2 July 2021

PRESS SUMMARY

R (on the application of Haworth) (Respondent) v Commissioners for Her Majesty's Revenue and Customs (Appellant)
[2021] UKSC 25
On appeal from [2019] EWCA Civ 747

JUSTICES: Lord Briggs, Lady Arden, Lord Leggatt, Lord Stephens, Lady Rose

BACKGROUND TO THE APPEAL

This appeal concerns the interpretation of the follower notice regime contained in Part 4 of the Finance Act 2014 ("FA 2014"). The regime applies where HMRC contends that a tax advantage claimed by a taxpayer depends on a particular interpretation of the relevant taxing statute and that a court or tribunal has already decided that that interpretation of that taxing statute is wrong. The effect of the regime is that a taxpayer who receives a follower notice must, in effect, decide whether to accept HMRC's interpretation of the relevant taxing statute, supported by that earlier court or tribunal decision, or continue to challenge HMRC's assessment on the basis of his or her own different interpretation of the provisions. If he or she chooses to litigate and loses, he or she may be assessed as liable to pay a substantial financial penalty in addition to the extra tax due.

The appeal arises out of Mr Haworth's tax return for the year 2000/2001. In that return, Mr Haworth disclosed that he had entered into arrangements whereby, he asserted, he avoided any charge to tax on a substantial capital gain arising from the disposal of shares by a trust of which he was the settlor. The effectiveness of his arrangements depended on a combination of the provisions of the Taxation of Chargeable Gains Act 1992 (the "TCGA") and the operation of the UK/Mauritius double taxation convention (the "Convention"). In particular, it depended on the place of effective management ("POEM") of the trust being in Mauritius at the time that the shares were disposed of.

HMRC opened an enquiry into Mr Haworth's tax return and, in 2016, issued him with a follower notice. The notice was issued on the basis that HMRC considered that Mr Haworth's arrangements were, in all material respects, the same as those that had been considered by the Court of Appeal in *Smallwood v Revenue and Customs Commissioners* [2010] EWCA Civ 778 ("*Smallwood*"). In particular, HMRC said that *Smallwood* established that, on the true construction of the Convention, the POEM of Mr Haworth's trust was in the UK at the time of the disposal and that, as a consequence, he was not relieved of liability under the TGCA as he claimed.

Mr Haworth applied for judicial review of the follower notice. The High Court dismissed his application. However, his appeal was allowed by the Court of Appeal, who unanimously quashed the follower notice on the basis that HMRC had not satisfied the conditions required to give the notice.

HMRC's appeal to the Supreme Court raises two principal issues: first, whether HMRC formed the opinion required by section 205(3)(b) FA 2014, i.e., that "*the principles laid down or reasoning given in [Smallwood] would, if applied to [Mr Haworth's] arrangements, deny the asserted advantage*" ("Issue 1"); and second, whether HMRC misdirected themselves in their analysis of *Smallwood* and whether this made a difference to HMRC's decision to issue the follower notice ("Issue 2").

Mr Haworth raises two further issues: first, whether factual findings form part of the principles laid down or reasoning given in a ruling for the purposes of section 205(3)(b) FA 2014 ("Issue 3"); and second, whether section 206 FA 2014 invalidates the follower notice because HMRC failed adequately to explain in the notice its reasons for concluding that *Smallwood* determined Mr Haworth's case ("Issue 4").

JUDGMENT

The Supreme Court unanimously dismisses HMRC's appeal and upholds the Court of Appeal's decision to quash the follower notice. Lady Rose gives the sole judgment, with which all members of the Court agree.

REASONS FOR THE JUDGMENT

Issue 1: Did HMRC form the opinion required by section 205(3)(b) FA 2014?

The Court answers this question "no". The issue turns on what is meant by the word "*would*" in section 205(3)(b) FA 2014 **[57]**. The word "*would*" must be interpreted in light of the fact that, although a taxpayer served with a follower notice is still free to bring his case before a tribunal, the risk of incurring a substantial penalty discourages this and so impedes the exercise of the constitutional right to access to justice. The provision must be interpreted restrictively to produce the minimum interference with that right, consistent with achieving the purpose for which Parliament enacted the regime. The use of the word "*would*" indicates that HMRC must form the opinion that there is "*no scope for a reasonable person to disagree that the earlier ruling denies the taxpayer the advantage*" **[58-61]**. That is not a gloss on the statutory wording; it merely gives full weight to the use of the word "*would*" rather than, for example, "*might*". It also does not usurp the role that Parliament conferred on HMRC to form the required opinion, nor does it create any anomalies with the test applied by the First-tier Tribunal when determining an appeal against a penalty under a follower notice **[62-63]**. In the present case, HMRC accepted that its evidence of what happened at the meetings of the relevant committee shows no more than that HMRC concluded that it was "*likely*" that the application of *Smallwood* would deny Mr Haworth his tax advantage **[46; 69]**. That is not sufficient for the purposes of section 205(3)(b) **[61]**.

Issue 2: Did HMRC misdirect themselves in their analysis of *Smallwood*?

The Court answers this question "yes". HMRC proceeded on the basis that, if seven specific indicators which HMRC considered had been highlighted by Lord Justice Hughes in *Smallwood* were present in a given case, the POEM of the trust in that case would inevitably be in the UK **[31; 74]**. This overstated the conclusion of the Court in *Smallwood*: Lord Justice Hughes did not consider the seven indicators to be necessary and sufficient to establish that, in any other case, the POEM of a trust is in the UK **[75]**.

The Court also rejects HMRC's suggestion that section 31(2A) of the Senior Courts Act 1981 means that the follower notice should not have been quashed. The Court of Appeal was correct to conclude that it is by no means self-evident that HMRC would have decided to issue a follower notice to Mr Haworth had the conclusions arrived at in *Smallwood* not been overstated **[76]**.

Issue 3: Does the "reasoning given" in a ruling cover factual findings?

The Court answers this question "yes". Mr Haworth's suggestion to the contrary misunderstands the nature of factual findings and their role in the precedential value of judicial decisions **[77-81]**. He is also incorrect to suggest that it makes any difference whether an appellate court, when rejecting an *Edwards v Bairstow* challenge, expresses its agreement with the conclusion of the fact-finding tribunal or states only that the tribunal was entitled to reach that conclusion on the material before it **[82-83]**.

Issue 4: Is the follower notice invalidated by Section 206 FA 2014?

The Court answers this question "no". The follower notice did not comply with section 206 FA 2014 because it failed to describe the features of Mr Haworth's arrangements that, in HMRC's opinion, meant *Smallwood* determined his case **[85]**. However, section 206 does not provide that any defect in a notice will render it invalid and, in the present case, the defects do not invalidate the notice **[86]**.

References in square brackets are to paragraphs in the judgment