[2022] UKUT 84 (TCC)

Appeal number: UT/2021/000037

CORPORATION TAX, CAPITAL GAINS TAX, INCOME TAX – expenditure allowable under s38(1)(b) of TCGA 1992 – penalties imposed under s95 of TMA 1970 – interaction of s393A of ICTA 1988, paragraphs 58 and 59 of Schedule 18 FA 1998 and Schedule 1A of TMA 1970 in relation to carry back of losses for corporation tax – appeal dismissed

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

PETER LOWE (1) **CIVIC ENVIRONMENTAL SYSTEMS LTD (2)**	**Appellants**
-and-	
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS	**Respondents**

TRIBUNAL: MR JUSTICE MARCUS SMITH
JUDGE JONATHAN RICHARDS

Sitting in public at Rolls Building, 7 Rolls Buildings, Fetter Lane, London EC4A 1NL on 18 February 2022

Michael Firth, instructed by The Independent Tax & Forensic Services LLP for the Appellants

Charles Bradley, instructed by The General Counsel and Solicitor for Her Majesty's Revenue and Customs for the Respondents

© CROWN COPYRIGHT 2022

DECISION

Introduction

1. The appellants appeal against a decision (the "Decision") of the First-tier Tribunal (Tax Chamber) (the "FTT") released on 26 November 2020. The Decision dealt with a number of disputes between the Appellants and HMRC. With the permission of the FTT, the Appellants appeal against some, but not all, of the FTT's conclusions.

2. The three issues that are now before us are as follows:

> (1) The extent to which expenditure incurred on building works at John Street Sheffield (the "Property") was deductible in calculating the gain the First Appellant ("Mr Lowe") made on disposal of the Property for the purposes of capital gains tax ("CGT"). We will describe that as the "CGT Issue".
>
> (2) The amount of penalty properly chargeable on Mr Lowe under s95 of the Taxes Management Act 1970 ("TMA") for the tax years 2006-07 and 2007-08. We refer to that as the "Penalty Issue".
>
> (3) The extent to which the Second Appellant ("CES") was entitled to carry back a loss arising in its accounting period ended 30 April 2008 against profits, increased by the FTT's decision, of its accounting period ended 30 April 2007. We refer to this as the "Carry Back Issue".

3. Since these various issues are not inter-related to any significant extent, we will deal with them in the separate sections below. References to numbers in square brackets are to paragraphs of the Decision unless we say otherwise.

[A] – THE CGT ISSUE

Relevant statutory provisions

4. It was common ground that to the extent that Mr Lowe made a chargeable gain on disposal of the Property, that chargeable gain was subject to CGT. Section 38 of the Taxation of Chargeable Gains Act 1992 ("TCGA") specifies expenditure that can be deducted in the computation of a gain providing, so far as material, as follows:

> **38 Acquisition and disposal costs etc.**
>
> (1) Except as otherwise expressly provided, the sums allowable as a deduction from the consideration in the computation of the gain accruing to a person on the disposal of an asset shall be restricted to—
>
> …
>
> (b) the amount of any expenditure wholly and exclusively incurred on the asset by him or on his behalf for the purpose of enhancing the value of the asset, being expenditure reflected in the state or nature of the asset at the time of the disposal, and any expenditure wholly and exclusively incurred by him in

> establishing, preserving or defending his title to, or to a right over, the asset…

5. It will be seen that the opening words of s38(1) identify "the person making the disposal" and s38(1)(b) permits a deduction for certain costs "incurred by him or on his behalf". In this case it was Mr Lowe who made the disposal and at issue is whether expenditure was "incurred by him or on his behalf" or whether, as HMRC argue, the expenditure is not deductible because it was incurred by, or on behalf of, someone other than Mr Lowe.

The Decision on the CGT Issue

6. Mr Lowe acquired an interest in the Property in various stages starting in around 1979 or 1980 ([42]). He sold his interest in the Property for a consideration, including deferred consideration, of £2m in January 2007 ([6]). The CGT Issue (described as "Issue 2" in the Decision) involved the extent to which expenditure incurred on building works on the Property was deductible for CGT purposes. The relevant building works were:

> (1) "Stage 1" building works undertaken in 1986 ([42(2)]; and
>
> (2) "Stage 2" building works involving the building of offices which took place in 1987 and 1989 ([42(3)].

7. At the time these building works were carried out, Mr Lowe held only a 50% interest in the relevant freehold titles in the Property, with the other 50% interest being held by Mr Almond, who was his business partner. Mr Lowe and Mr Almond also owned 50% each of the shares in a company called Hadee Engineering Co Ltd ("Hadee").

8. Difficulty arose because the evidence as to the nature and cost of the building works consisted of quotes from builders (largely addressed to Mr Lowe personally) and invoices from builders (largely addressed to Hadee), but there was not a single instance of both a quote and an invoice covering the same work. HMRC were not disputing that the amounts shown on the quotes or invoices had actually been paid ([58]). Nor were they disputing that the expenditure in question was reflected in the state or nature of the Property at the time of disposal. However, they put Mr Lowe to proof that the expenditure had been "incurred by or on behalf of" him as required by s38(1)(b). They argued that if, as the evidence appeared to suggest, some of the expenditure had been incurred "by" Hadee, Mr Lowe would need to establish that Hadee was incurring the expenditure "on behalf of" Mr Lowe if that expenditure was to be deductible.

9. That articulation of the dispute made it necessary for the FTT to decide what it meant for one person to incur expenditure "on behalf of" another. At [91] and [92] it noted that this phrase could have either a broader meaning that extended to the situation where one person incurred expenditure for the purpose of benefiting another or it could have a narrower meaning confined to a situation where one person is acting as agent, or similar, for another. At [92] it concluded that the narrower interpretation was appropriate in the context of s38 of TCGA.

10. The FTT's conclusion can be summarised as follows:

> (1) Where a quote or an invoice evidenced Stage 1 or Stage 2 expenditure and was addressed to Mr Lowe, the FTT accepted that this expenditure was indeed incurred by Mr Lowe with the result that it could be deducted from the gain.
>
> (2) Where a quote or invoice evidenced Stage 1 or Stage 2 expenditure and was addressed to Hadee, the FTT refused to accept that this expenditure was incurred by, or on behalf of Mr Lowe, and so refused to allow Mr Lowe to deduct that expenditure in the computation of his gain on disposal of the Property.
>
> (3) This approach left open the possibility that a quote and an invoice might reference the same expenditure but for one type of document to be sent to Mr Lowe, and the other type of document to be sent to Hadee. In fact, that situation did not arise in practice but, in case it did, the FTT held that it would apply a "tie-breaker" so that the deductibility or otherwise of the expenditure would be determined by reference to the addressee of the invoice which the FTT considered would have a greater evidential value than a quote for the same work.

Mr Lowe's challenges to the Decision on the CGT Issue

11. Mr Lowe makes the following broad challenges to the FTT's conclusions on the CGT Issue:

> (1) *Ground 1* - The FTT wrongly focused on the question of who actually paid for the building works. It should have considered who had the legal liability to pay for them. Only Mr Lowe could have had the legal liability since the works were being done on land in which he, and not Hadee, had an interest and the works were undertaken for Mr Lowe's benefit and not for the benefit of Hadee.
>
> (2) *Ground 2* - The FTT failed to deal adequately with Mr Lowe's submission that it was simply impossible, as a matter of law, for Hadee to incur the costs of the building works itself without Mr Lowe having to suffer the economic costs of those works.
>
> (3) *Ground 3* - The FTT wrongly directed itself that Hadee could only have incurred the expenditure "on behalf of" Mr Lowe if it was acting as his agent.
>
> (4) *Ground 4* - Even if it was correct that something akin to a relationship of agency was necessary before Hadee could incur expenditure "on behalf of" Mr Lowe, the FTT failed to deal adequately with the submission that there was an agency relationship between Hadee and Mr Lowe.

Discussion

Ground 1

12. The parties approached Ground 1 from very different perspectives. Mr Lowe argues that it involves a challenge to the FTT's legal approach. He contends that the FTT was, in effect, asking itself the wrong question, namely who paid for the building works rather than who had the legal obligation to pay for them. Since the FTT was asking itself the wrong question, Mr Lowe submits that the FTT's conclusion was necessarily wrong in law and should not be allowed to stand. He also advances an alternative contention namely that, even if the FTT was asking itself the right question (contrary to his submission), the FTT's conclusion was still vitiated by a failure to take into account relevant considerations.

13. HMRC, by contrast, characterise Ground 1 (and indeed Grounds 2 and 4) as *Edwards v Bairstow* challenges to the FTT's findings of fact. In their written and oral submissions, HMRC declined to make submissions as to whether s38(1)(b) is focusing on the liability to pay, or the actual payment, submitting that this distinction had no bearing on the issues that the FTT actually needed to decide.

14. In our judgment, the parties' competing submissions on Ground 1 must be considered in the light of the very difficult case that the FTT had before it. We have already noted that the dispute concerned events that took place between 1986 and 1989. A good part of the evidence consisted of invoices and quotes that had been sent to Mr Lowe and Hadee. The FTT's task was to infer, from old documents, the extent to which expenditure had been incurred by or on behalf of Mr Lowe between 30 to 35 years previously.

15. One difficulty that Mr Lowe faced was that quotes or invoices that were addressed to Hadee did not obviously demonstrate that the expenditure referenced in them was incurred by Mr Lowe or on his behalf. To meet that difficulty, Mr Lowe sought to explain his practice at the time of distinguishing between quotes and invoices relating to the engineering business conducted by Hadee and quotes and invoices relating to his personal interest in the Property. However, HMRC were able to demonstrate in cross-examination that the distinctions he sought to draw between the various categories of invoices or quotes did not always hold good (see, for example [50(4)]).

16. A further difficulty was that some quotes or invoices were addressed to Hadee without mentioning Mr Lowe at all, some were addressed to Mr Lowe "care of" Hadee. Some were addressed to Hadee "for the attention of" Mr Lowe. Various other formulations were used. The FTT had the unenviable task of deciding whether anything turned on these different formulations (see the discussion at [82]).

17. Therefore, Mr Lowe's case before the FTT was based on (i) quotes and invoices that were just as silent on the question of who had the liability to pay for the works as they were on the question of who actually paid for the works and (ii) inferences that Mr Lowe argued should be drawn from the documents and surrounding circumstances, such as the fact that Mr Lowe had an interest in the Property but Hadee did not. No contracts for the work, which could have shed a light on who had the liability to pay

for the works as distinct from who ultimately paid for them, were put in evidence. Certainly Mr Firth for the Appellants, here and below, made submissions (recorded at [60]) that, since s38(1)(b) was concerned with contractual liability, quotations were a better indicator of who "incurred" the expenditure for the purposes of s38(1)(b) because they were more related to the formation of a contract than its execution. However, the question of whether invoices or quotations were the more reliable documents ultimately did not need to be addressed because, as is common ground, none of the expenditure relevant to the CGT Issue was referenced both in an invoice and a quotation.

18. In his submissions, Mr Firth showed us the written closing submissions he made to the FTT. In paragraphs 4 to 6 he argued that s38(1)(b) is concerned with who had the liability to make the payment. In paragraph 9, Mr Firth submitted that it "would be expected" that Mr Lowe would have the obligation to pay for works at the Property since he had an interest in the Property but Hadee did not. In paragraph 18, he submitted that the builders could only have sued Mr Lowe, and not Hadee, if they had not been paid. However, none of these submissions were rooted in any evidence as to who had the contractual obligation to pay for the building works, as distinct from who actually paid for those works. That would not have been possible given the points we have made in paragraph 17. Rather, Mr Firth's submissions were based on the patchwork of evidence consisting of quotes and invoices and inferences from surrounding circumstances that could be drawn from them.

19. Having considered the way that Mr Lowe was putting his case before the FTT, we have concluded that HMRC are substantially correct to characterise Mr Lowe's challenge under Ground 1 as amounting to a challenge to what are essentially factual findings, involving difficult consideration of the limited evidence before the FTT, rather than involving any legal question. In short, the legal analysis does not arise given the nature of the factual evidence. The FTT did not need to decide whether s38(1)(b) was concerned with liability or payment since the evidence before it did not draw that distinction. If there had been a conflict between quotes and invoices for the same work, for example if a quote had been addressed to Mr Lowe alone, but an invoice for the same work had been addressed to Hadee alone, the issue might (and we stress we state no conclusion in this regard) have required resolution since Mr Firth was arguing that quotes, being more associated with contract formation than with payment, were a more reliable guide to whether expenditure was "incurred" by or on behalf of Mr Lowe. However, as we have noted, in no case was there both a quote and an invoice for the same work.

20. We therefore reject the first part of Mr Lowe's case under Ground 1, namely that the FTT made an error of approach in failing to direct itself as to whether s38(1)(b) was concerned with contractual obligation or actual payment. The FTT did not need to decide this question of statutory interpretation and we do not consider that we need to determine it either.

21. The next aspect of Mr Lowe's challenge under Ground 1 relies on the proposition that the FTT failed to take into account relevant considerations or took into account irrelevant considerations. That argument is developed as follows:

(1) The FTT found, at [78], that Mr Lowe was not always as sensitive as he should have been to the distinctions between himself as an individual and companies such as Hadee which he controlled or in which he had an interest.

(2) Having made that finding it was illogical to attach any material significance to whether Mr Lowe or Hadee was mentioned in any particular invoice or quote.

(3) Much more significant were the facts that (i) the work was done on land in which Mr Lowe had an interest but Hadee did not and (ii) the work was done for Mr Lowe's benefit and not for the benefit of Hadee. The FTT failed to have regard to these important considerations.

22. We reject that argument. Although it uses the language of a challenge to the FTT's decisions under *Edwards v Bairstow* principles, it is in reality an invitation to us, as an appellate tribunal, to engage in precisely the "island hopping in a sea of evidence" that Lewison LJ deprecated in *Fage UK Ltd v Chobani UK Ltd* [2014] EWCA Civ 5 at [114]. It did not follow from the FTT's finding that Mr Lowe was "not always as sensitive as he should have been" to distinctions between himself and Hadee that the addressee of quotes or invoices was irrelevant. Rather, it was for the FTT to evaluate the significance or otherwise of the ways in which different quotes or invoices were addressed and the FTT did precisely that in its careful decision. The FTT did not "ignore" the fact that Mr Lowe had an interest in the Property but Hadee did not. At [61], it noted the emphasis that was placed on the fact that the works were on land of which Mr Lowe was co-owner. Mr Lowe doubtless considers that the FTT did not give sufficient weight to this factor, but that does not demonstrate any error of law in the Decision in circumstances where the FTT's task, made difficult by the patchwork of evidence before it, was to evaluate the significance of competing indications.

23. We dismiss Mr Lowe's challenge under Ground 1.

Ground 2

24. As Ground 2, Mr Lowe argues that the FTT failed to understand, and so failed to address adequately, the submissions made in paragraphs 28 to 32 of the written closing submissions that Mr Firth made on his behalf.

25. The argument advanced in those paragraphs was that there was "no way that the transactions could have been structured" that would not have required Mr Lowe to suffer the costs that HMRC asserted had been "incurred" by Hadee. Specifically, it was submitted that:

(1) If the company had decided to pay Mr Lowe remuneration, or to declare a dividend, to be satisfied by Hadee paying for building work on Mr Lowe's land, that would involve Mr Lowe incurring the expenditure himself (since it would be his salary, or his remuneration, that was used to pay the builders).

(2) Alternatively, Hadee could add the sums to Mr Lowe's director's loan account, or they could have been unlawful distributions made to Mr Lowe

in his capacity as shareholder. In the former case, Mr Lowe would straightforwardly have had an obligation to repay Hadee the amounts in question. In the latter case the obligation would come from s830 or s847 of the Companies Act 2006.

26. Mr Lowe argues that the FTT was wrong, at [89], to reject this submission for lack of evidence. The FTT should have appreciated that the point being advanced was one of pure law. As such, no evidence was needed to support it and it should not have been dismissed because of a perceived lack of evidence.

27. We reject this argument. As HMRC point out, it was conceptually possible for Hadee to conclude that paying for the costs of building work on land it did not own was in its business and commercial interests. If it reached such a conclusion, it could quite properly pay for the works without declaring a dividend, debiting Mr Lowe's loan account or treating the sum as a payment of remuneration to Mr Lowe. Of course, if it had done so, it is quite possible that there would have been tax consequences for Mr Lowe: he could be regarded as receiving a taxable benefit from Hadee of some kind. However, it was not impossible for such tax consequences simply to have been overlooked. The FTT was entitled to conclude that something more than an assertion was needed to make good the points made in paragraphs 28 to 32 of Mr Firth's written closing submissions such as an explanation, supported by evidence, of why it could not be in the interests of Hadee to pay for the works.

28. In answers to questions from us during the Upper Tribunal hearing, Mr Firth submitted that, if Hadee had lawfully paid for the building works, the economic cost would have fallen on Mr Lowe because Hadee would have had less available cash with which to pay salary or dividends. However, that argument also would depend on evidence, as to the extent to which Hadee expected to distribute cash to Mr Lowe by way of salary or dividend instead of holding sums back for deployment in its business.

29. In short, we regard this ground also as substantially turning on the facts, rather than raising any issue of pure law. We dismiss Mr Lowe's appeal under Ground 2.

Ground 3

30. Ground 3 raises a question of pure statutory interpretation. Mr Lowe argues that the FTT was wrong to conclude at [92] that, for expenditure to be incurred on his behalf for the purposes of s38(1)(b) of TCGA , that expenditure had to be incurred by someone acting as his agent or in some similar capacity. He argues that the FTT should instead have concluded that the words "on behalf of" in s38(1)(b) include expenditure incurred for the purpose of benefiting Mr Lowe, even if not incurred by an agent or similar.

31. Neither party was able to refer us to any authority on the meaning of the words "on behalf of" in s38(1)(b). We were, however, referred to the judgment of the Supreme Court in *Plevin v Paragon Personal Finance Ltd* [2014] UKSC 61. That case concerned the application of s140A(1) of the Consumer Credit Act 1974 which gave the court power to make certain orders if satisfied that a relationship between creditor and debtor was unfair because of, inter alia, "any … thing done (or not done) by, or on behalf of, the creditor". In *Plevin*, a broker arranging a loan had failed to disclose the significant

amount of commission that both the lender and the broker would earn from payment protection insurance ("PPI") being sold to the borrower. Moreover, the broker had failed to consider the suitability of the PPI for the borrower. The question was whether these failures should be regarded as things that were not done "by, or on behalf of," the lender in circumstances where there was no relationship of agency between the broker and the lender.

32. Lord Sumption, with whom all of their Lordships agreed said, at [30] of his judgment:

> In their ordinary and natural meaning the words "on behalf of" import agency, which is how the courts have ordinarily construed them: see *Gaspet Ltd v Elliss (Inspector of Taxes)* [1985] 1 WLR 1214, 1220 (Peter Gibson J); *Clixby v Pountney (Inspector of Taxes)* [1968] Ch 719, at paras 728-729 (Cross J). I would accept that a special statutory or contractual context may require the phrase "on behalf of" to be read more widely as meaning "in the place of", or "for the benefit of" or "in the interests of": see *R (Cherwell District Council) v First Secretary of State* [2005] 1 WLR 1128 at para. 56 (Chadwick LJ); *R(S) v Social Security Commissioner* [2010] PTSR 1785, at paras 27-28; Rochdale *Metropolitan Borough Council v Dixon* [2012] PTSR 1336, at paras 49-50 (Rix J). But there is nothing in the present statutory context to suggest any of these wider meanings, and much that is inconsistent with them. In the first place, the full phrase is "by or on behalf of the creditor". In other words, acts or omissions "on behalf of" the creditor are treated as equivalent to acts or omissions "by" the creditor. They refer to things done or not done either by the creditor itself, or by someone else whose acts or omissions engaged the creditor's responsibility as if the creditor had done or not done it itself. They indicate as clearly as language can do that sub-paragraph (c) applies only where the "thing" is done or not done by someone whose acts or omissions engage the responsibility of the creditor. They are used in the same sense throughout the Consumer Credit Act whenever it refers to some act such as the execution of a document or the receipt of a notice or the occurrence of any other act which the legislator intends to engage the responsibility of the creditor.

33. Understandably, Mr Firth referred us to cases including *R (on the application of "G") v Thanet District Counci*l [2021] EWHC 2026 (Admin) in which the phrase "on behalf of" in a statutory provision had been held to mean something like "in the interest of or for the benefit of". Equally understandably, Mr Bradley (counsel for HMRC) made the point that those cases were concerned with different statutory schemes. The *Thanet District Council* case, for example, was a case concerned with planning law rather than tax law. However, in our judgment, reasoning by analogy with different cases is unlikely to provide much of a guide, since the task is to determine what the phrase "by him or on his behalf" means in s38(1)(b) specifically.

34. In our judgment, the short answer to this point is that there is no "special statutory context" (to use Lord Sumption's expression) which suggests that the phrase should be given any other than its ordinary and natural meaning of connoting a relationship of agency. The parties took us through various hypothetical examples involving A, an owner of land and B a person prepared to provide some kind of gratuitous benefit to A.

In scenario (i) B gives A £1,000 and A spends that on building works on the land. In scenario (ii) A enters into a contract with a builder for works to be performed on A's land but B gratuitously pays the builder £1,000 of the price of those works. In scenario (iii) B enters into a contract with a builder and pays the builder £1,000 in return for the builder agreeing to perform building works on A's land. Those three scenarios were, Mr Firth argued, economically indistinguishable and it would make no sense for the expenditure to count in scenario (i) but not in scenarios (ii) or (iii).

35. However, in our judgment, the discussion of these scenarios does not establish any "special statutory context". At most they establish that economically similar transactions might be taxed differently if the phrase "by him or on his behalf" is held to be limited to situations involving agency. However, that is not a particularly startling outcome. Economically similar transactions are not infrequently taxed in different ways. More generally, scenarios (i) to (iii) are products of the ingenuity of lawyers litigating a particular issue arising out of s38(1)(b). They do not address the more "mainstream" situation where a person owning an asset incurs expenditure either directly, or through an agent, on the improving of that asset and so are less capable of establishing a "special statutory context" that displaces the ordinary and natural meaning of the words.

36. Mr Firth also submitted that the purpose of the legislation is to tax gains, not gifts. So, he argued, the "transfers of value" arising within scenarios (i) to (iii) would be within the scope of a charge to inheritance tax ("IHT") and should not also come within the scope of the charge to CGT as a result of relief under s38(1)(b) being denied. However, the difficulty with that submission is that s38 makes no mentions of gifts or possible parallel charges to IHT. If Parliament had wished to prevent the result to which Mr Firth was referring, it would have done so more directly, rather than obliquely by expecting an astute reader of the statute to realise that IHT considerations should result in the phrase "by him or on his behalf" bearing something other than its usual meaning. In any event, we did not accept the premise of Mr Firth's argument. Gifts are not always subjected to a charge to IHT. There will frequently be no IHT charge on a gift if the donor survives for more than 7 years after making it, if the donor is a company or if the donor not domiciled in the UK and the gifted property is situated outside the UK. The extent of any CGT charge on disposal of the Property depends on the construction of the relevant legislation, and not on any overriding principle of not taxing twice over. By way of analogy, the case could be made that income tax should not be charged where that income is used to purchase goods subject to VAT (or *vice versa*) but that argument serves as little aid to the construction of VAT or income tax statutes in any particular case.

37. Nor are we persuaded by Mr Firth's argument that the words "on his behalf" would be redundant if they referred only to the situation of agency since s38(1)(b) is concerned with who incurred the contractual liability, not the person who made the payment, and a liability incurred by a person as agent could be regarded as incurred "by" the principal. We express no view on whether the premise of that argument, that s38(1)(b) is concerned with liability, is correct or not for reasons that we have given in paragraphs 19 and 20 above. However, even if it is correct, there would still be a benefit in Parliament making it absolutely clear, without requiring a reader of s38(1)(b) to engage

in a detailed analysis of the law of agency, that money does not need to be handed over physically by a person making a disposal in order to attract relief under s38(1)(b).

38. For the reasons set out above, we dismiss Mr Lowe's appeal on Ground 3.

Ground 4

39. As Ground 4, Mr Lowe argues that the FTT failed to deal with arguments made in paragraphs 24 to 26 of his closing submissions. In those paragraphs Mr Lowe argued that even if, contrary to his other submissions, the words "on his behalf" in s38(1)(b) were addressing only the situation of agency, Hadee was his agent to the extent that it incurred expenditure in connection with the Property. Mr Lowe referred to the following facts in support of that interpretation: (i) Mr Lowe sourced the quotes for the work and had them sent to Hadee, (ii) Mr Lowe caused Hadee to enter into building contracts for works done on land in which Mr Lowe had an interest (iii) Mr Lowe owned the Property (iv) the building works were of no benefit to Hadee (v) Hadee had nolegal right of its own to facilitate works on land owned by Mr Lowe and (vi) Hadee therefore had Mr Lowe's personal authority to enter into the contracts for works on the Property.

40. The short answer to this ground of appeal is that the FTT was referring to these very arguments in [66] of the Decision which uses phrasing identical to that used in paragraph 25 of Mr Firth's written closing submissions. Therefore, the FTT had these submissions clearly in mind when it reached its conclusions on the extent to which expenditure was incurred on behalf of Mr Lowe for the purposes of s38(1)(b) of TCGA.

41. Moreover, in our judgment the points summarised in paragraph 39 above by no means compelled the conclusion that Hadee incurred expenditure as agent for Mr Lowe. Points (i) and (ii) were entirely consistent with Mr Lowe being a director of Hadee. Mr Lowe did not own the entire interest in the Property but, even if he had, that did not necessarily constitute Hadee as his agent. Points (iv) and (v) could appropriately be regarded as adding little to the proposition that Mr Lowe had an interest in the Property but Hadee did not. Point (vi) sets out the conclusion that Mr Lowe wanted the FTT to draw. In short, the FTT was fully entitled, as it did, to treat points (i) to (vi) as factors relevant in its overall consideration of the extent to which Hadee was acting as Mr Lowe's agent, but those points did not compel any particular conclusion on that issue. We dismiss Mr Lowe's challenge under Ground 4.

[B] – THE PENALTY ISSUE

Legislation relevant to the Penalty Issue

42. HMRC imposed a penalty on Mr Lowe for what they considered to be negligent errors in his tax returns for the 2006-07 and 2007-08 tax years. The penalty regime applicable to those tax years was set out in s95 of the Taxes Management Act 1970 ("TMA"). Subsequently a new penalty regime was enacted in Schedule 24 of the Finance Act 2007, but that new regime is of no application in the circumstances of this appeal.

43. Section 95 provided, so far as material, as follows:

> **95 Incorrect return or accounts for income tax or capital gains tax.**
>
> (1) Where a person fraudulently or negligently—
>
> > (a) delivers any incorrect return of a kind mentioned in section 8 or 8A of this Act (or either of those sections as extended by section 12 of this Act ...
>
> he shall be liable to a penalty not exceeding the amount of the difference specified in subsection (2) below.
>
> (2) The difference is that between—
>
> > (a) the amount of income tax and capital gains tax payable for the relevant years of assessment by the said person (including any amount of income tax deducted at source and not repayable), and
> >
> > (b) the amount which would have been the amount so payable if the return, statement, declaration or accounts as made or submitted by him had been correct.
>
> (3) The relevant years of assessment for the purposes of this section are in relation to anything delivered, made or submitted in any year of assessment, that, the next following, and any preceding year of assessment;…

44. It was common ground that the FTT's powers on an appeal against a penalty were set out in 100B(2)(b) of TMA as follows:

> (2) On an appeal against the determination of a penalty under section 100 above section 50(6) to (8) of this Act shall not apply but—
>
> …
>
> (b) in the case of any other penalty, the First-tier Tribunal may –
>
> > (i) if it appears that no penalty has been incurred, set the determination aside,
> >
> > (ii) if the amount determined appears to be appropriate, confirm the determination,
> >
> > (iii) if the amount determined appears to be excessive, reduce it to such other amount (including nil) as it considers appropriate, or
> >
> > (iv) if the amount determined appears to be insufficient, increase it to such amount not exceeding the permitted maximum as it considers appropriate.

45. It will be seen from the above extracts from the legislation that:

> (1) There is a threshold condition for any penalty to become payable under s95: there must be some kind of fraudulent or negligent error.
>
> (2) Once that threshold condition is satisfied, s95(2) sets out a <u>maximum</u> penalty that can be charged.

(3) Provided that it does not exceed that maximum, the FTT has a broad discretion as to the amount of penalty.

(4) Section 95 does not itself contain any parameters regulating the way in which the FTT exercises its discretion, by contrast with the successor legislation in Schedule 24 of Finance Act 2007.

The FTT's decision on the Penalty Issue

46. The FTT found that Mr Lowe made the following errors in relation to his 2006-07 tax return ([140]):

(1) He omitted £17,425 of taxable interest income.

(2) He omitted £350 of rental income.

(3) He omitted a chargeable gain of £66,667.67 that arose on the grant of an option over shares in CES.

(4) He omitted a chargeable gain of £34,000 (excluding indexation allowance) on a disposal of shares in Just For Kids Limited ("JFK").

(5) He claimed an excessive deduction for the costs of building work in computing his gain on disposal of the Property.

(6) He also claimed excessive business asset taper relief on his disposal of the Property.

47. The FTT also found that Mr Lowe had made an error in his 2007-08 return by omitting a taxable dividend of £500,000 that he had received from Hadee in that year.

48. The FTT found that the error described in paragraph 46(2) was neither negligent nor fraudulent; it was an innocent mistake. It found that the other errors were negligent ([148]).

49. The fact that Mr Lowe's tax return for 2006-07 contained a number of discrete errors, not obviously related to each other, gave rise to some question of the proper approach the FTT should take in determining an appropriate penalty. The FTT noted, at [143] and [144] that s95 of TMA applies on a "tax return by tax return basis, and not by reference to individual errors". That meant that, as soon as a single negligent or fraudulent error was present in a return, a penalty could be chargeable with the amount of that penalty not to exceed the difference between (i) the tax actually due for that period and (ii) the tax shown as due on the face of the return[1]. The significance of this point can be seen from the following hypothetical example. Suppose that a taxpayer delivers a return showing tax due of £10,000 and that return contains (i) a fraudulent inaccuracy resulting in tax being understated by £250 (ii) a negligent inaccuracy resulting in tax being understated by £500 and (iii) an entirely understandable and justifiable error arising from a misunderstanding of applicable tax law on which there

---

[1] In fact, s95 appears to cap the liability at the tax payable over <u>three</u> relevant tax years (see s95(3)). However, neither party suggested that this was material in the context of these proceedings and we will, therefore, adopt the FTT's formulation of the maximum penalty as a shorthand.

was genuine disagreement that resulted in tax being understated by £2,000. On those assumed facts, the total actual tax liability for the period would be £12,750. On the basis of the FTT's interpretation of s95 (which is not challenged in these proceedings), a penalty would be chargeable because of the presence of the negligent and fraudulent errors. The maximum amount of that penalty would be £2,750, a figure much greater than the amount of the tax understated by the fraudulent and negligent errors. However, as the FTT noted at [144], it did not follow that a penalty of £2,750 would be charged in this situation: it would be appropriate to take into account all mitigating factors, including the fact that the £2,000 error was innocent.

50. The FTT's overall approach was to consider each error in Mr Lowe's tax return, calculate the amount of tax understated by that error and so the maximum amount of penalty attributable to that error. It would then consider mitigating factors that operated in relation to each error. Because of the conclusion we have summarised in paragraph 49 above, the FTT took into account the £350 understatement of rental income, even though it was neither negligent nor fraudulent. It concluded, however, that it would mitigate the penalty for that error by 100% ([150(b)]).

51. A related question concerned how to determine the appropriate amount of the penalty. One approach would be to start with the maximum penalty that could be charged under s95 and then mitigate that theoretical maximum by a discount that reflected, for example, the seriousness of the taxpayer's errors and the quality of the taxpayer's disclosure to, and co-operation with, HMRC. Such an approach might, conceptually, lead to less "serious" errors still attracting significant penalties if the taxpayer was not particularly co-operative after the initial error had been made. Another approach would be to give primacy to the seriousness of the errors in question, determine a penalty that was appropriately chargeable by reference to errors of that seriousness and then decide whether that penalty should be mitigated to reflect disclosure and/or co-operation. That approach might lead to errors of high "seriousness" attracting relatively low penalties if the taxpayer subsequently was co-operative and disclosed information to HMRC.

52. HMRC favoured the former approach that we have summarised in paragraph 51 above no doubt because their practice, which the FTT summarised at [36] and [37], was to follow this approach when making their own assessment of penalties to be imposed under s95. By contrast, Mr Lowe urged the FTT to follow the latter approach, submitting, among other matters, that it was more consistent with the approach that Parliament mandated in the successor legislation in Schedule 24 of Finance Act 2007.

53. The FTT concluded that it would follow HMRC's suggested approach saying, at [145(1)]:

> We can see no merit in Mr Firth's submission that the principles inherent in the regime under Schedule 24 of the FA 2007 should be applied in this context. We can see how, in terms of quantifying the penalty, the new regime effectively gives relatively less weight to disclosure and co-operation and relatively more weight to the culpability of the error in the tax return. However, it is a quite separate regime and, as Mr Bradley

rightly pointed out, it is not relevant to the application of the regime in Section 95 of the TMA.

We therefore see no reason to depart from the long-standing framework adopted by the Respondents in relation to Section 95 of the TMA pursuant to which the statutory maximum of 100% of the lost tax is subject to potential discounts as follows:

(a) up to 20% for "disclosure". This is calculated by reference to the promptness and fullness of the taxpayer's admission of the error. Exceptionally, the discount could be 30% for the prompt disclosure of an error that the Respondents might not have otherwise found;

(b) up to 40% for "co-operation". This is calculated by reference to the promptness and extent to which the taxpayer assisted the Respondents in quantifying and evidencing the necessary correction; and

(c) up to 40% for "seriousness". This is calculated by reference to the nature of, and reasons for, the original error and the amount of money involved. A minor error in relation to a small amount of tax qualifies for a large discount whereas a deliberate and contrived fraud in relation to a large amount of tax qualifies for no or only a small discount.

Mr Lowe's challenges to the FTT's conclusions on the Penalty Issue

54. Mr Lowe challenges the FTT's conclusions on the following grounds:

(1) *Ground 5* - The FTT's approach to the calculation of the penalties was wrong. It should have determined its own approach to mitigation of the penalties rather than simply following HMRC's practice.

(2) *Ground 6* – It was not sufficient for the FTT to refuse to follow the approach set out in Schedule 24 of FA 2007 simply because the provisions of that schedule were not in force at the relevant time. It should have concluded that the approach set out in Schedule 24 was appropriate instead of the approach it ultimately adopted.

(3) *Ground 7* – The FTT should have applied a framework that gave primacy to the nature of the conduct leading to the potential loss of tax.

(4) *Ground 8* – The FTT's approach was flawed as it led to disproportionate outcomes.

(5) *Ground 9* - The FTT should not have concluded that Mr Lowe was negligent in failing to declare the chargeable gain of £66,666.67 on the option premium he received in 2006-07 in circumstances where he had received professional advice from PwC on the reorganisation of his business interests that led to the receipt of that option premium.

(6) *Ground 10* - The negligence that the FTT found in respect of the overclaimed business asset taper relief (see paragraph [46(6)] above) was not part of HMRC's pleaded case.

> *Ground 11* - The FTT was wrong to conclude that Mr Lowe was negligent as regards the CGT Issue. His underlying position was reasonable. The negligence that the FTT identified in relation to the CGT Issue (Mr Lowe's failure to provide relevant documents to his accountants) did not cause the loss of tax.

Grounds 5 to 8

55. We take these grounds of appeal together as they all involve a challenge to the methodology that the FTT employed in deciding the amount of penalty that should be imposed.

56. Grounds 5 and 6 can be dismissed briefly. The FTT <u>did</u> consider for itself the framework it should apply. It also realised that Mr Lowe was inviting it to apply the <u>principles</u> set out in Schedule 24 of FA 2007 rather than the provisions of Schedule 24 itself which were not in force for relevant periods. Both of these conclusions are demonstrated by [145(1)] of the Decision. In the second sentence, the FTT declines to apply the "principles inherent in the regime under Schedule 24 of the FA 2007". In the final sentence it notes that it saw "no reason to depart from the long-standing framework adopted by [HMRC] in relation to Section 95 of the TMA", demonstrating that it realised that it was not bound by HMRC's practice but was simply choosing to follow it when making its own evaluation.

57. In our judgment, the arguments advanced under Ground 7 are unrealistic. By s95 of TMA, Parliament conferred a wide discretion on the FTT to determine the amount of penalty to be imposed. There was no obvious "right" way to approach that discretion. We have already highlighted, in paragraph 51 above, the differing consequences that could flow from the differing approaches advocated by the parties. As Mr Bradley said in his submissions on behalf of HMRC, reasonable people can disagree about the most appropriate framework to adopt. The framework that the FTT chose to follow was reasonable and rational. Moreover, there is a clear benefit in all FTTs hearing appeals on s95 penalties following similar methodologies since that gives taxpayers confidence that the FTT will assess all penalties by reference to similar principles. We do not, therefore, consider that the FTT made any error of law in choosing to follow a reasonable and rational approach that (i) has been followed by numerous other FTTs previously and (ii) is consistent with the approach that HMRC follow.

58. Mr Lowe's argument under Ground 8 was that the FTT's approach to the ascertainment of the penalties was wrong because it led to disproportionate outcomes. He referred, in particular, to (i) the 80% penalty that was imposed for a negligent failure to include bank interest receivable, (ii) the 35% penalty imposed in respect of the option premium and (iii) the 80% penalty imposed in respect of business asset taper relief and the claiming of excessive deductions under s38(1)(b) against the gain arising on disposal of the Property.

59. Ground 8 is formulated as a challenge to the FTT's whole approach, not to the conclusions reached following an application of that approach, even though specific examples of averred disproportionate outcomes are given. However, the mere fact that

Mr Lowe considers particular outcomes to be disproportionate does not make the FTT's methodology wrong in law for reasons that we have given in connection with Ground 7 above. If Mr Lowe had wished to challenge the particular conclusions reached by the FTT in respect of the items mentioned in paragraph 58, he could have done so. But that is not the argument made under Ground 8 as demonstrated by the fact that Mr Lowe has not specified what penalty he considers should appropriately have been charged in respect of those matters. We therefore dismiss Ground 8 as formulated. Of course, we appreciate that a challenge to a specific penalty could have been mounted by Mr Lowe. In such a case, we would only be minded to interfere in the FTTs discretion if we were satisfied that no reasonable tribunal could have imposed a penalty of that amount. We say nothing further on this point, because the point was not argued before us.

Ground 9

60. Mr Lowe used the services of Nicholas & Walters ("N&W") to prepare his tax returns. In 2006-07, he effected a reorganisation of his business interests, obtaining tax advice from PricewaterhouseCoopers ("PwC"). That reorganisation resulted in Mr Lowe receiving a premium in return for the grant of an option over his shares in CES. That premium was taxable, but was omitted from Mr Lowe's return for 2006-07.

61. The FTT found that this omission was negligent at [148(2)(a)]. It found that Mr Lowe had not told N&W about the receipt of the option premium but that this was not necessarily culpable as he was entitled to assume that PwC would have told N&W about it. However, it concluded that Mr Lowe was negligent in signing his 2006-07 tax return that N&W had prepared without reading it. Had he read the return, he would have noticed that the option premium had been omitted and asked N&W why. That would have alerted N&W to the receipt of the premium which would then have been included in the return, so the causal link between the negligence and the insufficiency of tax was established.

62. Mr Lowe criticises this reasoning arguing that the FTT should have considered whether Mr Lowe received "implicit advice" of the kind discussed by the Upper Tribunal in paragraphs 61(1) and 85 of *HMRC v Bella Figura Limited* [2020] UKUT 120 (TCC). In short, he argues that his tax returns were prepared by tax professionals and the FTT should have considered whether he was entitled to assume that everything that needed to be included in the 2006-07 tax return was so included.

63. However, that defence to the accusation of negligence could succeed only if the FTT found as a fact that Mr Lowe reasonably concluded from the fact that the option premium was not included in the return for 2006-07 that the premium was not taxable. However, the FTT's findings precluded such a conclusion. Mr Lowe, negligently, did not read the return for 2006-07 before it was submitted. He could not, therefore, have known whether the option premium was included or not and could not, therefore, have derived any implicit reassurance of the kind for which he argues. The FTT made no error in failing to consider a possible defence that was inconsistent with its findings of fact and we dismiss Mr Lowe's appeal on Ground 9. We need say nothing about whether Mr Lowe would have received "implicit advice" had he read and considered the 2006-07 tax return, because he did not do so. But we do not consider that an

omission like this should automatically result in the inference that the omission is (i) anything other than an error which (ii) does not entail the giving of advice. However, in cases such as this, the specific circumstances are all-important, and the fact is that Mr Lowe never read the return, with the result that the issue does not arise.

Ground 10

64. In his tax return for 2006-07, Mr Lowe claimed business asset taper relief against the whole gain arising on disposal of the Property. In fact, as is now common ground, only part of the gain qualified for taper relief.

65. Therefore, the FTT proceeded on the basis that there were two errors in Mr Lowe's return relating to the Property. The first was the overclaim of business asset taper relief to which we have just referred. The second was an overclaim of allowable expenses that . Mr Lowe claimed that the operative cause of the understatement of CGT on disposal of the Property was the overclaim of business asset taper relief, and not any overclaim of allowable expenditure. We will return to this issue in our consideration of Ground 11. Mr Lowe then said that, because HMRC had not pleaded in their Statement of Case that the overclaim of business asset taper relief was negligent, they could not pursue a claim for a penalty on that basis (see his submission recorded at [127(3)]).

66. At [148(2)(b)] the FTT found that Mr Lowe was negligent in failing to provide adequate information to N&W in relation to the extent to which the Property was used for business purposes (which would underpin any claim that a gain on the Property could be reduced by business asset taper relief). That, argues Mr Lowe, was a finding that was not open to the FTT because that specific failure had not been pleaded as an indication of negligence. However, in our judgment, this involves an over-literal approach both to pleadings in the FTT and a failure to read the Decision as a whole.

67. Pleadings before the FTT are not governed by the same rules as in the courts. By Rule 25 of the FTT's rules of procedure, HMRC were obliged, in their Statement of Case to set out the legislative provisions under which their decision was made and set out their "position in relation to the case". HMRC set out their "position" in paragraph 16 of their Statement of Case, namely that Mr Lowe knew, or ought reasonably to have known, that his return for 2006-07 was not correct. The FTT agreed. It found, among other matters, that Mr Lowe signed his returns without reviewing them and failed to provide adequate information to his advisers. It found at [150(e)] that "there is no reasonable explanation for claiming business asset taper relief to an excessive extent". The FTT reached those findings after a careful review of the evidence in a decision running to over 80 pages. These findings were perfectly capable of supporting the allegation of negligence that HMRC had made in their Statement of Case. We dismiss Mr Lowe's appeal on Ground 10.

Ground 11

68. As Ground 11, Mr Lowe argues that the FTT failed to consider whether the understatement of CGT due on disposal of the Property was caused by his provision of inadequate information to his accountants. He says that Mr Lowe actually claimed

£681,203 of allowable expenditure in respect of the Property. Had he provided his accountants with all of the documents that he ultimately relied on in evidence he would, taking into account the FTT's decision on the Property Issue, have been entitled to deduct around £750,000. Therefore, the provision of inadequate information to his accountants could not have caused any loss of tax since, if he had provided adequate information, he would have been claiming more allowable expenditure, not less.

69. Mr Bradley accepted the factual premise of Mr Lowe's argument that we have just summarised. He did not accept that it demonstrated an error of law in the Decision, since the situation to which Mr Lowe refers arose partly in consequence of the Decision and so could not realistically have been addressed in the Decision itself. He did, however, accept that the situation had some bearing on the seriousness of the error in calculation of CGT due on disposal of the Property. Before Mr Lowe had alighted on this point, it might be thought that the error was attributable to two factors: both a negligent overclaim of business asset taper relief and a negligent failure to provide proper information on allowable expenditure to Mr Lowe's accountants. The FTT regarded the seriousness of the second of these as "difficult to assess" (see [150(e)]). Now it appears likely that there was just one operative cause: namely the failures in relation to taper relief.

70. We heard little argument on this issue at the oral hearing. At this remove from the evidence, we would also find it difficult to perform our own re-evaluation of the "seriousness" of the error in the CGT calculation on disposal of the Property. We will therefore suggest to the parties that (i) they should seek to agree between themselves whether, and if so by how much, the penalty charged on Mr Lowe should be reduced in the light of the points he makes under Ground 11 but that (ii) if they cannot agree, we will hear further submissions as to whether Ground 11 establishes any error of law in the Decision. We hope and expect that the parties will be able to reach agreement to render this course unnecessary.

[C]: THE CARRY BACK ISSUE

Background to the issue

71. The issue is best understood in the context of the following table summarising profits and losses of CES for its accounting periods ended 30 April 2007 and 30 April 2008:

Accounting period	Profit shown on return	Profit post FTT Decision
y.e 30.4.2007	£142,039	£682,039
y.e. 30.4.2008	(£444,748)	(£444,748)

72. CES made a loss in its accounting period ended 30 April 2008 (the "2008 period"). That loss was not subsequently reduced in the FTT proceedings. At the date CES submitted its return for that period, it thought that taxable profits of its 2007 accounting period (the "2007 period") were £142,039. CES therefore claimed to carry back

£142,039 of its loss against profits of the 2007 period and to carry forward the balance of its loss (£302,709) against profits of subsequent periods. It is common ground that CES made its claim to carry back its loss for the 2008 period after 30 April 2009 which was after the deadline on which CES could, by paragraph 15 of Schedule 18 of Finance Act 1998 ("FA 1998"), apply to amend its return for its 2007 period (see [195(2)]). It was also common ground that by making this carry-forward claim, CES has to date received and retained relief for £302,709 of losses by way of reducing taxable profits in subsequent accounting periods.

73. The FTT subsequently decided, after CES made its carry back claim, that its trading profit for its accounting period ended 30 April 2007 should be increased by £540,000. There is no appeal against that conclusion.

74. CES argues that, having increased profits of the 2007 period by £540,000, the FTT was obliged to decrease those profits by £302,709 (the balance of the losses for the 2008 period that had not already been carried back).

75. HMRC, however, argue that CES's analysis of the legislation is wrong, reasoning as follows:

> (1) At the time CES claimed to carry back its loss, the time limit for amending its return for the 2007 period had expired.
>
> (2) Therefore, its claim was, by paragraphs 58(2), 58(3) and 59 of Schedule 1A of TMA, treated as a claim for discharge or repayment of tax. The regime set out in Schedule 1A should prevail over any contrary effect set out in s393A of the Income and Corporation Taxes Act 1988 ("ICTA").

76. The FTT accepted HMRC's argument and, since we will perform our own analysis, we need not set out its reasoning in detail.

Relevant legislation

77. Section 393A of ICTA as in force at the relevant time permitted companies to "carry back" losses incurred in one accounting period against profits of a previous accounting period as follows:

> (1) Subject to section 492(3), where in any accounting period ending on or after 1st April 1991 a company carrying on a trade incurs a loss in the trade, then, subject to subsection (3) below, the company may make a claim requiring that the loss be set off for the purposes of corporation tax against profits (of whatever description)—
>
> > (a) of that accounting period, and
> >
> > (b) if the company was then carrying on the trade and the claim so requires, of preceding accounting periods falling wholly or partly within the period specified in subsection (2) below;
>
> and, subject to that subsection and to any relief for an earlier loss, the profits of any of those accounting periods **shall then be treated as reduced by the amount of the loss**, or by so much of that amount as

> cannot be relieved under this subsection against profits of a later accounting period.
>
> (2) The period referred to in paragraph (b) of subsection (1) is (subject to subsection (2A) below) the period of twelve months immediately preceding the accounting period in which the loss is incurred; but the amount of the reduction that may be made under that subsection in the profits of an accounting period falling partly before the beginning of that period shall not exceed a part of those profits proportionate to the part of the accounting period falling within that period.

78. The emphasis in the above quote is our own as the words highlighted are central to the argument. It is common ground that the claim to carry back the loss for the 2008 period was necessarily a claim to carry back the entirety of that loss (to the extent that there were profits in the 2007 period available for set-off against that loss). Therefore, it is common ground that CES was not allowed to carry back part only of its £444,748 loss. In those circumstances CES argues that the treatment in s393A is mandatory. The profits of £682,039 in the 2007 period must be reduced by the loss of £444,748.

79. If s393A were the only relevant provision that would be a powerful case. However, the statutory provisions relating to carry back of losses were materially overhauled following the introduction of self-assessment for both individuals and companies. The reason for the overhaul is straightforward to understand. The ethos behind the self-assessment regime was that a taxpayer's own return for a period should be final unless specifically disturbed by, for example, a closure notice issued following an enquiry into that return. There was a degree of conflict between that ethos and the idea that a return for an earlier year could be disturbed by carry back of a loss arising in a later year.

80. Following the introduction of self-assessment for companies, paragraphs 58 and 59 of Schedule 18 of FA 1998 were enacted which provided, so far as material as follows:

> **58 Claims or elections involving more than one accounting period**
>
> (1) This paragraph applies to a claim or election for tax purposes if—
>
> > (a) the event or occasion giving rise to it occurs in one accounting period (the period to which it "relates"), and
> >
> > (b) it affects one or more other accounting periods (whether or not it also affects the period to which it relates).
>
> (2) If a company makes a claim or election which—
>
> > (a) relates to an accounting period for which the company has delivered a company tax return and could be made by amendment of the return, or
> >
> > (b) affects an accounting period for which the company has delivered a company tax return and could be given effect by amendment of the return,
>
> the claim or election is treated as an amendment of the return.
>
> The provisions of paragraph 15 (amendment of return by company) apply.

> (3) Schedule 1A to the Taxes Management Act 1970 (claims and elections not included in returns) applies to a claim or election made by a company if or to the extent that it is not—
>
> > (a) made by being included (by amendment or otherwise) in the company tax return for the accounting period to which it relates, and
> >
> > (b) given effect by being included (by amendment or otherwise) in company tax returns for the accounting periods affected by it.
>
> **59 Other claims and elections**
>
> (1) Schedule 1A to the Taxes Management Act 1970 applies to a claim or election for tax purposes which is not within paragraph 57 or 58, whether or not it is included (by amendment or otherwise) in a company tax return.
>
> (2) The provisions of this Schedule do not apply where or to the extent that the provisions of Schedule 1A apply.

81. The cross-reference to paragraph 15 in paragraph 58(2) is to a paragraph of Schedule 18 that permits a company to amend its tax return by notice. It was common ground that, by the time CES submitted its tax return for the 2008 accounting period, and made the claim to carry back its loss in the return so submitted, it was no longer in time to amend its return for the 2007 period. Therefore, the fact that HMRC retained power to amend profits of the 2007 period following completion of any enquiries did not fall within paragraph 15 and so did not cause paragraph 58(2) to apply.

82. Therefore, paragraph 58(3) does apply and imports Schedule 1A of TMA. Paragraph 4 of Schedule 1A of TMA provides as follows:

> **4 Giving effect to claims and amendments**
>
> (1) Subject to sub-paragraphs (1A), (3) and (4) below and to any other provision in the Taxes Acts which otherwise provides, an officer of the Board or the Board shall, as soon as practicable after a claim other than a partnership claim is made, or such a claim is amended under paragraph 3 above, give effect to the claim or amendment by discharge or repayment of tax.

83. Paragraph 3 of Schedule 1A of TMA provides a limited period for taxpayers to amend claims they have submitted. It is common ground that CES made no amendment to its carry back claim within the period set out in paragraph 3.

84. Accordingly, the dispute between the parties on the Carry Back Issue depends on whether the consequences of the successful claim are set out in s393A of ICTA or in paragraph 4 of Schedule 1A. CES says that s393A is the operative provision which provides for the entirety of the loss for the 2008 period to be carried back to the extent that there are profits of the 2007 period sufficient to absorb those losses. HMRC says that Schedule 1A sets out a self-contained code applicable to CES's carry back claim and that CES's failure to amend its claim within the time limit set out in paragraph 3 of Schedule 1A is fatal to any claim to carry back more than £142,039 of loss.

Discussion of the Carry Back Issue

85. In support of its argument that the treatment specified in s393A of ICTA should prevail, CES characterises the provisions of Schedule 1A of TMA as "machinery" and relies on the following extract from the judgment of Lord Carnwath in *R (Derry) v Revenue & Customs Commissioners* [2019] UKSC 19:

> 37. Turning to the TMA, it is true that words of Schedule 1B taken on their own would be apt to apply to a claim under sections 132-133. However, I do not regard that as enough to displace the clear provisions of the ITA in respect of liability. I do not see this as turning so much on whether one set of provisions is more specific than the other, but rather on the fact that the ITA is in principle the governing statute in respect of tax liability, and as such should take precedence in the absence of any indication to the contrary.

86. We do not, however, agree that *Derry* supports the conclusion that the issue before us can be determined by an analysis of whether paragraph 4 of Schedule 1A of TMA, or s393A of ICTA, should appropriately be labelled as "machinery" or "the governing statute in respect of tax liability". Rather the task, as a close reading of *Derry* demonstrates, is to construe the statutory provisions involved.

87. *Derry* concerned a claim for share loss relief. The taxpayer had claimed the relief in the 2009-10 tax year by deducting it from his "total income" for that year. Section 23 of the Income Tax Act 2007 ("ITA") specifically mentioned share loss relief as an item that was to be deducted from total income in this way. HMRC argued that, despite the express reference to share loss relief in s23 of ITA, other provisions of ITA demonstrated that the relief should not have been given by reduction of 2009-10 total income, but rather should have been treated as governed by Schedule 1B of TMA.

88. The Supreme Court's decision was that the clear stipulations set out in s23 of ITA should prevail over contrary indications that were more obscure. TMA's status as a set of provisions dealing with management was not determinative but rather was an ingredient in the process of ascertaining Parliamentary intention, as demonstrated by the following extract from Lord Carnwath's judgment:

> 36. Having taken such care to walk the taxpayer through the process of giving effect to his entitlement as part of his tax liability for the year specified by him, it would seem extraordinary for that to be taken away, without any direct reference or signpost, by a provision in a relatively obscure Schedule of another statute concerned principally, not with liability, but with management of the tax.

89. We accept HMRC's argument that in the circumstances of this case, CES's claim was governed by the provisions of Schedule 1A of TMA for the following reasons:

> (1) Unlike the situation considered in *Derry*, s393A cannot fairly be read as a comprehensive provision. Section 393A is dealing with a situation where profits of an earlier accounting period have been calculated, but subsequently a loss in a later accounting period is carried back so as to reduce taxable profits of the earlier period to less than they were thought to

be. The mere statement in s393A that profits of the earlier accounting period are to be reduced cannot deal with all the complexities arising from that situation. In particular, where tax has been paid by reference to profits of the earlier period as they were originally thought to be, a reader of s393A would realise that there may well need to be some refund or credit of that tax. Moreover, some additional provisions would be needed to displace the normal position, provided for by the self-assessment regime enacted subsequent to s393A, under which a tax return becomes final 12 months after it is filed unless there is an amendment or enquiry into that return.

(2) Therefore, while a reader of s23 of ITA considered in *Derry* would not necessarily have realised that there was more to the situation than met the eye, a reader of s393A would do so.

(3) Parliament has designated Schedule 1A of TMA as containing the provisions to apply when, as here, the claim is made after the deadline for amending the tax return for the earlier period. Paragraph 4 contains specific provisions that require (i) HMRC to act as soon as practicable and (ii) to "give effect to" the claim by making a discharge or repayment of tax which must necessarily be of a specific amount. It is not clear how HMRC could comply with the obligations imposed by paragraph 4 if the true obligation was that imposed by s393A, namely to wait and see what the profits of the earlier period finally turned out to be following the determination of any statutory appeals to the FTT.

(4) If CES's interpretation were correct, there would be both a discharge or repayment of tax under Schedule 1A and a reduction of profits under s393A. Parliament could not have intended both consequences to flow. In our judgment, the better interpretation is that Schedule 1A sets out provisions that <u>give effect to</u> the reduction of profits specified by s393A.

90. In arguing against this analysis, CES submits that Parliament could not have intended whether full statutory effect is given to s393A to depend on the mere "happenstance" of whether a claim to carry back a loss was made before or after the deadline for amending the earlier period's return. However, we regard that as a relatively weak indication since Parliament has quite clearly legislated in paragraph 58 of Schedule 18 of FA 1998 to provide for carry back claims made before this deadline to be treated differently from carry back claims made afterwards.

91. CES also pointed out that by paragraph 3(1)(b) it had just one year to amend its claim. It argued that the interpretation set out in paragraph 89 would make it difficult to exercise that right effectively. It could scarcely have been expected to realise within just one year that the FTT would increase its profits for the 2007 accounting period and so could not have acted in time to secure the full carry-back of the loss for the 2008 period that Parliament prescribed. We see the logic of this point. However, in our judgment, it is simply the result of the time limit that Parliament has imposed. It does not demonstrate that the interpretation we have set out in paragraph 89 is incorrect.

Disposition

92. The taxpayers' appeals are dismissed in their entirety, save as regards the point at paragraph 70 above, where we have invited the parties to consider an adjustment to the penalty imposed on Mr Lowe to reflect the points made in paragraphs 69 and 70 above. If this matter cannot be resolved, either party may apply to the Upper Tribunal for a determination of Ground 10. Any such application must be made no later than 21 days from the release of this decision in final form.

Signed On Original

MR JUSTICE MARCUS SMITH

JUDGE JONATHAN RICHARDS

RELEASE DATE: 17 March 2022