



TC05908

**Appeal numbers: TC/11/01065, TC/2012/04361, TC/11/05289, TC/11/05288 and
TC/11/04891**

*INCOME TAX AND NIC – tax avoidance schemes – whether alternative
assessments for different companies in schemes – no – whether Tribunal
has power to order HMRC to ‘set-off’ assessments for different taxes in
different companies –no- application refused*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

**JAMES H DONALD (DARVEL) LTD, GORDON DAVIES, Appellants
REGINALD DONALD & RICARDO TOGNERI**

- and -

**THE COMMISSIONERS FOR HER MAJESTY’S
REVENUE AND CUSTOMS Respondents**

TRIBUNAL: JUDGE ANNE SCOTT

Sitting at George House, 126 George Street, Edinburgh on Friday 5 May 2017

**For the Appellants: Philip Simpson, QC and Nicholas Davis, Solicitor;
For the Respondents: Duncan Tebbet and Barry Marriot, Officers of HMRC**

DECISION

Introduction and summary

1. After a hearing on conjoined appeals, a decision was issued by the First-tier Tribunal (“FTT”) on 3 June 2014. The judge in that Tribunal was Kenneth Mure QC
5 who has sadly died since then.

2. That decision was a decision in principle dealing with the effect of each of three arrangements known as “Plan 2”, “Plan 5” and “Plan 7” respectively. The appellants acknowledged that those were all devised as tax avoidance schemes.

3. The FTT decision had been a decision limited to those issues so there were
10 other matters outstanding in regard to the appeals. The only issue now remaining in contention is whether the first appellant should be, or indeed can be, given any credit for corporation tax paid by other participants in Plans 5 and 7 for the period when those plans were operating. Effectively the first appellant seeks a Direction from the FTT ordering HMRC to set that corporation tax off against the liabilities arising under
15 the assessments under appeal.

4. Since the FTT decision had been appealed, on 22 December 2014, the FTT referred that issue to the Upper Tribunal “to direct us on what is the appropriate course”. However the matter was not raised by the appellants at the Upper Tribunal hearing and unsurprisingly the decision of Lord Jones in the Upper Tribunal, which was
20 released on 5 October 2015, did not address that issue.

5. There had been three grounds of appeal and grounds 1 and 2 were dismissed. The third ground of appeal was remitted to the FTT to give further reasons for rejecting the appellant’s appeal in respect of Plan 2. The Supplementary Decision, released on 14 June 2016, which did so confirmed that it was not within that remit to
25 address the question of corporation tax.

6. On 10 January 2017 Judge Raghavan issued Directions that a hearing should be listed in Edinburgh to decide the following issues:-

“a. Whether the Tribunal has power to order HMRC to set off the Corporation Tax paid by
30 James H Donald Company Services Ltd and J H Donald Retail Limited against assessments and determinations on the J H Donald (Darvel) Ltd; and

b. If the Tribunal does have the power referred to in a) above, whether such Corporation Tax should be set off.”

The relevant parties and their connection with the tax avoidance schemes

5. Plan 5 was introduced in November 2000 and to implement it, J H Donald
35 Company Services Ltd (“Services”) was incorporated on 13 November 2000. Its shares were issued to James H Donald (Darvel) Ltd (“Darvel”), a private company limited by shares, the sole director of whom was Reginald Donald.

6. Plan 7 was introduced in October 2005 and another company, J H Donald Retail Ltd (“Retail”), which had been set up in 2002 and was owned initially by Reginald

Donald was utilised for Plan 7. In March 2006, and on a number of subsequent occasions, shares in Retail were allotted to individuals who were, or had been, employees of Darvel. Reedon Partnership LLP (“Reedon”) was incorporated as a limited liability partnership on 16 January 2006. In accordance with Plan 7 the individuals who were shareholders in Retail received dividends and also a profit share as members of Reedon.

The FTT’s decision

7. In regard to Plans 5 and 7 the FTT made the following Findings in Fact and Law which were upheld by the Upper Tribunal, namely:-

- 10 (i) Mr Reginald Donald was sole director of Darvel and solely responsible for the management and control of its business.
- (ii) Although Mr Donald was registered only as secretary of Services, he was its controlling mind.
- 15 (iii) Although he was registered only as secretary of Retail, he was its controlling mind.
- (iv) Notwithstanding its constitution, the real control of Reedon rested with Mr Donald.
- (v) Each of Services, Retail and Reedon did not act independently but merely as ciphers of Darvel and that under the *de facto* control of Mr Donald. The object was to facilitate the payment of wages/salaries to Darvel’s employees with a tax saving.
- 20 (vi) Notwithstanding Plan 5, the total sums received by the subscribers from Services, whether by way of wage or salary or dividend, represented emoluments of their employment with Darvel.
- 25 (vii) Notwithstanding Plan 7, the total sums received by the subscribers from Reedon, whether by way of profit share or dividend from Retail, represented emoluments of their employment with Darvel.
- (viii) Mr Donald’s intention in introducing each of the Plans was to secure tax and National Insurance Contribution (“NIC”) savings in Darvel’s business’ wage and salary bill.
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Implementation of Plans 5 and 7 and the consequences

8. Plan 5 operated such that employees’ contractual pay was replaced by earnings at National Minimum Wage rates. The difference between their pay net of PAYE and NIC according to their contractual rate and their net pay at National Minimum Wage rates was paid to the employee as a dividend from Services.

9. Plan 7 operated such that the employees who were members of Reedon were allocated profits which were less than their contractual rates of pay. Dividends were then awarded to bring the overall income entitlement to approximately the net amount they would otherwise have received had PAYE and NIC been applied to their contractual earnings.

10. The majority of the employees who used Plan 5 transferred to Plan 7 although two employees remained in Plan 5 until the end of 2006/07. Plan 7 continued until approximately the middle of August 2014.

5 11. As part of both Plans, Darvel entered into a number of partnership deeds with Services and a joint venture agreement with Reedon. Retail was a partner in Reedon and received a substantial share of the profits of that partnership.

12. In effect Darvel, Services and Retail acted on the basis that Plans 5 and 7 had the tax consequences that they were intended to have. Therefore Darvel's profits were calculated after deduction of all wages and profit share paid to Reedon and Services.
10 Retail and Services in turn paid corporation tax on all profits.

13. Services and Retail submitted self-assessment corporation tax returns, and paid the corporation tax in those assessments, on that basis. There is no dispute that Services paid in total £226,661.62 and that Retail paid £397,690.39.

14. In terms of Schedule 18, paragraph 48, Finance Act 1998, a copy of which is
15 annexed at Appendix I, it is not possible for those corporation tax assessments to be appealed to the Tribunal since they are self-assessments.

15. HMRC opened enquiries into Darvel's tax returns. Those enquiries were concluded with HMRC assessing Darvel as the employer of the participants in Plans 5 and 7. Assessments to recover unpaid PAYE were made under Regulation 80 of the
20 Income Tax (PAYE) Regulations 2003 and assessments to recover unpaid NIC were made under Section 8 Social Security Contributions and Benefits Act 1992. Those assessments were the subject matter of these appeals ("the Darvel assessments"). They have all been upheld in principle and the quantum agreed, subject to the outcome of this hearing.

25 16. HMRC had the power to open an enquiry into the corporation tax assessments for Services and Retail but chose not to do so.

The appellant's submissions

17. Although the first issue had been described as being the question of "set off" of corporation tax, Mr Simpson made it very clear that the issue was in fact whether the
30 corporation tax which had already been paid should be treated as a credit and that therefore the tax charged by the Darvel assessments should be limited to the difference between the total of those and the total of the corporation tax assessments.

18. That argument was predicated on the basis that the Darvel assessments and the corporation tax assessments were made on inconsistent, factual and legal bases and
35 are therefore alternative assessments. If they are alternative assessments then it is not open to HMRC to collect the sums charged by both sets of assessments.

19. Broadly the corporation tax assessments had been on the basis that Services and Retail had carried on trades. At the time they argued that they did. That is a question of fact. However, HMRC's argument, which was confirmed by the FTT and the

Upper Tribunal, was that those companies were not carrying on any trade or business and that money simply flowed through the companies which were ciphers or agents for Darvel.

5 20. Accordingly, the fact now is that there never was any trade in either company and therefore there can be no corporation tax liability. The money was at all times remuneration for the employees and therefore cannot be taxable receipts in Services or Retail.

10 21. Services and Retail received all payments from Darvel (in the case of Retail, via Reedon) as bare trustees (or agents or nominees) for Darvel and therefore none of the money should be treated as income assessable to tax in their hands.

22. Mr Simpson argues that “the inevitable consequence” is that the corporation tax paid to HMRC by Services and Retail was not corporation tax and was effectively paid by those companies to HMRC on behalf of Darvel since they were mere ciphers.

15 23. It was argued that HMRC can raise alternative assessments where a self-assessment return has been filed and they can then only collect tax under one of the assessments, whether self-assessment or their assessment.

20 24. The corporation tax has been paid so only the difference between the Darvel assessments and the corporation tax would be exigible. Therefore the Darvel assessments must be reduced by the amounts already paid by Services and Retail with effect from the date of those payments.

HMRC’s submissions

25 25. The Darvel assessments arose as a result of the failure by that company to meet its obligations under the Taxes Acts. Those obligations arose on Darvel as an employer and neither Services nor Retail were the employer.

26. The liabilities paid by Services and Retail arose from corporation tax obligations that they decided that they had incurred.

30 27. Neither Services nor Retail was an appellant in the Darvel appeals. No Tribunal has had any appeals from either Services or Retail and nor are there any appeals which could be heard by the Tribunal because the self-assessment returns are final and conclusive. They therefore cannot constitute alternative assessments.

28. Darvel would have no right to claim credit for tax paid by a legally separate company.

35 29. HMRC argue that the Darvel assessments were not raised as an alternative to the self-assessment corporation tax returns made by Services and Retail. For there to be alternative assessments, both or all would have to be raised by HMRC. Alternative assessments must be appealable and the self-assessment tax returns could not be appealed.

30. There is no legal basis which would allow HMRC to take into account for one taxpayer, amounts of tax paid by other legal entities.

31. The Tribunal's right to amend assessments is limited to that permitted in terms of Section 50 Taxes Management Act 1970.

5 **Discussion**

32. In essence Mr Simpson is arguing that it is unfair that, since the schemes did not work, Darvel should have to account for PAYE and NIC yet the tax that was paid as part of those schemes is also retained by HMRC. Effectively he argues that the corporation tax should now be re-characterised because HMRC's stance is inconsistent.

33. Of course, from one perspective, HMRC's approach does appear to be inconsistent when one looks at Darvel, Retail and Services together and in the round. However, Services and Retail have never been parties to these appeals or any other appeals. Frequently, in this Tribunal, we quite properly reject arguments from taxpayers that we should look at how HMRC have dealt with other taxpayers. To an extent that is what the appellant is asking me to do in this instance.

34. It is argued that HMRC cannot have their cake and eat it, in that they should not be able to assess Darvel for PAYE and NIC and still retain the corporation tax which Services and Retail self-assessed. However, even if I agreed with that proposition, what are the powers of this Tribunal?

35. HMRC correctly argue that the only assessments in issue in these appeals were the Darvel assessments. The Tribunal is a statutory body and the only statutory power to amend assessments is to be found in Sections 50(6) and (7) Taxes Management Act 1970. That reads as follows:-

25 "50 **Procedure**

(6) If, on an appeal to the Tribunal, the Tribunal decides ...

(c) that the appellant is overcharged by an assessment other than a self-assessment, the assessments or amounts shall be reduced accordingly, but otherwise the assessment or statement shall stand good.

30 (7) If on an appeal notified to the Tribunal the Tribunal decides ...

(c) that the appellant is undercharged by an assessment other than a self-assessment, the assessments or amounts shall be increased accordingly."

36. The self-assessment corporation tax assessments have never been appealed and most certainly are not the subject matter of these appeals. I fail to see how the validity of the self-assessed corporation tax returns for Services and Retail can be challenged in these proceedings because these proceedings solely concern the Darvel assessments.

37. Whilst I accept that Services and Retail were indeed ciphers for Darvel and had no substance, I do not accept that the payments of corporation tax were made as agents or bare trustees for Darvel. Those payments were deliberately made on the self-assessed profits that those companies declared.

5 38. Mr Simpson referred me to *AEI Group Ltd & Anr v HMRC*¹ (“AEI”) where the Tribunal stated that the case law establishes quite clearly that

“HMRC is entitled to issue alternative assessments in order to prevent loss of tax properly payable ... We see no reason why HMRC should not be entitled to conduct enquiries and require returns from several potential taxpayers in relation to the profits of the same business”.

10 39. That is perfectly correct but is of no application in this instance. His argument was that *AEI* was authority for the proposition that alternative assessments could be raised on multiple taxpayers. I disagree. It is authority for the proposition only that HMRC can seek returns to be made by more than one entity in relation to the same business where they are unclear as to who is conducting the business.

15 40. Self-assessment has been introduced since that time, but both parties relied on *Lord Advocate v McKenna*² (“McKenna”) and had very different arguments based thereon. In summary, in *McKenna* three assessments were made on each of the defenders as individuals and one on two defenders jointly and severally. A further assessment was made on a company operated by them. There was no dispute that
20 there was only one sum of income or gain relating to the same transaction in question and that all of the assessments related to that sum. The Court in the Outer House looked to Section 32(1) Taxes Management Act 1970 (“TMA”) which reads:

25 “(1) If on a claim made to the Board it appears to their satisfaction that a person has been assessed to tax more than once for the same cause and for the same chargeable period, they shall direct the whole, or such part of any assessment as appears to be an overcharge, to be vacated, and thereupon the same shall be vacated accordingly.”

41. The Court found that although Section 32 envisaged a situation where two assessments had been made for one cause, there is no express statutory provision allowing for assessments to be made in alternative form but having reviewed the
30 authorities the Court found that it is competent for HMRC to proceed by making alternative assessments. Lord Allanbridge in the Inner House in *McKenna* made it clear that where assessments are truly alternative then only one can be upheld on appeal.

42. The problem in this instance is that there is no appeal in regard to the self-
35 assessments by Services and Retail. It is only the quantum of the Darvel assessments that can be the subject matter of an appeal.

43. HMRC’s argument based on *McKenna* is that for assessments to be considered to be made in the alternative they must relate to the same transaction triggering either a

¹ 2015 UKFTT 290

² 1988 SLT 523 (Outer House) and 1989 STC 485 (Inner House)

source of income or gain and if tax was charged on one or more such assessment then there would be a danger of double taxation.

5 44. Mr Simpson disagreed arguing that *McKenna* was not concerned with double taxation but rather was authority for the proposition that there could be alternative assessments on different taxpayers where the same monies were involved and that that was the case in these appeals. One had to look at the face of the assessments and at the basis therefor and if they were not consistent then they must be alternative assessments.

10 45. Firstly, Lord Allanbridge made it clear in *McKenna* at page 489 at ‘e’ that assessments can be made on an alternative basis where there is a risk of double taxation.

46. Secondly, I have no doubt that it is of course competent for HMRC to make alternative and inconsistent assessments and on more than one entity, but that is not the position here. HMRC have raised only the Darvel assessments.

15 47. The Darvel assessments relate to monies paid (albeit indirectly) whether by way of wages or dividend. HMRC have quite properly allowed as a credit in the computation of the Darvel assessments, the income tax already accounted for in respect of the monies received by the employees by way of dividend.

20 48. It is undoubtedly the case that the Darvel assessments were raised on the basis that Darvel had not complied with its obligations in terms of the Taxes Acts to account for PAYE or NIC on the payments that were made to its employees. The PAYE is not a tax on Darvel. Rather the assessments were raised because Darvel had failed to account for the income tax that should have been deducted from the payments. Darvel’s obligation, like every other employer is to **collect** tax on their employee’s earnings (and sometimes some other small items of income) through the PAYE system for HMRC and then remit it to HMRC.

25 49. The whole sums paid out by Darvel were allowed as a deduction in its tax computation.

30 50. By contrast the corporation tax self-assessed by Services and Retail was tax payable on the profits that they declared to HMRC.

35 51. Although the funds effectively came from one “pot”, namely Darvel, I am not convinced that it can be viewed or treated as the same money. In diverting the money into Services, Retail and Reedon the structure of the transactions triggered different treatments for tax purposes. The funds acquired different characteristics as they moved through the various entities and that was entirely the choice of those entities, albeit directed by Mr Donald.

52. The key distinction with *McKenna* is that in that case it was a matter of agreement that the various assessments were mutually exclusive: tax was only **payable** on the same sum once.

53. Collection of PAYE and NIC on payments to employees is not an alternative to self-assessed corporation tax in another entity. They are not mutually exclusive. There is no double taxation on the same income.

5 54. Although Mr Simpson argues that he is simply seeking that the corporation tax paid be treated as a credit on the Darvel assessments, essentially he is arguing that the corporation tax assessments are invalid because there was no trade. That is not a matter for this Tribunal. In any event, although a self-assessment return cannot be appealed to this Tribunal, after the Upper Tribunal decision was issued, Retail would have been in time to argue that its profits had been over-stated in the return and seek
10 to amend the return under paragraph 15 Schedule 18 Finance Act 1998 or to seek relief under paragraph 51 of the same Schedule. No such action was taken.

15 55. One of the cases considered in *McKenna* was *Bye v Coren*³ and the question of unfairness and the allied point, which Mr Simpson raised, to the effect that Retail would not have utilised Schedule 18 Finance Act 1998 because it still believed that it had a trade, was addressed. Laughton LJ indicated that he could see no unfairness where alternative assessments were properly put forward. The taxpayers had a variety of routes by which they could avoid any problems of unfairness to them. He stated:

20 “The argument of counsel for the taxpayers was that Mr Coren could not in good conscience have appealed against the assessment ... because he had always accepted that the gains were capital gains ... What he could have done when he found himself presented with alternative assessments was to have appealed against both ...”.

56. Retail could have taken action arguing that although they disagreed with it, the decision in the Upper Tribunal was final. It did not.

25 57. I do not consider that the Darvel and self-assessments are alternative assessments. The latter were, and are, final and conclusive. This Tribunal has no jurisdiction to consider the self-assessment returns for Services and Retail.

58. HMRC referred me to *Greene King & Anr v HMRC*⁴ where, albeit obiter, Judge Bishopp said at paragraph 84:

30 “We are unimpressed with Mr Peacock’s argument that our conclusions on issues 2 and 3 might lead to double taxation. As we have said, the transactions were a device for ensuring that relief for payment was not matched by the taxation of the receipt; and the appellants had no evident difficulty with that outcome. It does not seem to us that they can legitimately complain if the scheme fails in its purpose and instead results in their paying tax twice.”

35 59. Although the facts in that case are completely different to the facts in this case, the principle remains exactly the same, that the appellants knowingly embarked on tax avoidance schemes and those schemes did not work.

³ 1986 STC 393

⁴ 2012 TC/02069 at paragraph 84

60. For all these reasons I find that the Tribunal has no power to order HMRC to set off or credit the corporation tax paid by Services and Retail against the Darvel assessments.

5 61. 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
10 “Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)” which accompanies and forms part of this decision notice.

ANNE SCOTT

TRIBUNAL JUDGE

RELEASE DATE: 25 MAY 2017

APPENDIX I

48—(1) An appeal may be brought against any assessment to tax on a company which is not a self-assessment.

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(2) Notice of appeal must be given—

(a) in writing;

(b) within 30 days after the notice of the assessment was issued,

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(c) to the officer of the Board by whom the notice of the assessment was given.