News
Draft FB 2018, business risk & more

Cases
VAT on unredeemed vouchers

One minute with...
Laura Charkin, partner, Goodwin

TAX JOURNAL

Insight and analysis for the business tax community

Issue 1369 | 22 September 2017

The Court of Appeal in *Hely-Hutchinson*

Should not 'fairness' be an issue of substance?

Michael Sherry | Temple Tax Chambers

Review of draft Finance Bill 2018

Claire Hooper | EY

Lessons from the first tribunal decision on SAO reasonable steps

Mark Kennedy, Tim Hayle & Tharaka Mudalige | Deloitte

The latest private client developments that matter

Andrew Goldstone & Nicola Simmons | Mishcon de Reya

The new VAT disclosure regime: from VADR to DOTAS

Etienne Wong | 15 Old Square Chambers

Ask an expert: Technical services and withholding tax

Stuart Rogers & Chris Harrison | PKF Francis Clark

Analysis

Hely-Hutchinson: was HMRC merely unfair or 'conspicuously unfair'?

Speed read

How should HMRC treat taxpayers who are substantially in the same position but procedurally in different stages of resolving their affairs with HMRC, when it changes its mind about the correct view of the law? After *Mansworth v Jelley* in 2003, the Revenue's web guidance allowed many claims for capital losses. Six years later, it changed its mind, even though some cases were still unresolved. HMRC applied the revised view of the law. Mr Hely-Hutchinson applied for judicial review, as he had been given a legitimate expectation as to how he would be dealt with. Although he could show no detrimental reliance, he claimed that to treat him differently from those already settled purely because of procedural reasons was 'conspicuously unfair'. Whipple J agreed but the Court of Appeal disagrees. Should not 'fairness' be an issue of substance?

Michael Sherry
Temple Tax Chambers
Michael Sherry is a tax counsel and head of chambers at Temple Tax. He advises on all areas of tax with some emphasis on OMBs, private client issues, accounting issues, and financial services. Cases of note include *Mansworth v Jelley, Grays Timber, College of Estate Management, Langham v Veltema,* and *Forde and McHugh.* Email: michael.sherry@templetax.com; tel: 020 7353 7884.

Establishing the facts

In the Court of Appeal's decision in *R (oao Hely-Hutchinson) v HMRC* [2017] EWCA Civ 1075 (reported in *Tax Journal*, 4 August 2017), the Court of Appeal agreed with the general approach of the judge below (Whipple J) but took a different view of the facts.

Those facts may be summarised briefly. Mr Hely-Hutchinson worked for ABN Amro PLC (ABN). ABN granted him share options in 1989 in respect of his employment. He exercised the options in 1999 and 2000; and, in both cases, he sold the shares shortly thereafter. He filed his tax returns for 1998/99 and for 1999/2000 on the basis that no liability to capital gains tax arose.

He prepared his returns on the following basis: he computed his gains by taking the actual proceeds of selling the shares; and against that he set the actual cost of exercising the options and (pursuant to TCGA 1992 s 120) a further deduction. This was equal to the amount upon which he was subject to income tax on exercising the options; being the market value of the shares acquired less any amounts actually paid to acquire the option and to acquire the shares on exercise. The upshot was that the deductions were equal to the shares' market value at the time of exercise; and as the shares acquired were sold almost immediately, there was no gain or loss on their disposal.

In December 2002, the Court of Appeal decided, in *Mansworth v Jelley* [2003] STC 53, that the figure to use for base costs when calculating the gain on employment options was the market value at the date of the exercise of the options. Because Mr Jelley had been non-resident at the time the options were granted, there was no question of him being subjected to income tax at that time on the gain realised on the exercise of the options.

A change of HMRC guidance

Following that decision in 2003, the Revenue issued guidance in the form of a web statement ('the web guidance'). It states that the Revenue did not intend to appeal the decision in *Mansworth v Jelley*; however, so far as past cases were concerned, the base cost of employment shares acquired by options was to be calculated as follows: where employees acquired options upon which they suffered income tax on exercise, the base cost was to be arrived at by adding the market value at the time of acquisition to the amount upon which income tax was levied. (Broadly speaking, then as now income tax was levied on the difference between, on the one hand, the amount paid to acquire the option plus the amount paid to exercise it, and on the other, the market value of the shares at the time of exercise.)

> The case turned on the assessment of what is and is not 'conspicuous unfairness'. We can all have a view on that!

The Finance Act 2003 amended TCGA 1992 for any options exercised after 9 April 2003. This put beyond doubt, going forward, that the position was as the Revenue had thought it to be before *Mansworth v Jelley*; i.e. computed in the way in which Mr Hely-Hutchinson had originally computed his gains.

Originally, Mr Hely-Hutchinson had submitted his tax returns on the basis of no gain no loss; however, in the light of the *Mansworth v Jelley* web guidance, he amended his returns adding the market value to his base cost and thus giving rise to substantial losses which he claimed in the amendments to his returns. The Revenue opened enquiries into the relevant returns. There was correspondence which stretched over many years, until 2009, when HMRC issued Revenue & Customs Brief 30/09, withdrawing the web guidance previously issued. This was on the basis that the web guidance was wrong in law.

Brief 30/09 said that the web guidance would no longer be applied. It also said that, going forward, in any case relating to the exercise of an option before 10 April 2003, the base cost of shares acquired upon the exercise of an option would be arrived at by taking the market value of the shares at the date of acquisition (on exercise), and any amount treated as income arising on exercise and charged to income tax would be disregarded.

Brief 30/09 also said that this revised treatment would apply to any enquiry or appeal still open at the date Brief 30/09 was released, where what was in issue was *Mansworth v Jelley* losses. This covered Mr Hely-Hutchinson's case, so he could now expect to have his loss claims disallowed.

However, in Brief 60/09 HMRC then said it would not apply this new approach in cases where the taxpayer had a 'legitimate expectation' that he could depend upon the original web guidance. In this context, it was explained that the benefit of this legitimate expectation treatment would

be extended only to taxpayers who could demonstrate that they had 'reasonably acted in reliance on the previous guidance and would suffer detriment from the correct application of the statute'. This meant that the taxpayer had to show that he had acted in reliance on the web guidance; and that he must have done or refrained from doing something as a direct consequence of the web guidance. In this context, HMRC also made plain that it only accepts that the taxpayer had suffered detriment as a result of such reliance if they had suffered a real loss, rather than merely a disappointment or upset.

Necessary reliance and detriment

Mr Hely-Hutchinson found himself in the position of having an open enquiry into his *Mansworth v Jelley* loss claims, but he was unable to show the necessary reliance and detriment. He brought proceedings by way of judicial review of HMRC's decision to withdraw the web guidance from him in these circumstances, and was successful at first instance before Whipple J [2016] STC 962.

The judge had held that a remedy for breach of legitimate expectation can be available where there is no detrimental reliance, provided that the withdrawal of the promised treatment nevertheless amounted to 'conspicuous unfairness'. She held that while it was a matter for HMRC to decide on any particular case, there was little material in front of the court indicating why HMRC had decided to confine the exceptions to its change of policy to cases where detrimental reliance could be shown, and why it thought it was not conspicuously unfair to withdraw the treatment set out in the web guidance from people like Mr Hely-Hutchinson and those in similar circumstances; i.e. having an enquiry or unresolved appeal on foot when the policy changed.

Whipple J indicated that, on the material in front of her, her own view was that such treatment did appear to be conspicuously unfair. However, she did not hold that Mr Hely-Hutchinson's treatment was necessarily unlawful. Rather, she required HMRC to reconsider its position in the light of her judgment.

Comparative and conspicuous unfairness?

The Court of Appeal adopted a similar approach. The decision of the court was given by Lady Justice Arden (with whom McCombe and Sales LJJ, agreed). The Court of Appeal dealt with the matter as giving rise to three issues.

The first was whether the policy adopted by HMRC involved comparative unfairness (by withdrawal of the web guidance) between those whose claims had already been settled in respect of past years and those whose claims in respect of past years remained open. On this issue, the Court of Appeal held that there was a fundamental difference between those with claims still 'open' and those whose claims were settled. Therefore, the comparative unfairness criteria was not satisfied, as all those with open claims had been treated in the same way.

The second issue was whether or not the withdrawal of the web guidance amounted to a matter of unfairness other than by reference to legitimate expectation or was incompatible with the European Convention on Human Rights Protocol 1 article 1, which guarantees the right to private property. Here, the argument for the taxpayer was that he was being unlawfully discriminated against because he was not receiving the same treatment as those whose claims had been settled before HMRC changed its mind on the web guidance. This was discriminatory because all those whose claims had not been settled were those whose employers were involved in schemes similar to that used by ABN Amro; they were all employed in the financial services industry.

The court rejected this argument on the basis that there was no discrimination against those in the financial services industry, who were probably under investigation by reason of HMRC's concern about the national insurance liability of their employers in respect of the share option schemes in question. More particularly, the court held that 'the Respondent's [Mr Hely-Hutchinson's] case on unfairness stands or falls, as I see it, on the facts of his individual case, taking into account the general principles of legitimate expectations as they apply to the Revenue'.

The third issue addressed by the court was whether, given that the decision to withdraw the guidance was lawful, it could be said that the way in which the officer had approached the individual case was itself so unfair as to render it unlawful. The Court of Appeal held that the test here was again that of showing 'conspicuous unfairness'.

> In substance, the two sub-groups were in the same position. The only difference was a procedural one

The court reached the conclusion that the threshold had not been crossed. All that had happened was that Mr Hely-Hutchinson had been returned to the position he had been in when he committed himself to the transactions in question in the first place. Moreover, the court noted that HMRC had also warned Mr Hely-Hutchinson, in the years during which his affairs had been under enquiry, that it did not accept his *Mansworth v Jelley* loss claims because, for the time being, they were thought to be connected with a national insurance tax avoidance scheme used by his employer. This was not the same as rejecting the claims but, the court held, it certainly put Mr Hely-Hutchinson on notice that he could not rely upon the claims during this interim period. (There was no challenge to the conduct of the enquiries before the Court of Appeal.) Although there were a large number of other claims which had been resolved under the 2003 web guidance, the existence of such claims and the number of them were held to be immaterial because 'this does not give rise to unfairness because the case of people who have closed years and open years is different'.

The court did show a degree of sympathy for those in the position of Mr Hely-Hutchinson: 'The decisions under challenge are clearly hard for those whose claims were outstanding in 2009. Nonetheless, in my judgment, the level of unfairness is not that of conspicuous unfairness.'

Comment

What does and what does not amount to conspicuous unfairness? Surely, this is a question of fact to be decided upon in the light of all the circumstances and is what we lawyers often call a 'jury question'. It would be interesting to know, from the readers of this magazine, how many think that HMRC's treatment of Mr Hely-Hutchinson (and those in a similar position) is conspicuously unfair; and how many think that, whilst hard, its treatment falls short of that threshold? There are few, if any, applicable comparative decisions by the courts.

Nevertheless, the case turned on the assessment of what

is and is not 'conspicuous unfairness'. We can all have a view on that!

The Court of Appeal approached the essential issue of fairness by splitting it up. Was it fair for HMRC to withdraw the web guidance as a matter of policy? And, if the policy was OK, was there something in Mr Hely-Hutchinson's particular circumstances that made the decision about him not OK? Was there any discrimination?

In answering these questions, the Court of Appeal treated those whose appeals were still open as being in a fundamentally different position from those whose enquiries or appeals were settled before the web guidance was withdrawn. It seems difficult to me, and I think it will be difficult for any ordinary member of the public, to find it anything other than 'conspicuously unfair' to have different treatment for those whose enquiries were closed before HMRC changed its mind, and those whose enquiries were closed afterwards. In substance, the two sub-groups were in the same position. The only difference was a procedural one. From a non-lawyer's point of view, all these people were all in exactly the same position when they started out. The only reason they fall into different groups is because of HMRC's actions: firstly, in not settling one subset of the group of cases within the same time span as it had managed to settle others within the group; and secondly, because HMRC had changed their mind.

The issue of the public's confidence in HMRC is of great importance

There was nothing the taxpayers in Mr Hely-Hutchinson's subset could do about those matters. They started off in exactly the same position as the rest of the group – as those whose claims were settled. Why it can be thought that there is no 'conspicuous unfairness' in them ending up being treated differently, merely because of the way in which the procedural rules around the settling of appeals operate, is a mystery. While it must be accepted that a public body can change its policy, in deciding how that change should be applied it seems self-evident that HMRC should have regard to how it has already treated those with whom it has already settled, and whose original circumstances were in substance the same as those who are left to sort out.

It seems to me that any ordinary non-lawyer would recognise that treating these people differently, simply because of procedural differences which were always within the hands of HMRC, is 'conspicuously unfair'.

In the Court of Appeal, counsel for HMRC had submitted that Mr Hely-Hutchinson, and those like him whose claims had not been settled, were in a materially different position from those whose claims have been closed. This was said to flow from TMA 1970 s 29(4) and (5). That submission by HMRC was accepted by the Court of Appeal without further analysis as to why it was thought to be correct: the procedural difference between the two groups is identified and said to be material, but why that should be so in these particular circumstances is not explained. There is no evaluation of the unfairness as perceived either specifically by the taxpayer, in this case Mr Hely-Hutchinson, or as would be perceived by the general body of taxpayers concerning this type of treatment by HMRC.

It may be that by cutting the case into three separate issues, the Court of Appeal lost sight of the overall question: does it feel wrong and does it look (is it conspicuous) that it is wrong/unfair in all the circumstances?

The first instance judge, Whipple J, seemed to have this right when she said: 'the reasons the claimant finds himself in this position is because of a mistake made by [the Revenue] in 2003. That factor, although perhaps not carrying much weight on its own, is part of the overall picture and should have been taken into account … [The Revenue] should not be able to profit from a mistake, by correcting that mistake in such a way as to deprive an individual of a benefit that he would have had but for the correction.'

And a little earlier the judge had said: 'I accept that [TMA 1970] ss 9A and 29(2) give rise to factual and legal differences between the sub-set and the rest of the cohort. But those differences do not make it fair to impose the tax on the sub-set, they just give [the Revenue] the opportunity to do so. The effect of those provisions was that the claims by the sub-set remained within [the Revenue's] reach in 2009 and beyond, whereas the claims by the rest of the 2003 cohort were by that time dead. … That is not just a matter of private complaint by those who are in the sub-set and have to pay more tax than their comparators, it is a public interest issue because taxpayers have been treated differently, and that risks undermining public confidence in a fair and non-discriminatory tax system … [C]omparative fairness was, in my judgment, a significant issue in this case, which should have been considered by [the decision making officer] in conducting the balancing exercise.'

One could add to this passage that it is also something which should have been considered by HMRC when it released Brief 30/09 withdrawing the earlier web guidance.

The issue of the public's confidence in HMRC is of great importance. If public confidence in the ability of HMRC to act fairly is undermined, then there is a greater probability that the public will take matters into their own hands and simply fail to comply in a lawful and open way with the authorities. Hitherto, the public in this country has been overwhelmingly compliant in its dealings with HMRC over the years. However, there is a clear feeling that HMRC (perhaps with political support) is now acting in ways which are perceived to be unfair. Anecdotally, it appears that amongst the member nations of the OECD, HMRC is the least 'trusted' fiscal authority. In another context, the former chairman of the Treasury Select Committee wrote an open letter to the chancellor about the way in which HMRC has been issuing accelerated payment notices and partnership payment notices. If the decision in this case stands, then it will further undermine the ability of HMRC to claim that it acts in a fair way, in the ordinary sense of the word 'fair'.

It is understood that Mr Hely-Hutchinson is seeking permission from the Supreme Court to appeal against the Court of Appeal's decision in his case. He has throughout been represented on a *pro bono* basis; and at each level, while the court has had a costs jurisdiction, there has been an order in place preventing HMRC from recovering costs from the taxpayer in the event that HMRC wins. It would be impossible for him to pursue an appeal to the Supreme Court without a similar order. Whether or not he gets such an order and whether or not he gets permission is yet to be seen but we must hope he does. ■

For related reading visit www.taxjournal.com

- Cases: *HMRC v R Hely Hutchinson* (1.8.17)
- *Hely-Hutchinson*, legitimate expectation and judicial review (Mark Whitehouse & Peter Halford, 2.12.15)
- *Mansworth v Jelley* and trust in HMRC (Lynnette Bober, 7.6.12)