



Neutral Citation: [2022] UKFTT 00156 (TC)

Case Number: TC08483

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

By remote video hearing

Appeal reference: TC/2019/05609
TC/2019/05611

INCOME TAX – discovery assessments – hedging product redress payment – taxable but not returned as such – white space disclosure – whether loss of tax caused carelessly by agent under s 29(4) TMA 1970 – yes – appeal dismissed

Heard on: 4 April 2022

Judgment date: 04 May 2022

Before

**TRIBUNAL JUDGE NIGEL POPPLEWELL
MR JOHN ROBINSON**

Between

**TIMOTHY JOHNSON
ALISON JOHNSON**

Appellants

and

THE COMMISSIONERS FOR HER MAJESTY’S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellants: Mr Andrew Green of Mayfield & Co

For the Respondents: Mr Charles Bradley of counsel, instructed by the General Counsel and Solicitor to HM Revenue and Custom

DECISION

INTRODUCTION

1. The appellants appeal against discovery assessments in respect of the tax year 2013/2014 issued on 5 and 6 November 2018 (the “**assessments**”). The original amounts of the assessments were reduced on review and are now agreed at £15,340.79 for the first appellant and £15,689.09 for the second appellant. The appellants had filed tax returns for that tax year. The sole issue is whether, as HMRC submit, a loss of tax was brought about carelessly by a person acting on the appellants behalf. It is agreed that if this is the case, then the assessments are valid, and the appellants do not dispute the amounts so assessed.

THE LAW

2. The legislation is not in dispute and is set out below.

3. Under Section 29 of the Taxes Management Act 1970 (“**TMA**”):

29. Assessment where loss of tax discovered

(1) If an officer of the Board or the Board discover, as regards any person (the taxpayer) and a year of assessment —

(a) that any income, unauthorised payments under section 208 of the Finance Act 2004 or surchargeable unauthorised payments under section 209 of that Act or relevant lump sum death benefit under section 217(2) of that Act which ought to have been assessed to income tax, or chargeable gains which ought to have been assessed to capital gains tax have not been assessed, or

(b) that an assessment to tax is or has become insufficient, or

(c) that any relief which has been given is or has become excessive,

the officer or, as the case may be, the Board may, subject to subsections (2) and (3) below, make an assessment in the amount, or the further amount, which ought in his or their opinion to be charged in order to make good to the Crown the loss of tax.

(2) Where—

(a) the taxpayer has made and delivered a return under section 8 or 8A of this Act in respect of the relevant year of assessment, and

(b) the situation mentioned in subsection (1) above is attributable to an error or mistake in the return as to the basis on which his liability ought to have been computed,

the taxpayer shall not be assessed under that subsection in respect of the year of assessment there mentioned if the return was in fact made on the basis or in accordance with the practice generally prevailing at the time when it was made.

(3) Where the taxpayer has made and delivered a return under section 8 or 8A of this Act in respect of the relevant year of assessment, he shall not be assessed under subsection (1) above—

(a) in respect of the year of assessment mentioned in that subsection; and

(b) in the same capacity as that in which he made and delivered the return,

unless one of the two conditions mentioned below is fulfilled.

(4) The first condition is that the situation mentioned in subsection (1) above was brought about carelessly or deliberately by the taxpayer or a person acting on his behalf.....

4. Under section 36 TMA:

36. Loss of tax brought about carelessly or deliberately etc

(1) An assessment on a person in a case involving a loss of income tax or capital gains tax brought about carelessly by the person may be made at any time not more than 6 years after the end of the year of assessment to which it relates (subject to subsection (1A) and any other provision of the Taxes Acts allowing a longer period).

5. Under section 118 TMA:

(4) For the purposes of this Act a loss of tax or a situation is brought about carelessly by a person if the person fails to take reasonable care to avoid bringing about that loss or situation.

THE EVIDENCE AND FINDINGS OF FACT

6. We were provided with a bundle of documents. Officer Stephen Boyd of HMRC tendered a witness statement and gave oral evidence for HMRC. Mr Andrew Green tendered a witness statement and gave oral evidence for the appellants. Mr Timothy Johnson tendered a witness statement which was taken as read. From this evidence we find the following:

(1) During the tax year 2013/2014, the appellants ran a dental practice through a company, Tim Johnson Dentistry Ltd. They also owned, in their own names, outside that company, a property which was rented out and from which they derived rental income.

(2) The tax return for that tax year for the first appellant declares total rents from property of £3,600 and loan interest and other financial costs of £1,234. The tax return for the second appellant for that tax year records total rents of £12,480 and loan interest and other financial costs of £5,931.

(3) Those tax returns had been completed by Mayfield & Co (“**Mayfield**”) acting through Mr Green as agent for the appellants. They were filed with HMRC on or around 26 January 2015.

(4) In 2007 the appellants had entered into a NatWest vanilla swap with a maturity date of 19 February 2017. Following a review by the Financial Conduct Authority of such interest rate hedging products, the appellants were awarded compensation by NatWest. The amount awarded was set out in a letter to the first appellant from NatWest dated 22 January 2014. It set

out the redress amount as being £100,214.64 with some additional interest for which tax has been deducted which resulted in a total redress payment of £101,245.27. This was then further broken down in a subsequent letter from NatWest to the first appellant dated 10 September 2014. That letter identifies a total sum of £86,347.88 as a refund of net amounts payable by the appellants on the original swap. Interest is identified at £18,509.24 against which tax has been deducted at 20%.

(5) On page 7 of the first appellants' 2014 tax return, there is a white space disclosure which reads "a compensation payment of GBP 43218 was received during the year from NatWest in respect of Interest Rate Hedging Products which is not considered to be taxable." An identical white space disclosure was made on the second appellants' 2014 tax return.

(6) On 26 January 2018, Officer Boyd notified the appellants that he would be conducting a check on their 2013/2014 tax returns. Having carried out a pre-opening case review, it was apparent to him that the redress payments which should have been included in the appellants' tax returns had not been so included.

(7) In extensive correspondence with Mayfield during the course of 2018, the taxability of those redress payments was discussed at length. This correspondence led, ultimately, to the issue of the assessments on 5 on 6 November 2018, and also to the imposition of carelessness penalties on both appellants which were subsequently reduced by 100%. The penalties were cancelled on review. The review also led to the reduction in the amounts set out in the original assessments. The conclusions of the reviews were set out in the review conclusion letters dated 30 July 2019.

(8) On 22 August 2019 the appellants appealed against the reviewed assessments.

(9) NatWest's letter of 22 January 2014 includes a paragraph entitled "tax" which states, inter alia, "..... You should include the gross interest and tax deducted figures together with the remaining balance of the redress payment in the accounts of your business and report this information to HM Revenue & Customs in either your own or your business' tax return as appropriate."

(10) HMRC had made guidance available on the gov.uk website as at 16 January 2015. This included three documents which Mr Green accepts were so available. The first, entitled "Advice for the Tax Treatment of Interest Rate Hedging Products Redress Payments" includes the statement "the redress will usually be paid out as a single payment that is taxable in the year it is received. This will mean that there is no need to amend your previous years tax returns. The payment is taxable because you would have previously claimed tax relief for the payments under the Interest Rate Hedging Product as an allowable business deduction. When the redress payments are made to you they must be treated as business income and reflected in your business accounts."

(11) The second document was entitled "Additional Guidance on Interest Rate Hedging Products (IRHP) redress payments" includes a heading "INDIVIDUALS" and under the heading "Why is this receipt taxable?" states that "the payment is taxable because the business would have previously claimed tax relief for the payments under the IRHP as an allowable business deduction against profits. When the redress payments are made to you they must therefore be treated as business income and reflected in your business accounts in accordance with applicable accounting standards."

(12) The final document which Mr Green accepts that he had reviewed at the time, which was published on 25 July 2014, was entitled: “IRHP: tax position on redress payments” It then goes on to say:

“If you have received one of these payments you will need to account for it in your tax return.

The full redress payment is generally taxable for individuals, companies and partnerships. This is because you will have claimed tax relief for the payments as an allowable business deduction. So the payment should be treated as business income and you should reflect it in the business accounts...

When completing your Self Assessment or Corporation Tax return you should account for the payment as follows:

basic redress and consequential losses-the payment should be shown as income in the section of the return where the product costs were originally deducted.....

There are certain circumstances where the tax treatment of the payment will be different and you may want to seek advice. For example

..... the product was for a non-business loan..... If this applies then the payment is not taxable as income.....”

(13) In his witness statement Mr Green stated that he is currently employed by Mayfield as a senior tax manager and has worked in taxation since 1988. Part of his role includes providing advice on tax payments and considering any unusual transactions. He had responsibility for preparing the 2014 tax returns for the appellants. As well as holding information about their affairs on his file, he was also in possession of NatWest’s letter of 10 September 2014 dealing with the redress payment. He was happy that the interest element was taxable but was not clear of the tax treatment of the redress payment. On 16 January 2015 he carried out an Internet search and read HMRC’s published guidance dated 25 July 2014 which suggested that if the product was for a non-business loan, then the payment was not taxable as income. Since the redress payment was made in the personal names of the appellants and was not in relation to their business, this suggested that the payment related to a non-business loan. That loan had been taken out to purchase the rental property which was sold on 30 April 2013. He, accordingly, thought that the payment related to compensation paid to the appellants and thus was not likely to be taxable. However, given the amount at stake, he made the white space disclosure.

(14) In cross examination Mr Green added that he accepted that the two other HMRC guidance documents were available on 16 January 2015. He probably did not know what the loan related to but could not be certain. He was uncertain as to the tax treatment. It is clear from HMRC’s guidance, looking at it in retrospect, that it probably does make clear that if the finance payments have been deducted against income, the redress payment was taxable. That, however, is with the benefit of hindsight and at the time there was considerable uncertainty. It was his view that the appellants did not have a business outside that which was run through the company He did not look into the detail of the redress payment and the facts relating to the redress payment. He knew that the appellants had rental income and deductions had been made from rental income for the finance costs relating to the hedging product. He knew therefore that there was rental income but did not equate business income with rental income. There was

therefore an ambiguity about the tax status of the redress payment which was the reason why he made the white space disclosure.

DISCUSSION

7. The burden of establishing that the assessment is a valid assessment rests with HMRC, and they must show that it is valid on the balance of probabilities.

8. Mr Bradley's position is straightforward. What is required is that an agent takes reasonable care to avoid an insufficiency or loss of tax and clearly an agent who read HMRC's guidance but then takes a different respectable technical review is not careless. That is not the situation here. Mr Green did not look at anything besides HMRC's guidance and Mayfield, acting through Mr Green failed to take reasonable care in submitting the return without having declared that the redress was taxable without having established even the most basic facts relating to the payment in question. Mr Green's evidence was ambiguous. It may be that he did not know that the payment related to the loan taken out to purchase the rental property. At another part of his evidence he had suggested he did not know that it related to that loan at all. But in either case, the reasonably competent tax adviser, against which Mr Green's advice must be tested, would have undertaken an investigation into the facts in order to establish whether HMRC's guidance (namely that the redress payment was taxable if it related to a business and the taxpayer had obtained a tax deduction for the finance costs of the product) applied to the appellants. This lack of reasonable care was causative of the loss of tax since had he undertaken the proper analysis, the appellants' tax returns would have included the redress payment as taxable income.

9. Mr Green submits that neither he nor Mayfield were careless. At the time there was considerable ambiguity regarding the taxability of redress payments. This is demonstrated by a number of decisions such as *Lovell*, *Wilkinson* and *Gadhavi*. HMRC encourage taxpayers to use white space disclosure which is an essential part of a tax return. The white space disclosure contained precise details of the amount of payment and its source. It complied with SP 1/06 in that it provides "enough information for an HMRC officer to realise within the enquiry period that the self-assessment is insufficient". HMRC should have read the white space disclosure and enquired into the return in which case the position would have been resolved. The loss of tax has been caused by HMRC's failure and not by his or Mayfield's. Their position was a reasonable one since they recognised that uncertainty existed and alerted HMRC to that uncertainty by the white space disclosure.

10. We have no doubt that Mr Green and Mayfield acted in good faith and that in Mr Green's mind there was ambiguity concerning the tax status of the redress payment. In our view, too, Mr Green was mistaken in his view that the redress payment was not taxable since it did not relate to a business carried on by the appellants. But simply because he acted in good faith and made a mistake does not mean that he took reasonable care. In our view Mayfield, acting through Mr Green, failed to take reasonable care when tested against the standard of a reasonably competent tax adviser.

11. Mr Green's evidence is not entirely consistent as to whether he knew that the loan had been taken out to purchase the property and that the redress payment related to the loan (on the one hand) and whether he could be certain as to whether the loan related to the purchase of the property (on the other). In our view it is more likely to be the former and we find that as a fact. In the 2013/2014 tax returns, rental income is returned as too are finance costs. It was clear to

Mr Green, therefore, that the two were related since otherwise we cannot see any justification for setting costs off against the income. We suspect that this happened in previous years.

12. Mr Green is an experienced tax adviser and thus would have known of the provisions of section 264 Income Tax (Trading and Other Income) Act 2005. This states that a person's UK property business consists of every business which the person carries on for generating income from land in the United Kingdom and every transaction which the person enters into for that purpose otherwise than in the course of such a business. Generating income from land includes exploiting land as a source of rents. It would have been apparent, therefore, to Mr Green that the receipt of rental income is treated as a UK property business. If he did not actually know this, as an experienced tax adviser, he should have done.

13. The HMRC guidance which Mr Green had read, namely that of 25 July 2014 makes it very clear that the redress payment should be treated as business income and reflected in the business accounts where tax relief for the payments has been claimed as an allowable business deduction. The other material available at that time on HMRC's website supports this.

14. So at the time Mr Green completed the appellants' tax returns, he knew that they were receiving rental income from the property and that rental income is treated as income of a business. He knew that the appellants had taken out a loan to purchase the property, and he had completed one if not more tax returns setting off the financing costs, including the costs of the swap, against the rent received from the property. He knew of HMRC's guidance that in these circumstances a redress payment should be treated as taxable business income and returned accordingly.

15. To our thinking, what brought about the loss of tax was the failure to return the redress payment as taxable income in the 2014 tax returns. If Mr Green and Mayfield had taken reasonable care, they would have realised that the redress payment was taxable and would have submitted the 2014 tax returns accordingly. Whilst we are sympathetic to Mr Green's submission that HMRC should have enquired into the return since they were on notice, by dint of the white space disclosure, that there was some doubt in Mr Green's mind as to the appropriate way in which the redress payment should be taxed, that has not caused the loss of tax. It is Mayfield's, and Mr Green's failure to take reasonable care in returning the redress payment as taxable income which has caused the loss.

16. We accept, too, that at the time, there may have been some ambiguity about the taxability of redress payments (having said that, given that symmetry is a fundamental tenet in taxation, and having received a deduction for the finance costs, an experienced tax adviser would, in our view, have thought it pretty likely that a compensation payment would be taxable) our sympathies lie with Mr Bradley's submission, namely that Mr Green failed to undertake an adequate fact find so that he was in a position to apply the law and guidance which he knew of, at the time. That shows a failure to take reasonable care, too.

17. Mr Green's submission that the white space disclosure provided enough information to HMRC, in accordance with SP1/06, for an officer to appreciate that the self-assessment in the appellants tax returns was insufficient is, with respect, misconceived. That statement is made in the context of the hypothetical officer posited in section 29(5) TMA. But not in the context of a careless agent which is relevant to section 29(4) TMA. And in any event, as we have said above, even if HMRC were on notice of the ambiguity and should have opened an enquiry within the enquiry window, their failure to do so was not the cause of the loss of tax. It was the

failure by Mayfield acting by Mr Green to properly return the redress payment as taxable in the 2014 tax returns which caused the loss of tax.

DECISION

18. For the foregoing reasons we dismiss these appeals.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

19. 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.

**NIGEL POPPLEWELL
TRIBUNAL JUDGE**

Release date: 04 MAY 2022