appeal is against a discovery assessment. The appellant has not conceded that the discovery assessment was validly made and it is therefore for HMRC to prove this. The appellant applied for the issue of whether the discovery assessment was validly made to be tried separately in advance to the issue of whether
30 the discovery assessment was right.

11. The parties were agreed that the question of whether the discovery was validly made involved three main questions (in paraphrase):

- (1) Was there a discovery by an HMRC officer of an (alleged) under-declaration (paragraph 41 of Sch 18 Finance Act 1998)? And if so:
- 35 (2) Was the (alleged) under-declaration brought about deliberately or carelessly? (para 43) Or, in the alternative,

(3) Could HMRC not have been reasonably expected to be aware of the under-declaration at the relevant time (para 44).

12. The parties were also agreed that the principles on when to order a preliminary issue were those set out in *Wrottesley* [2015] UKUT 637 (TCC) as follows:

(1) The matter should be approached on the basis that the power to deal with matters separately at a preliminary hearing should be exercised with caution and used sparingly.

(2) The power should only be exercised where there is a “succinct, knockout point” which will dispose of the case or an aspect of the case. In this context an aspect of the case would normally mean a separate issue rather than a point which is a step in the analysis in arriving at a conclusion on a single issue. In addition, if there is a risk that determination of the preliminary issue may prove to be irrelevant then the point is unlikely to be a “knockout” one.

(3) An aspect of the requirement that the point must be a succinct one is that it must be capable of being decided after a relatively short hearing (as compared to the rest of the case) and without significant delay. This is unlikely if (a) the issue cannot be entirely divorced from the evidence and submissions relevant to the rest of the case, or (b) if a substantial body of evidence will require to be considered. This point explains why preliminary questions will usually be points of law. The tribunal should be particularly cautious on matters of mixed fact and law.

(4) Regard should be had to whether there is any risk that determination of the preliminary issue could hinder the tribunal in arriving at a just result at a subsequent hearing of the remainder of the case. This is clearly more likely if the issues overlap in some way - (3)(a) above.

(5) Account should be taken of potential for overall delay, making allowance for the possibility of a separate appeal on the preliminary issue.

(6) The possibility that determination of the preliminary issue may result in there being no need for a further hearing should be considered.

(7) Consideration should be given to whether determination of the preliminary issue would significantly cut down the cost and time required for pre-trial preparation or for the trial itself, or whether it could in fact increase costs overall

(8) The tribunal should at all times have in mind the overall objective of the tribunal rules, namely to enable the tribunal to deal with cases fairly and justly.

(2), (3) and (6) *Succinct knockout point?*

13. Both parties were agreed that the question of whether the CT assessment was valid was a knockout point. If HMRC were unable to establish the validity of the discovery assessment, there would be no need for the rest of the CT appeal ever to be heard. That would save time and costs.

14. They were not agreed on whether the point was a succinct one. Ms Shaw took the view that a hearing on this would take one and a half days to two days, compared to the single hearing of both CT issues which she estimated would take six and a half to seven days. HMRC thought three days for the preliminary hearing was more likely. My view is that HMRC were more likely to be right: hearings concerning the validity of discovery assessments tended to be time intensive on factual evidence as well as legal issues.

15. Therefore, I would not describe the discovery issue as a ‘succinct’ point, however much it was a knockout point.

15 (3) & (4) *Is the evidence separate?*

16. While at first glance the evidence for the question of discovery would appear to be quite separate to the evidence concerned with whether the CT assessment was right, I was not convinced that it would not overlap. For instance, HMRC sought to show, for the purpose of the validity of the assessment, that the (alleged) under-declaration was careless; I was not convinced that evidence on that issue could be entirely divorced from the evidence which would surround the question of the appellant’s motive in doing what it did, which was an issue (see §7(c) above) to be determined when deciding whether the CT assessment was right. While these two points were quite different, the evidence was likely to overlap as it concerned the reason why various things were done or not done, and what the appellant should have understood.

17. A potential overlap in evidence meant that the Tribunal did not order a preliminary issue in *Addo* [2018] UKFTT 93 (TC). Ms Shaw did not think that the same concern arose in this appeal; but I agree with Mr Yates that there would be some overlap because a Tribunal dealing with the issue of whether paragraph 44 was satisfied (see §11(3) above) would have to understand how the scheme was intended to work in order to understand the parties’ cases on whether enough information was disclosed to HMRC at the relevant time from which they ought to have concluded there was an under-declaration to tax. Splitting the appeal would involve duplication of the Tribunal’s time.

18. In conclusion, I was concerned that the two aspects of the CT appeal could not be cleanly separated and a preliminary issue on one risked the later Tribunal having to re-hear evidence on the same matter.

(5) Overall delay?

19. The potential to save time and costs only existed if the question of whether the CT assessment was right was stayed behind the determination of whether the CT assessment was valid. A preliminary issue would therefore inevitably delay the
5 determination of whether the CT assessment was right, assuming that ever had to be decided.

20. The appellant considered the delay was justified by the potential to save costs: HMRC did not consider that it was. They pointed out that if the discovery point determination was appealed, the determination of whether the CT assessment was
10 valid might be delayed for years, with the evidence growing quite stale.

21. Ms Shaw did not consider that I should take into account the possibility of appeals from the FTT decisions: the future cannot be predicted. I considered, on the contrary, that I would be burying my head in the sand if I was to overlook the obvious
15 statistic that high value tax appeals involving complex points of law (such as discovery) are often appealed by the losing party. In any event, it was a factor that the Upper Tribunal in *Wrottesley* (see (5) at §12 above) said should be considered.

22. And I was concerned that ordering a preliminary issue would potentially result in years of delay in determination of the CT appeal in circumstances where it was a case involving a significant and complex factual dispute, which in an ideal world
20 should be heard as soon as compatible with proper preparation of the evidence.

23. While a minor point, I noted that both parties appeared to consider that one of the issues which would arise in the appeal on discovery was the whether the discovery was stale, and if so, whether it affected its validity. While there was Upper Tribunal
25 authority on the point, it was clearly a contentious issue and one that might result in a decision on discovery in this case being appealed to Court of Appeal level.

(7) Cost saving/increase

24. While success for the appellant in the preliminary issue would result in overall costs savings for both parties at least in the first instance, a successful appeal would probably result in the determination of the appeal as a whole being more expensive
30 (as involving two sets of hearings rather than one). This was only a minor consideration

Other considerations

25. There was some dispute between the parties over the impact of the Upper Tribunal decision in *Tooth* [2018] UKUT 18 (TCC). In that case, the Upper Tribunal
35 decided that the discovery assessment was invalid as HMRC had failed to prove that the taxpayer's (alleged) under-declaration was deliberate and because it was stale. Mr Yates point was that HMRC were seeking to appeal *Tooth* and so there was no rush to hear the validity of assessment point in this appeal, where a question of staleness also arose.

26. Ms Shaw's point was that if *Tooth* was relevant it suggested the entire appeal should be stayed pending the final determination of *Tooth*, although, as permission to appeal has not yet, and might never be, granted, she did not consider *Tooth* should impact on the determination of this interim application.

5 *Conclusion on preliminary issue*

27. I was not satisfied that a preliminary hearing was justified in the CT appeal: it was not enough that the validity of the discovery assessment had the potential to be a knock out point. Plenty of legal issues had that potential in an appeal: that did not by itself justify a separate hearing. Here the value of any potential cost saving was not as significant as it might be had the preliminary issued involved a pure point of law, as the discovery issue involved evidence likely to be very much in dispute, so the hearing was unlikely to be short. Moreover, a separate hearing of the discovery question was contra-indicated because of the risk of an appeal by the losing party significantly delaying the resolution of the underlying appeal, allowing the evidence in that appeal to go stale. I was also not entirely satisfied that there would be no overlap in relevant evidence. So far as the relevance of *Tooth* was concerned, Ms Shaw was, I think, right to say that it had no impact either way on the question of whether there should be a preliminary hearing; so far as a stay behind *Tooth* was concerned, neither party had applied for one and I would not prejudge any such application.

28. Taking all factors into account, I thought the balance of justice was to have the CT appeal as a single hearing. I refuse the application for a preliminary hearing.

A 'lite' preliminary hearing?

29. During the hearing, Ms Shaw canvassed the view that if I was not persuaded that there should be a preliminary issue of the full three issue concerning the validity of the assessment (see §11), I should order one to consider the 'lite' version (as she described it) being only the question of whether HMRC were within paragraph 41 of Sch 18 (the question of whether there was a 'discovery').

30. That issue alone had the potential to be a knock-out point. If HMRC did not succeed on paragraph 41, the question of whether they succeeded on paragraphs 43 and/or 44 became irrelevant. The appellant would win the entire CT appeal.

31. It was a more succinct point. So far as evidence was concerned, it would involve less evidence as issues of the appellant's alleged careless/deliberate behaviour would not arise, nor to a large extent questions of what HMRC should have known. Ms Shaw's view was that it would be largely a legal issue of whether the assessment was stale (in other words, made too long after the 'discovery'). The hearing might only take a day. The cost savings would be potentially more substantial than the full validity issue because, if the appellant won on the paragraph 41 'discovery' point, none of the rest of the appeal would need to be heard.

32. Moreover, the evidence was less likely to overlap with that of the rest of CT appeal and some of the concerns outlined in §16-18 did not apply. Nevertheless, any Tribunal hearing a preliminary issue on the paragraph 41 point would have to engage with the planning scheme to some extent to decide whether and when there was a discovery.

33. And the concerns with the risk of overall delay remained. The staleness point appeared still contentious and there was likely to be an appeal possibly to the Court of Appeal if HMRC sought to challenge the Upper Tribunal rulings on this (*Patullo* is binding on the FTT). That would lead to a delay on virtually all determinations of fact which needed to be made and a risk of stale evidence. The point at §24 also remained true.

Conclusion

34. The ‘lite’ preliminary hearing had more to recommend it than a preliminary hearing of the full validity issue, for the reasons explained above. Nevertheless, overall, taking into account that preliminary hearings should be ordered sparingly and with caution, I decided that it was preferable for the full appeal to be heard rather than for the paragraph 41 point to be heard as a preliminary issue, risking staleness of evidence in the rest of the appeal. While I recognised that that meant the potential saving from hearing a knock out point would be lost, my decision took account of the fact that this knockout point was (a) in an appeal concerning a significant sum of money and (b) involved at least one potentially contentious issue (staleness of discovery), such that the losing party was likely to appeal the FTT determination and therefore the ‘knock out’ point might well fail to give early and cheap determination of this appeal even if the appellant succeeded in the FTT.

Should these appeals be joined/consolidated?

35. The parties were again in general agreed on the legal principles to be considered in the application although were obviously not agreed on the outcome.

36. I was referred to the principles set out in *Maharani Restaurants* [1999] STC 295 which were summarised by the Upper Tribunal in *First Class Communications* [2014] UKUT 244 (TCC) as follows:

- (1) commonality of appellants;
- (2) commonality of witnesses;
- (3) degree of overlap of evidence;
- (4) risk of prejudice to the appellants in relation to the presentation of similar fact evidence;
- (5) avoiding the need for witnesses to give evidence more than once (and the risk that their evidence on the same point might be accepted in one appeal but not in another);
- (6) cost of holding more than one appeal or single consolidated appeal;

(7) length of hearing required for separate appeals and for single consolidated appeal; and

(8) listing and delay.

37. I deal with each in turn.

5 *(1) commonality of appellants*

38. The appellant in the two appeals is the same. This favours consolidation or joinder of the appeals but is far from decisive.

(2) Commonality of witnesses

10 39. The appellant's position, from which HMRC did not detract, was that there would be no overlap of witness evidence because the MD appeal essentially concerned a point of law and the relevant facts were either likely to be agreed before the hearing or the parties would rely on a few documents to establish them. The CT appeal, however, was likely to involve a lot of contested factual evidence concerning issues such as the purpose of the transactions.

15 40. It was likely there would be no commonality of witnesses.

(3) Overlap of evidence

20 41. There would be some overlap of evidence because at root of both appeals was the same transaction. The appellant's position was that the overlap would be more in the background to the appeals and the 'reading in' of that by the judicial panel, than in contested evidence at the hearing. Again, I did not understand HMRC to suggest that this view was wrong.

42. It was unlikely that the two appeals involved overlapping disputed evidence.

(4) Similar fact evidence

25 43. I was not addressed on this. The appellant plainly did not consider itself at risk on this point: its position was that there would be no disputed evidence in the income tax appeal and a great deal in the corporation tax appeal. Joining them would not create the risk of prejudice from similar fact evidence.

(5) Bringing the administration of justice into disrepute

30 44. In general, it would be inconvenient to witnesses to give the same evidence twice; moreover, having two separate hearings having to make decisions on the same factual issue risked inconsistent findings of fact and bringing the administration of justice into disrepute. But for the reasons given above, neither party suggested that duplicated fact finding was much of a risk here.

45. It did appear to me, and I think the parties agreed, that if the hearings were split, a separate judicial panel would have to hear each appeal to avoid the risk of bias inherent in having to make a finding of fact in the CT appeal on a matter which had already arisen for decision in the MD appeal. In any event, the appellant was keen to avoid listing difficulties which would ensue if the second hearing was restricted to the same judicial panel as the first.

(6) Costs

46. Neither party suggested that there would be significant cost implications of consolidating, or not consolidating, the appeals. This reflected the fact that they saw the issues as (largely) separate. The main saving in consolidation or joinder would be in the 'reading in' time for the judicial panel.

(7) Length of hearing

47. The appellant's position was that the income tax appeal raised a discrete issue which would require a separate hearing of half to one day, or extend the hearing of the corporation tax appeal by the same amount (bar the reading in time which would be saved). I did not understand HMRC to disagree.

(8) Listing and delay

48. It was really under this heading that the appellant objected to consolidation. Its point was that there was approximately £6.5million in dispute in the income tax appeal. While the tax was postponed pending the appeal, nevertheless the appellant was obliged by accounting rules to make provision for the potential tax liability in its accounts. It wanted the matter resolved sooner rather than later.

49. Its position was that the resolution of the income tax appeal would be delayed if it was consolidated with the corporation tax appeal, as the corporation tax appeal would take significantly longer to prepare. Extensive witness evidence would be served in the corporation tax appeal, but not in the income tax appeal; moreover the UK GAAP issue in the corporation tax appeal made it virtually inevitable that once the factual evidence was served, the parties would follow it with an exchange of expert opinion evidence. There was no need for any such evidence in the income tax appeal. The appellant's position was that the corporation tax appeal might take as much as a year longer to prepare for hearing than the income tax appeal. Moreover, the appellant reasonably expected it to be quicker to get a listing for a 1 day hearing rather than a multi-day hearing (as would be required if the two appeals were consolidated).

50. However, I was not persuaded that the time saving of keeping the appeals separate was likely to be as long as the appellant anticipated. The appellant assumed that the MD appeal would be quick to prepare for hearing as it did not anticipate a dispute on the relevant facts and I did not understand HMRC to disagree with this. Nevertheless, my experience was that it often took time for the parties to agree facts (no doubt as they want to be very careful not to commit themselves to a position they

will later regret), and if agreement on all the relevant facts could not be reached in the CT appeal, then there would need to be time for documents to be exchanged (and potentially a witness statement).

51. I did accept that it was likely that the MD appeal would be ready to be heard before the CT appeal if they were not joined.

52. But I was also concerned with whether, hearing the MD first, might ultimately lead to a stay of the CT appeal. Whatever the FTT determined in the substantive MD appeal, the amount of money concerned would make an appeal to the Upper Tribunal likely, particularly as the parties appeared agreed it turned on an arguable point of law. While the appellant contemplated preparing the CT appeal for hearing at the same time as the MD appeal, there was a possibility, because of the s 973 point, that the FTT would decide not to hear the CT appeal until the MD appeal was finally determined. A stay of the CT appeal would be unfortunate as the CT appeal was the one in which there was a significant factual dispute. This risk would be avoided if the appeals were heard together.

53. The final potential relevant factor in delay was the possibility of the CT appeal itself being delayed by a preliminary issue hearing. For this reason, I had considered the application for a preliminary issue before considering the application for consolidation/joinder. As I concluded (§28 and §34) not to order a preliminary hearing, this risk of delay would not arise.

Conclusion

54. The appellant did not ask for the CT appeal to be stayed pending determination of the MD appeal: it simply wanted the appeals to proceed separately because, if they did not, it reasonably anticipated that the MD appeal would take longer to be determined by the FTT than otherwise. However, I was not persuaded that the delay would be particularly long for the reasons given above.

55. HMRC wanted the appeals to be joined for the sake of convenience and I accept it would be more convenient to the Tribunal if only one judicial panel had to read into the factual background rather than two, and that, if they were not joined, reserving the second appeal to the same judicial panel would be unwise. It would also be convenient if the same hearing determined the s 923 point as the CT issues, in order to avoid the risk of a stay of the CT appeal while the s 923 point went on appeal.

56. Aside from these issues, there seemed to be no factors which pointed towards the appeals being joined, despite the fact that the appellant and transaction in issue was the same. Nevertheless, while taking into account the appellant's concerns with the financial impact of delay on its business, I considered the overall benefit of consolidation/joinder did outweigh the disadvantages.

57. My decision is that the two appeals should be consolidated. I DIRECT that they are so consolidated and both appeals shall in future be referred to by the single reference number TC/17/5032.

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.

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Barbara Mosedale

TRIBUNAL JUDGE
RELEASE DATE: 20 June 2018

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