Neutral Citation: [2022] UKFTT 00165 (TC)

Case Number: TC08492

FIRST-TIER TRIBUNAL
TAX CHAMBER

By remote video hearing

Appeal reference: TC/2020/01415

FOLLOWER NOTICE PENALTIES – incentive scheme implemented by Appellant - whether decision of Supreme Court in UBS was a relevant judicial ruling, whether reasonable in all the circumstances not to take the necessary corrective action – level of mitigation – appeal against the imposition of the penalties dismissed – appeal against quantum allowed in part

Heard on: 8-9 September and 15-16 November 2021
Judgment date: 23 May 2022

Before

TRIBUNAL JUDGE JEANETTE ZAMAN

Between

WHISPERING SMITH LTD

Appellant

and

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Ximena Montes Manzano, counsel, instructed by PwC

For the Respondents: Marika Lemos and Matthew Bignell, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

DECISION

INTRODUCTION

1. Whispering Smith Ltd ("WS") has appealed against two penalties (the "FN penalties") which were issued to it under s208 and s211 Finance Act 2014 ("FA 2014") on 13 March 2018 for failure to take corrective action in response to a follower notice ("FN") issued by HMRC. The FN was issued on the basis that the decision of the Supreme Court in *UBS AG v HMRC and DB Group Services (UK) Ltd v HMRC* [2016] UKSC 13 (together referred to as "*UBS"*) was a "relevant judicial ruling".

2. The FN was issued in respect of WS's entry into and participation in a series of transactions in the accounting period ended March 2004 which were referred to in the papers as the Deloitte Short Term Equity Deferral Plan, STEED or STEP arrangements (the "STEP Arrangements"). HMRC assessed penalties of £1,607,791.30 in respect of income tax and £554,466.31 in respect of NICs.

3. The penalty assessments were calculated at the maximum amount specified by the legislation. HMRC have since indicated in correspondence with WS that they would apply a reduction of 20% for cooperation, which would result in an 8% reduction in quantum of the penalty assessments from 50% to 42% (a total reduction of £345,961.22 from the amounts stated to be due under the penalty assessments). The penalty assessments have not, however, been reduced (as HMRC are unable to make such an amendment by reason of s213 FA 2014).

4. WS has appealed against the FN penalties on the basis that UBS is not a relevant judicial ruling and, alternatively, it was reasonable in all the circumstances for WS not to comply with the FN. Even if a penalty is payable, WS submit that they should have received the maximum level of mitigation available, reducing the penalty to 10% of the denied advantage. HMRC's position is that penalties are due and that the reduction for cooperation be 20% of the denied advantage.

5. For the reasons set out below, I have concluded that the FN penalties were properly imposed – UBS is a "relevant judicial ruling" and WS has not established that it was reasonable in all the circumstances not to take the necessary corrective action by the specified date. However, I have also concluded that the quality of WS' co-operation merits a further reduction in the quantum of the FN penalties – mitigation of 40% is allowed and the FN penalties are reduced to 34% of the denied advantage.

FACTS

6. WS (formerly Rajan Imports Limited) was incorporated in 1985 and trades in the import and wholesale distribution of fashion wear. During the accounting period ended 31 March 2004 the directors were Krishnan Lal Kumar, his sons Rajan Kumar ("Rajan") and Sanjay Kumar ("Sanjay"), Diane Heslop, Michelle Keeling and Peter Morley.

7. WS sought advice from Deloitte & Touche LLP ("Deloitte"). Around February 2003, John Tillotson of Deloitte presented a few options to the company including a Short Term Equity Deferral Plan. WS took advice from Peter Trevett QC in August 2003 and decided to enter into the STEP Arrangements, ie the Short Term Equity Deferral Plan which had been presented to them.

Implementation of STEP Arrangements

8. The rationale for entering into the STEP Arrangements and the setting of the Performance Condition (as defined below) are considered separately under Additional Findings of Fact.

9. The following steps took place:

(1) On 1 October 2003, Rajan Group plc (which has since changed its name to Whispering Smith Group plc ("WSGP"), and is the parent company of WS) settled the Rajan Group Plc (No 1) Employee Benefit Trust ("EBT1") and the Rajan Group Plc (No 2) Employee Benefit Trust ("EBT2"), both with Jersey-based trustees.

(2) On 22 October 2003, Chatam Limited ("Chatam") was incorporated in Jersey. The authorised share capital of Chatam was 10,000,002 divided into 1 "A" Ordinary Share, 1 "B" Ordinary Share, and 10,000,000 redeemable shares of £1 each (the "Redeemable Shares").

(3) On 11 November 2003, the "A" and "B" Ordinary Shares were transferred to WSGP, and Rajan and Sanjay were appointed as directors of Chatam.

(4) On 17 November 2003, WSGP applied for the allotment of 8,000,000 Redeemable Shares in Chatam at par. The application was approved by the directors of Chatam on the same day and WSGP arranged for £8m to be transferred to Chatam's bank account for the Redeemable Shares.

(5) On 21 November 2003:

(i) WSGP transferred the "B" share in Chatam to the trustees of EBT2 for nil consideration.

(ii) WSGP awarded 50 Redeemable Shares to both Rajan and Sanjay.

(iii) 10 Redeemable Shares were transferred to EBT1 for nil consideration.

(6) On 17 December 2003, WSGP awarded a further 7,999,890 Redeemable Shares in Chatam to certain employees of WS/WSGP, as set out in the table below:

Name	Award – 21 Nov 2003	Award – 17 Dec 2003	Total
Sanjay Kumar	50	3,992,082	3,992,132
Rajan Kumar	50	3,992,082	3,992,132
Michelle Keeling	-	10,000	10,000
Diane Heslop	-	3,050	3,050
Sian Mills	-	2,676	2,676
	100	**7,999,890**	**7,999,990**

(7) The awards carried a condition, as set out at Article 9.1 in the Article of Association of Chatam, that the holder(s) of the shares must transfer their shares in Chatam for nil consideration to the holder of the "B" share in Chatam (ie to the trustees of EBT2) if the turnover of WS recorded in the management accounts for the three-month period ended at 23:59 on 31 January 2004 was less than £12m (the "Performance Condition"). The award letters to each employee included an indemnity clause under which, if the employee accepted the award, the employee indemnified WS/WSGP for any PAYE tax and NICs arising in relation to the award.

(8) On 29 December 2003, the 10 Redeemable Shares held by EBT1 were transferred to Peter Le Breton, a Jersey resident.

(9) The Performance Condition was achieved, and the Redeemable Shares vested unconditionally in the shareholders.

(10) On 2 and 9 April 2004, Redeemable Shares in Chatam were transferred as set out in the table below:

Shareholder	Shareholding	Transfer to	Transferred 2 April 2004	Transferred 9 April 2004

Michelle Keeling	10,000	Sanjay Kumar	2,500	2,500
		Rajan Kumar	2,500	2,500
Diane Heslop	3,050	Sanjay Kumar	1,525	-
		Rajan Kumar	1,525	-
Sian Mills	2,676	Sanjay Kumar	1,338	-
		Rajan Kumar	1,338	-
Peter Le Breton	10	Sanjay Kumar	-	10
	15,736		**10,726**	**5,010**

(11) In May 2004, both Rajan and Sanjay transferred their Redeemable Shares into life interest settlements ("LIS"). The trustees of these settlements were based in Jersey.

(12) On 6 August 2004, Chatam was wound up and the assets of the company, including the £8m share subscription proceeds, were distributed to the shareholders of the Redeemable Shares, being the trustees of the LIS.

(13) Rajan and Sanjay resigned as directors of Chatam as part of the winding-up process.

10. The Redeemable Shares were thus awarded to five individuals: Rajan and Sanjay (both directors, both of whom were involved in sales, buying and sourcing), Ms Heslop (Finance Director), Mrs Keeling (who worked in business operations, with a focus on importing, logistics and banking facilities, and had been the account manager for certain large accounts) and Ms Mills (who had run the London office and had been a major contributor to design, sales and sourcing). (I infer that Mr Le Breton, who received 10 Redeemable Shares from EBT1 and later transferred them to Sanjay, had no connection with the business of WS.)

HMRC enquiry and final determinations and decisions

11. HMRC opened enquiries into WS's implementation of the STEP Arrangements on 10 November 2006.

12. On 4 February 2009 HMRC issued a determination under regulation 80 Income Tax (Pay As You Earn) Regulations 2003 (the "Regulation 80 Determination") for £3,215,582.60 and decisions under s8 Social Security (Transfer of Functions, etc.) Act 1999 (the "Section 8 Decisions") for a total of £1,108,932.63.

13. WS appealed against the Regulation 80 Determination and the Section 8 Decisions. Those appeals were stayed behind what became the appeals of UBS and Deutsche Bank. Those lead cases were determined by the Supreme Court in *UBS* on 9 March 2016.

Follower Notice and Accelerated Payment Notices

14. HMRC issued the FN and Accelerated Payment Notices ("APNs") in respect of the STEP Arrangements on 17 February 2017. The amounts of the APNs were:

(1) PAYE - £3,215,582.60; and

(2) NICs - £1,108,932.63.

15. The date specified in the APNs and FN for payment of the specified amounts and the taking of corrective action (respectively) was 23 May 2017.

16. The FN set out HMRC's position in relation to the required conditions. The notice sets out HMRC's opinion that there is a final judicial ruling which is relevant to the chosen

arrangements for the purposes of s205(3) FA 2014. The relevant judicial ruling is then described as follows:

> "On 9 March 2016 the Supreme Court gave a ruling the in the cases of UBS AG v Commissioners for Her Majesty's Revenue and Customs, and DB Group Services (UK) Ltd v Commissioners for Her Majesty's Revenue and Customs [2016] UKSC 13, (the "UBS" case and the "DB" case). The ruling was that the arrangements used in those cases do not achieve the intended result for tax and Class 1 National Insurance Contributions ("NICs").
>
> You have used a similar scheme…
>
> We consider the ruling in the UBS and DB cases is relevant to you as it relates to earnings and the relevant Class 1 NICs thereon and the ruling is now a final ruling. We also consider that the principles laid down or the reasoning given in that ruling would, if applied to your arrangements, deny the asserted advantage…"

17. The notice then referred to certain details of the STEP Arrangements as implemented by WS and to certain aspects of the facts in *UBS* and various paragraphs of the decision of the Supreme Court.

18. WS made representations to HMRC on 12 May 2017 and HMRC upheld the FN and APNs on 23 August 2017.

19. WS sent a letter before claim for judicial review ("JR") to HMRC on 15 September 2017 and then issued a claim for JR against the FN on 3 November 2017.

20. On 17 November 2017 HMRC applied to the court for a stay of the JR proceedings pending the final determination of the case of *R (oao Haworth) v HMRC*. A consent order for that stay was endorsed by the court on 22 November 2017.

Follower Notice Penalties

21. HMRC issued two penalty assessments for failure to comply with the FN – the FN penalties - on 13 March 2018, in the following amounts:

(1) PAYE - £1,607,791.30; and

(2) NICs - £554,466.31.

22. WS appealed against both penalties on 9 April 2018.

Settlement of disputed tax

23. On 13 September 2019, WS and HMRC entered into a settlement agreement in respect of the disputed tax in respect of the STEP Arrangements and another incentive plan (referred to as the "DOTAS Arrangements") which had been implemented by WS in the subsequent accounting period (but is not the subject of this appeal). The settlement agreement did not cover the FN penalties.

24. WS filed a Notice of Discontinuance of its JR claim on 11 December 2019.

25. WS notified its appeal against the FN penalties to the Tribunal on 27 March 2020.

RELEVANT LEGISLATION

26. The relevant provisions of FA 2014 are set out below:

> **"204 Circumstances in which a follower notice may be given**
>
> (1) HMRC may give a notice (a "follower notice") to a person ("P") if Conditions A to D are met.
>
> (2) Condition A is that—

(a) a tax enquiry is in progress into a return or claim made by P in relation to a relevant tax,

or

(b) P has made a tax appeal (by notifying HMRC or otherwise) in relation to a relevant tax,

but that appeal has not yet been—

(i) determined by the tribunal or court to which it is addressed, or

(ii) abandoned or otherwise disposed of.

(3) Condition B is that the return or claim or, as the case may be, appeal is made on the basis that a particular tax advantage ("the asserted advantage") results from particular tax arrangements ("the chosen arrangements").

(4) Condition C is that HMRC is of the opinion that there is a judicial ruling which is relevant to the chosen arrangements.

(5) Condition D is that no previous follower notice has been given to the same person (and not withdrawn) by reference to the same tax advantage, tax arrangements, judicial ruling and tax period.

(6) A follower notice may not be given after the end of the period of 12 months beginning with the later of—

(a) the day on which the judicial ruling mentioned in Condition C is made, and

(b) the day the return or claim to which subsection (2)(a) refers was received by HMRC or (as the case may be) the day the tax appeal to which subsection (2)(b) refers was made.

205 "Judicial ruling" and circumstances in which a ruling is "relevant"

(1) This section applies for the purposes of this Chapter.

(2) "Judicial ruling" means a ruling of a court or tribunal on one or more issues.

(3) A judicial ruling is "relevant" to the chosen arrangements if—

(a) it relates to tax arrangements,

(b) the principles laid down, or reasoning given, in the ruling would, if applied to the chosen arrangements, deny the asserted advantage or a part of that advantage, and

(c) it is a final ruling.

(4) A judicial ruling is a "final ruling" if it is—

(a) a ruling of the Supreme Court, or

(b) a ruling of any other court or tribunal in circumstances where—

(i) no appeal may be made against the ruling,

(ii) if an appeal may be made against the ruling with permission, the time limit for applications has expired and either no application has been made or permission has been refused,

(iii) if such permission to appeal against the ruling has been granted or is not required, no appeal has been made within the time limit for appeals, or

(iv) if an appeal was made, it was abandoned or otherwise disposed of before it was determined by the court or tribunal to which it was addressed.

(5) Where a judicial ruling is final by virtue of sub-paragraph (ii), (iii) or (iv) of subsection (4)(b), the ruling is treated as made at the time when the sub-paragraph in question is first satisfied.

208 Penalty if corrective action not taken in response to follower notice

(1) This section applies where a follower notice is given to P (and not withdrawn).

(2) P is liable to pay a penalty if the necessary corrective action is not taken in respect of the denied advantage (if any) before the specified time.

(3) In this Chapter "the denied advantage" means so much of the asserted advantage (see section 204(3)) as is denied by the application of the principles laid down, or reasoning given, in the judicial ruling identified in the follower notice under section 206(a).

(4) The necessary corrective action is taken in respect of the denied advantage if (and only if) P takes the steps set out in subsections (5) and (6).

(5) The first step is that—

(a) in the case of a follower notice given by virtue of section 204(2)(a), P amends a return or claim to counteract the denied advantage;

(b) in the case of a follower notice given by virtue of section 204(2)(b), P takes all necessary action to enter into an agreement with HMRC (in writing) for the purpose of relinquishing the denied advantage.

(6) The second step is that P notifies HMRC—

(a) that P has taken the first step, and

(b) of the denied advantage and (where different) the additional amount which has or will become due and payable in respect of tax by reason of the first step being taken.

(7) In determining the additional amount which has or will become due and payable in respect of tax for the purposes of subsection (6)(b), it is to be assumed that, where P takes the necessary action as mentioned in subsection (5)(b), the agreement is then entered into.

(8) In this Chapter—

"the specified time" means—

(a) if no representations objecting to the follower notice were made by P in accordance with subsection (1) of section 207, the end of the 90 day post-notice period;

(b) if such representations were made and the notice is confirmed under that section (with or without amendment), the later of—

(i) the end of the 90 day post-notice period, and

(ii) the end of the 30 day post-representations period;

"the 90 day post-notice period" means the period of 90 days beginning with the day on which the follower notice is given;

"the 30 day post-representations period" means the period of 30 days beginning with the day on which P is notified of HMRC's determination under section 207.

(9) No enactment limiting the time during which amendments may be made to returns or claims operates to prevent P taking the first step mentioned in subsection (5)(a) before the tax enquiry is closed (whether or not before the specified time).

(10) No appeal may be brought, by virtue of a provision mentioned in subsection (11), against an amendment made by a closure notice in respect of a tax enquiry to the extent that the amendment takes into account an amendment made by P to a return or claim in taking the first step mentioned in subsection (5)(a) (whether or not that amendment was made before the specified time).

(11) The provisions are—

(a) section 31(1)(b) or (c) of TMA 1970,

(b) paragraph 9 of Schedule 1A to TMA 1970,

(c) paragraph 34(3) of Schedule 18 to FA 1998,

(d) paragraph 35(1)(b) of Schedule 10 to FA 2003, and

(e) paragraph 35(1)(b) of Schedule 33 to FA 2013.

209 Amount of a section 208 penalty

(1) The penalty under section 208 is 50% of the value of the denied advantage.

(2) Schedule 30 contains provision about how the denied advantage is valued for the purposes of calculating penalties under this section.

(3) Where P before the specified time—

(a) amends a return or claim to counteract part of the denied advantage only, or

(b) takes all necessary action to enter into an agreement with HMRC (in writing) for the purposes of relinquishing part of the denied advantage only,

in subsections (1) and (2) the references to the denied advantage are to be read as references to the remainder of the denied advantage

210 Reduction of a section 208 penalty for co-operation

(1) Where—

(a) P is liable to pay a penalty under section 208 of the amount specified in section 209(1),

(b) the penalty has not yet been assessed, and

(c) P has co-operated with HMRC,

HMRC may reduce the amount of that penalty to reflect the quality of that cooperation.

(2) In relation to co-operation, "quality" includes timing, nature and extent.

(3) P has co-operated with HMRC only if P has done one or more of the following—

(a) provided reasonable assistance to HMRC in quantifying the tax advantage;

(b) counteracted the denied advantage;

(c) provided HMRC with information enabling corrective action to be taken by HMRC;

(d) provided HMRC with information enabling HMRC to enter an agreement with P for the purpose of counteracting the denied advantage;

(e) allowed HMRC to access tax records for the purpose of ensuring that the denied advantage is fully counteracted.

(4) But nothing in this section permits HMRC to reduce a penalty to less than 10% of the value of the denied advantage

213 Alteration of assessment of a section 208 penalty

(1) After notification of an assessment has been given to a person under section 211(2), the assessment may not be altered except in accordance with this section or on appeal.

(2) A supplementary assessment may be made in respect of a penalty if an earlier assessment operated by reference to an underestimate of the value of the denied advantage.

(3) An assessment or supplementary assessment may be revised as necessary if it operated by reference to an overestimate of the denied advantage; and, where more than the resulting assessed penalty has already been paid by the person to HMRC, the excess must be repaid.

214 Appeal against a section 208 penalty

(1) P may appeal against a decision of HMRC that a penalty is payable by P under section 208.

(2) P may appeal against a decision of HMRC as to the amount of a penalty payable by P under section 208.

(3) The grounds on which an appeal under subsection (1) may be made include in particular–

(a) that Condition A, B or D in section 204 was not met in relation to the follower notice,

(b) that the judicial ruling specified in the notice is not one which is relevant to the chosen arrangements,

(c) that the notice was not given within the period specified in subsection (6) of that section, or

(d) that it was reasonable in all the circumstances for P not to have taken the necessary corrective action (see section 208(4)) in respect of the denied advantage.

…

(9) On an appeal under subsection (2), the tribunal may–

(a) affirm HMRC's decision, or

(b) substitute for HMRC's decision another decision that HMRC had power to make."

ISSUES

27. WS did not dispute that it had failed to take corrective action in respect of the denied advantage before the specified date (which had initially been specified as 23 May 2017 but was then extended to 28 September 2017 and later to 30 October 2017).

28. WS appealed against the FN penalties on the basis that:

(1) The judicial ruling relied upon by HMRC in the FN, namely the decision of the Supreme Court in *UBS*, is not a relevant judicial ruling as defined by s205(3) and that Condition C in s204(4) was therefore not satisfied.

(2) It was in any event reasonable in all the circumstances for WS not to comply with the FN.

(3) Even if a penalty is properly payable, WS should have received full mitigation (reducing the penalty to 10% of the denied advantage).

29. HMRC rejects these arguments although, as noted in the Introduction, HMRC is not seeking to support the level of penalty that was actually issued (ie the maximum penalty), but submits that mitigation of only 20% should be allowed.

30. The parties disagreed as to where the burden of proof lies in respect of the first ground of appeal. (WS accepted that, once HMRC has established that the FN penalties were validly issued (which, in its submission, included establishing that *UBS* is a relevant judicial ruling), WS bears the burden of establishing that it was reasonable in all the circumstances not to comply and as to the level of mitigation sought.)

31. HMRC accepted that there is an initial burden of proof on HMRC where it has issued a penalty assessment which has been appealed. However, HMRC's position was that this is limited to showing the circumstances giving rise to the challenged penalty exist, and in the present appeal it was not disputed that:

(1) the FN was issued;

(2) the necessary corrective action was not taken by the specified date; and

(3) the amount of the penalty has been correctly computed in accordance with the statutory provisions.

32. On this basis, HMRC's position was that there is nothing further for it to discharge and the burden is on WS to show that the ground of appeal relied on – ie its submission that UBS is not a relevant judicial ruling - is satisfied.

33. A taxpayer does not have a right of appeal against the issue of a follower notice and, as with APNs and partner payment notices ("PPNs"), must challenge their validity by means of a claim for JR. The Court of Appeal has decided in *Beadle v HMRC* [2020] EWCA Civ 652 that the FTT has no jurisdiction to entertain a public law challenge to the validity of a PPN in the course of an appeal against a penalty notice. Relevant to that decision was the fact that statutory appeal rights continue to apply in respect of the underlying tax liability. The position in respect of follower notices is different, and s214(3) sets out the grounds on which an appeal may be made against liability to a FN penalty which include (at s214(3)(a) to (c)) matters relevant to the validity of the notice. One such ground is that on which WS relies, namely that the judicial ruling specified in the notice is not one which is relevant to the chosen arrangements (s214(3)(b)).

34. WS argues that the burden of proof is different as between the ground in s214(3)(b) (and, by implication, grounds s214(3)(a) and (c)) in comparison to the ground of appeal in s214(3)(d), where it accepts that it bears the burden of showing it was reasonable in all the circumstances not to have taken the necessary corrective action. I do not accept that there is such a difference.

35. WS's argument is essentially that s208 permits the issuance of a penalty in circumstances where a follower notice has been issued, and in establishing that the circumstances entitling it to issue a penalty assessment are met, HMRC must establish that a valid follower notice was

issued. Whilst I find this argument initially attractive, as requiring HMRC to show that an (invalid) follower notice was issued is arguably no burden at all, I note that s208 is similar to s226 FA 2014 (which provides for penalties in the context of the APN regime) and the existence of the requirement in s226 that HMRC had issued an APN was not sufficient to persuade the Court of Appeal in *Beadles* that on an appeal against a penalty there was any ability at all (let alone one on which the burden was on HMRC) to challenge the validity of the APN said to have been issued.

36. I consider that I should not approach s208(1) on the basis that it requires that a valid follower notice was issued (such as would, in my opinion, require that to be a matter on which HMRC then bore the burden in the context of an appeal against a penalty). Instead, the grounds upon which a taxpayer can challenge a penalty are set out in s214 and it bears the burden of establishing that the grounds on which it relies are made out. The burden is thus on WS to establish that *UBS* is not a relevant judicial ruling (or that its alternative grounds are made out).

37. The standard of proof is the balance of probabilities.

EVIDENCE

38. I had an extensive hearing bundle and a bundle of authorities, as well as a copy of the advice which WS had received from Peter Trevett QC and various authorities which were handed up during the course of the hearing. In addition to providing me with skeleton arguments, HMRC provided detailed notes by way of a written closing, to which WS responded in writing after the hearing.

39. I heard evidence from three witnesses:

(1) Diane Heslop - Ms Heslop had prepared a witness statement dated 8 January 2021, and gave evidence on which she was cross-examined at the hearing. Ms Heslop has been a director of WS since 1999, was Finance Director at the time the STEP Arrangements were entered into and remains Finance Director. She also deals with operational aspects of the business. Her evidence is assessed below.

(2) Benjamin Roseff – Mr Roseff is a tax partner at PwC and had prepared a witness statement dated 8 January 2021. His evidence was that PwC had been appointed by WS in June 2019 to assist them in reaching a settlement with HMRC in respect of the STEP Arrangements (as well as the DOTAS Arrangements). Mr Roseff had previously worked at Deloitte and had attended a meeting with HMRC in September 2008 with others from Deloitte which had covered what were described as "Deloitte Manchester 03/04 STEP schemes and 04/05 STEED schemes". He was credible, but to the extent that his evidence comprised his opinion as to the level of cooperation provided by WS to HMRC I place no weight on such opinion.

(3) Mark Gebski – Mr Gebski had provided a witness statement dated 19 February 2021. He has been employed by HMRC since 2014, was an investigator in the Counter Avoidance Directorate from September 2015 to January 2021, moved to the Counter Avoidance Policy Development Team where he was a policy advisor and is now policy lead for that team. In 2017 he was appointed lead investigator in respect of certain taxpayers' use of the "Deloitte STEED ES16 – Short Term Equity Deferral Plan with Interest in Possession Trust", ie the DOTAS Arrangements which had been implemented by WS in 2004-05. He had been involved in assisting with preparation for the litigation in relation to the STEP Arrangements since 2018. His witness statement included a detailed summary of the chronology, including all of the correspondence with HMRC, as well as an explanation of why HMRC had concluded that the decision of the Supreme

Court in *UBS* was a relevant judicial ruling and the background to the issue of penalties for failure to take corrective action.

40. There was no evidence from either Rajan or Sanjay Kumar. HMRC drew attention to the fact that they were indirect shareholders and controlling directors of WS and stood to gain most from the implementation of the STEP Arrangements (receiving almost £8 million of bonuses in 2003-04). They had attended many of the meetings with Deloitte and tax counsel and had attended meetings with HMRC. Ms Lemos submitted that I should draw adverse inferences from the absence of evidence from Rajan and Sanjay, including that they would not have been able to give evidence to support the commerciality of the STEP Arrangements generally or the operation of the Performance Condition in particular.

41. Ms Heslop explained that that she was giving evidence on behalf of WS as she is the Finance Director, had been involved in establishing the STEP Arrangements, had the correspondence with HMRC, and she deals with all corporate issues and litigation for the group. The implication was that she could speak to all relevant matters and it was not necessary to hear from Rajan or Sanjay.

42. I consider the evidence of Ms Heslop, and the absence of evidence from Rajan and Sanjay, together:

(1) Ms Heslop was well-placed to explain the decision to implement the Step Arrangements. She had attended the key meetings, and was directly involved in setting the Performance Condition.

(2) Her evidence was not entirely satisfactory. There were areas where she could not explain what had happened. In part, this can be understood by the passage of time - the STEP Arrangements were implemented at the end of 2003, some 18 years before the hearing. This was less understandable in the context of questions about the action which had been taken by WS following receipt of the FN (and APNs) – the FN was issued on 17 February 2017, and the penalties on 13 March 2018, yet there was little documentary evidence about what had happened in this window and the vagueness of Ms Heslop's answers as to what they had done and what they had understood was noticeable and leaves a gap in the evidence.

(3) Ms Heslop denied that the STEP Arrangements constituted tax avoidance and insisted that the outcome of the Performance Condition was not known. I read nothing into the former position – Ms Heslop explained that she considered tax avoidance meant a failure to pay tax that was due (an explanation more akin with tax evasion). In that light, her position is entirely logical. I have more difficulty accepting her evidence in relation to the incentivisation purpose of the STEP Arrangements generally and the setting of the Performance Condition – Ms Heslop could not explain how the STEP Arrangements could or did incentivise Rajan and Sanjay in particular given that they were also shareholders in the business (and having regard to time-frames, responsibilities and any action taken that was different (eg as regards suppliers and customers) as a result of having this incentivisation in place).

(4) I was left with a rather mixed view of Ms Heslop's evidence. I approach it with some caution.

(5) Rajan and Sanjay would have been able to provide evidence on many of the facts which are in issue between the parties (in particular as to whether there was a commercial purpose to the Performance Condition and the advice taken subsequent to the issue of the FN). It would have been helpful to have that evidence. That is particularly the case given the gaps in the explanations provided by Ms Heslop (although I recognise that the

existence of such gaps may not necessarily have been known when preparing this appeal). The explanation that was provided by Ms Heslop for the absence of evidence from either Rajan and Sanjay (ie that this matter is within her remit and she had attended the meetings) is plausible, but in a family business, where the family members are controlling directors and involved in the operation of the business, I would have expected to hear from at least one of them. Nevertheless, I do not draw specific adverse inferences from the absence of evidence from them – the range of matters covered by Ms Lemos' cross-examination was broadly within Ms Heslop's remit, and I am not persuaded that, for matters where there were gaps, that Rajan and/or Sanjay would have assisted in those areas. This does not mean that the decision not to call them is without consequence for WS, as the result is that in areas where WS bears the burden of proof and where the facts are disputed, there is less evidence before me on which to make my findings and satisfy that burden.

43. I have taken account of all of the submissions received, both oral and written, but have not found it necessary to refer to all of them in setting out my findings of fact and reasons for my decision.

ADDITIONAL FINDINGS OF FACT

44. I have already described the STEP Arrangements and the process which followed in relation to the enquiry, the issue of the FN, the issuance of the FN penalties and the subsequent settlement of the underlying tax liabilities. I consider here areas that were disputed between the parties, including the decision to implement the STEP Arrangements, the approach to setting the Performance Condition and action taken following the issue of the FN. Further findings of fact are made in the Discussion.

Decision to implement the STEP Arrangements

45. The rationale for the implementation of the STEP Arrangements is relevant to the consideration of whether *UBS* was a "relevant judicial ruling", as Lord Reed had concluded in UBS at [85] that the reference in s423(1) to "any contract, agreement, arrangement or condition which makes provision to which any of subsections (2) to (4) applies" is to be construed as being limited to provisions "having a business or commercial purpose, and not to commercially irrelevant conditions whose only purpose is the obtaining of the exemption". Whilst this needs to be considered specifically in relation to the Performance Condition, such condition should not be viewed in isolation, but needs to be considered in the context of the decision to implement the STEP Arrangements.

46. Ms Heslop's explanation for the decision to introduce the STEP Arrangements was that it was an incentivisation scheme, which was introduced in the light of concerns about trading conditions, and was designed to incentivise management to drive the business through challenging times:

> (1) In early 2002 the directors recognised that they potentially had difficult times ahead, and had concerns about future trading conditions, including:
>
> > (a) In 2001, a World Trade Organisation ("WTO") agreement on textile and clothing eliminated the use of quotas in all textile and clothing trade between WTO nations. This agreement was considered to be a real threat to the company's market sector.
> >
> > (b) The retail environment had changed. Supermarkets had started to invest in their clothing offering, and this was a big threat to clothing discounters on the high street.

(2) They asked Deloitte to assist in developing a plan to incentivise management. Deloitte first presented various options in February 2003. One of those options was the STEP Arrangements.

(3) WS met with Peter Trevett QC in August 2003. He advised that the STEP structure proposed was "his preferred structure" as it was tax efficient and "more robust". Counsel advised that "the most critical element would be the inclusion of performance criteria that result in a genuine risk of forfeiture". Relying on both sets of advice, WS decided that the STEP Arrangements would be the most suitable for its needs.

(4) When discussing levels of turnover with Deloitte in September and October 2003 for the purpose of setting the Performance Condition, WS were also concerned about the long summer (which meant that orders for winter ranges had not been forthcoming) and China's manufacturing had been affected by the SARS outbreak and extreme weather, which in turn had a knock-on effect on incoming goods and orders being delayed or cancelled.

(5) The board of WS expected the company's trade to be adversely affected and predicted that there would be a reduction in sales of around 25%; the challenge was to ensure they did not drop below this, as that would result in a reduction of workforce and infrastructure.

47. Ms Heslop denied that the STEP Arrangements were a tax avoidance arrangement, and said she considered them to be low-risk. Her explanation for them not being "tax avoidance" was that she couldn't recall anyone having described them in this way and she understood "tax avoidance" to mean that there is tax to pay and you are avoiding paying it.

48. HMRC challenged this evidence, submitting that the STEP Arrangements did not have any incentivisation role, and the Performance Condition was a device designed to make the tax saving work and did not support any commercial or business purpose. HMRC's position was that the STEP Arrangements involved a series of pre-ordained steps which WS knew would happen, including the satisfaction of the Performance Condition. They relied on the financial statements, Deloitte's engagement letter (dated 20 August 2013) which refers to advice "in respect of appropriate methods of extracting funds from the company and incentivising senior individuals" and the fact that £8 million was transferred to Chatam in October 2003 before the Performance Condition had even been finalised. HMRC's position was that the turnover condition had been suggested by counsel, there was no evidence as to how the Performance Condition (applying across a three-month period) was thought to address the long-term concerns apparently identified by WS, or how the existence of the arrangements might change behaviour and motivate employees. Instead, the purpose of the STEP Arrangements was to deliver (mainly to Rajan and Sanjay) in a tax-free form the amount which would otherwise have been paid to them as a dividend.

Financial performance

49. The only written records of the actual financial performance of WS are the financial statements of that company and a turnover comparison sheet, showing monthly turnover in each of the accounting periods ended March 2002 to March 2009 (the "Turnover Comparison").

50. The auditors of WS prepared the financial statements on the basis of information provided by Ms Heslop, and the directors would then agree and approve them. The accounts of WS recorded:

(1) Year ended 31 March 2002, signed off on 31 January 2003 – The "Review of Business" stated that "The directors are satisfied with the results for the year, and are

optimistic that the level of activity and profitability will be maintained in the current year." Total dividends for the year were £8 million. Turnover had been £70,979,075 (up on £69,662,163 the previous year), with a profit before tax of £6,327,654. After tax and the payment of the dividends there was then a loss of £3,617,278. The balance sheet recorded that there was cash at the bank and in hand of £6,254,910.

(2) Year ended 31 March 2003, signed off on 24 October 2003 – The "Review of Business" still refers to the directors being satisfied with the results and optimistic. Turnover increased to £71,663,449 and profit before tax was £11,793,249, with after tax profits being £8,202,874. No dividend was declared.

(3) Year ended 31 March 2004 – The "Review of Business" continues to refer to satisfaction with the results and optimism for the current year. No dividends were declared. Turnover was £69,054,416, profit before tax was £589,175. This drop in profits can be seen to arise largely from an increase in staff costs for the year, which were £10,615,151 (up from £1,964,797 the previous year).

51. The note of conference with Mr Trevett (which took place in August 2003) does not record any concerns having been expressed by WS about trading conditions. The STEP Arrangements were framed as an incentivisation scheme, but the focus in that note is about extracting funds from WS. The note records:

(1) Counsel advised that the "most critical" element would be the inclusion of performance criteria that result in a genuine risk of forfeiture.

(2) An example was given as to where the net assets of the group are less than £1 million at a specified date. No examples had been put to counsel about basing this on turnover.

(3) The advice was prefaced on the fact that at the end of the period the shares could be forfeit (and the arrangements relied on the new exemption in s429).

(4) Addressing the risk of a *Ramsay*/*Furniss* approach, such that the cash paid for the sale/redemption of the redeemable shares may be construed as a bonus payment, counsel advised that this could be minimised by the way in which the newco invested the subscription monies (in investments with fluctuating values) and a gap of at least three months, preferably six months, between the award of the redeemable shares and their sale/redemption.

52. The note also considers a second possible structure which had been put forward by Deloitte, a dividend planning arrangement. That was not implemented, but in the context of considering the steps involved counsel referred to the need to attach conditions so that they fall within the definition of "restricted securities" and gave examples including employee conditions and asset value, and noting that a profit or turnover based condition would be stronger.

Setting of the Performance Condition

53. Ms Heslop's evidence was that:

(1) The business of WS was driven by key staff who focused on sales, stock and cashflow. These were the three key performance indicators for their staff.

(2) The company's financial systems in 2003 were unsophisticated in comparison to those used at present. The only management information in existence was bank balances and daily sales records summarised at the end of each month via the daybook. They did not undertake sophisticated forecasting or cash management - they monitored the cash coming in.

(3) As sales turnover was the main focus of the business at the time and it was easily analysed via the daybook, it was decided that turnover would be the most appropriate threshold for the forfeiture condition.

54. The Performance Condition was ultimately set with a turnover target for WS of £12 million for the three-month period from 1 November 2003 to 31 January 2004. The condition is included in the share rights of the Redeemable Shares of Chatam.

55. There had been various email exchanges between Ms Heslop and Deloitte about setting the Performance Condition, and Mr Tillotson of Deloitte set out clearly in September 2003 that the most robust conditions are those that cannot already be determined. Ms Heslop was well aware that it should not be set by reference to a past event.

56. The initial discussions as to the setting of the turnover target included:

(1) On 1 October 2003, Ms Heslop was envisaging that the turnover target would be the turnover of WS, the trading company, for a three-month period, October to December 2003, with the target set at £20,235,582, this being a 10% reduction on the turnover for that period the previous year.

(2) An email exchange almost two weeks later (on 13 October 2003), referring to discussions the previous week, shows that it was envisaged that the turnover target would be £18 million for that period.

(3) By 20 October 2003 they were not looking to adjust the period or the target, but contemplated that it would be met by reference to the turnover of "Rajan Group plc and its subsidiaries".

57. Chatam was incorporated on 22 October 2003 and the share rights of the Redeemable Shares reflected this position, ie the target was that the turnover of what is now WSGP and its subsidiaries as recorded in the consolidated management accounts for the three-month period ending on 31 December 2003 was £18 million.

58. However, discussions as to the Performance Condition continued:

(1) On 3 November 2003, Ms Heslop suggested adding a further £4 million to the target to cover the period from 1 October 2003 to 31 January 2004, ie £22 million for the four-,month period.

(2) On 6 November 2003 Ms Heslop emailed to say that the forfeiture figure should be £12 million for the period from 1 November 2003 to 31 January 2004. Giving evidence Ms Heslop explained that they had removed October from the period because of the timing of implementation – the sales in October had taken place. There was no reference in these emails to whether this should be measured by reference to the group's turnover or just that of WS.

(3) Deloitte emailed the documentation to amend the articles of Chatam on 10 November 2003. The amendment was to amend the Performance Condition to the final version, ie turnover of WS alone and was set at £12 million for the three-month period from 1 November 2003 to 31 January 2004. Ms Heslop explained that the move from group turnover to WS only was that the group included companies receiving income from rents and other companies over which Rajan did not have control.

59. The relevant meetings of Chatam approving the amendments took place on 11 November 2003, and the special resolution was registered on 20 November 2003.

60. On 20 November 2003, there was a board meeting of the directors of WSGP, attended by Rajan, Sanjay and their father. They decided to award shares to Rajan and Sanjay, as well as to EBT1.

61. There was then a board meeting of WS on 15 December 2003 at which the directors resolved to award the Redeemable Shares to "key employees". The shares were awarded on 17 December 2003.

Information available to WS

62. Ms Heslop emphasised the lack of management information available to WS at the time when explaining why it was not certain that the Performance Condition would be met. She explained that they had up-to-date information about cash held and what she referred to as the sales daybook. They raised invoices when goods left the warehouse, and ran daily/monthly reports for sales. On any specified date they could run a report for sales so far that month.

63. However, I find that there was also additional information available, in the form of records as to turnover in prior years and the forward order book, which would have helped WS, when setting the Performance Condition and awarding the Redeemable Shares, to assess the likelihood of its being met.

Forward order book

64. WS's position was that the forward order book is not a reliable indicator of how sales would materialise. Forward orders were usually received months in advance of any given season as customers wanted to secure new stock due to arrive into the warehouses. WS would often take more orders than they could fulfil in order to make provision for non-payment of credit accounts, and last-minute postponement or cancellation of orders. They regard forward orders as merely speculative, and they do not reflect actual achieved sales.

65. Ms Heslop explained that reasons they may not proceed may be as a result of the customer not passing credit checks and stock not being available. It is not known when the requested stock will be delivered, even if the order is confirmed. Furthermore, Ms Heslop explained that the forward order book was not easy to interrogate – it required substantial work to put together, and couldn't be used to run a report for a different day or used to compare the position to a date the prior year.

66. I was not provided with an extract or illustration from the forward order book. Moreover, there was no evidence as to the extent to which forward orders do or do not turn into actual sales, other than Ms Heslop's evidence that forward orders may not materialise. The absence of evidence as to even a rough estimate of the percentage of forward orders which crystallise into sales was significant.

67. I accept that forward orders placed are not certain to proceed. However, it is notable that some of the uncertainties inherent in forward orders (as described by Ms Heslop) relate to timing (eg when the customer confirms they want the stock, or when stock is available) rather than whether the order will proceed at all.

Historical turnover information

68. The Turnover Comparison could not have been available in this form to WS at the time at which they were setting the Performance Condition (as it includes information relating to future periods). However, I do find that Ms Heslop, as Finance Director and the person providing information to their accountants, would have had access to this form of historic turnover information per month (both for prior years and preceding months) – she referred to this data in her emails with Deloitte in October 2003.

69. The Performance Condition was set by reference to November, December and January in the accounting period ended March 2004. The monthly figures actually achieved were £6,109,218, £4,774,578 and £4,722,895.

70. Looking at the turnover of WS in the years ended March 2002, March 2003 and March 2004:

(1) It is apparent that there is a significant variation between calendar months. September and October seem to be the strongest months.

(2) Ms Heslop had referred to concerns about ensuring turnover did not drop more than 25%. September to November 2002 had a total turnover of approximately £27.39 million; the same three months the following year had a total of £25.57 million; there was a drop, but not of the magnitude of 25% (albeit that Ms Heslop then clarified that this 25% drop had referenced a drop for the calendar year 2004, not the accounting period ending March 2004).

(3) When, on 3 November 2003, Ms Heslop had suggested making the performance period four months and adding January 2004 and increasing the target by £4 million, she explained that she had been looking at the previous year's turnover and seen that turnover in January 2003 had been £4,267,903.

(4) Turnover in the three months ended January 2002 was £17.8 million; turnover in the same period in subsequent years was £16.5 million to January 2003 and £15.6 to January 2004 (the three months covered by the Performance Condition).

71. Looking at the turnover in subsequent years:

(1) In the accounting periods ended March 2005 to March 2009 there was a decline, with total turnover at £59,025,176, £44,831,474, £42,520,338, £45,416,489 and £48,098,119. So turnover was at its lowest in the year ended March 2007 and has been recovering since.

(2) Turnover in the three-month period to end January dropped to £15.2 million for the period ended January 2005, £13.5 million for the period ended January 2006 then £10 million to January 2007.

Award during the three-month period

72. Whilst WS emphasised that the Performance Condition set a target for a three-month period, the practical reality is that:

(1) the target was only approved on 11 November 2003, and the special resolution registered on 20 November 2003, and

(2) a small number (100) of Redeemable Shares were issued to Rajan and Sanjay on 21 November 2003; but

(3) the vast majority (7,999,890) of the Redeemable Shares were awarded on 17 December 2003, more than half way through the period.

73. On 17 December 2003, WS would have known the actual turnover which had been achieved for November 2003 (£6,109,218, ie more than half the target amount), and actual turnover achieved for half of December. Turnover for all of November and December 2003 was £10,883,796, but there was no evidence as to how much of this was achieved after 17 December.

Satisfaction of the Performance Condition

74. The target of £12 million turnover was met at 31 January 2004. This was accepted by HMRC, but they did draw attention to the lack of any documentation from WS (eg board minutes, or internal emails) confirming this.

75. Whilst Ms Heslop's evidence was that it was hoped that the target would incentivise five key employees (including the founding directors) to change the business strategy including finding new customers to replace those who were winding up or starting to underperform, place emphasis on the quality of items making the Company less reliable on retail discounters and source new factories outside of China:

(1) The trading concerns identified by Ms Heslop were potentially of long-term impact. The only evidence as to these trading difficulties was provided by Ms Heslop, and they were referenced in her email exchanges with Deloitte in October 2003. However, Ms Heslop was not able to give a satisfactory explanation of how the Performance Condition, which provided a turnover target for a three-month period, was intended to address these concerns.

(2) There was no evidence of any change in strategy between the decision to award the shares in December 2003 (or even the original amendment of the share rights in November 2003) and the end of January 2004 to address the issues of concern.

(3) There was no evidence of how the company had monitored whether the incentivisation had worked – Ms Heslop's explanation of the success of the condition was essentially by reference to the fact that the target had been met and therefore it had worked.

(4) Given that most of the Redeemable Shares were awarded to Rajan and Sanjay, who were also indirect shareholders, there was no evidence as to why the STEP Arrangements offered a better incentivisation for them than the retention of profits and payment of dividends.

(5) Furthermore, the STEP Arrangements had an inbuilt hedge if the condition had not been met. The shares would be forfeit to EBT2, and the Trustees had been told (by WS) that if the shares were transferred to the EBT then WSGP wished that these shares should be applied for the benefit of the employees of WSGP in the future.

Conclusions

76. On the basis of the evidence:

(1) There are no concerns about financial performance in the accounts for the accounting periods ended March 2002 and March 2003 (the latter having been signed by the directors in October 2003). No dividend was paid out of the profits in the period ended March 2003, and Ms Heslop accepted that the information received from Deloitte in February 2003 about incentivisation arrangements was relevant to decisions the directors had taken; this would have included the decision not to pay a dividend.

(2) Whilst the options presented by Deloitte were in the form of incentivisation arrangements, there was no reference therein to concerns about trading performance, or the need to introduce triggers to incentivise employees. The first reference to the introduction of a performance condition based on turnover was the suggestion by Mr Trevett in August 2003.

(3) I accept Ms Heslop's evidence as to the existence of the difficult trading conditions in the sector, namely as to the WTO, difficulties with supplies from China and the problem of competition for high street retailers. However, the recognition of such issues

in the market does not require that I also accept that WS identified at that time the possibility of these matters resulting in a 25% reduction in turnover, or that this was the point at which they would need to reduce workforce or infrastructure. There was no evidence as to detailed forecasts or modelling, no analysis of supply chains or customer profiles. There was nothing to support the very high-level explanations provided by Ms Heslop, in an area where I would have expected the Finance Director to have conducted detailed analysis.

(4) There was no credible evidence as to how the existence of a target for a three-month period could address the long-term concerns which had been identified, the impact this had on behaviour, or how WS sought to monitor any changes (eg new suppliers or customers).

(5) In setting the Performance Condition, Ms Heslop was aware that there needed to be seen to be a risk of forfeiture, and that a condition which related to past events would not satisfy this. When considering various options, the pattern was of the target amount being reduced. This can be explained in part by the fact that October, which was historically one of the strongest contributors to turnover, was removed from the period.

(6) WS had a range of information available to it when setting the Performance Condition – turnover information for previous years, the forward order book and a very up-to-date picture of current trading from the daybook.

(7) Whilst some shares were awarded on 21 November 2003, most were awarded on 17 December 2003, more than half way through the target period. At this time, WS would have known the turnover achieved in November 2003 and, on the basis of the daybook, would have known the turnover for the first half of December 2003. By the end of December, only an additional £1,116,204 of turnover needed to be achieved in January 2004 to meet the target.

(8) None of these sources of information were perfect; but when the majority of the shares were awarded on 17 December 2003, WS could be reasonably certain that the Performance Condition would be met.

Engagement with HMRC

77. HMRC had opened an enquiry into the STEP Arrangements on 10 November 2006. WS instructed Deloitte to respond to HMRC's letters and requests for information.

78. By the end of 2008 WS and Deloitte had provided to HMRC the majority of the information which had been requested by HMRC. It is clear from the correspondence that there were still some requests outstanding at that time, notably bank statements of the trusts:

(1) On 29 June 2007 Deloitte had sent various information to HMRC, stating they considered it was everything that HMRC were seeking but that they had not provided documents which constituted tax advice or were protected by privilege. That letter stated that they were in discussions with the trustees in relation to the availability of bank statements for the transactions entered into, but had supplied those which they did hold.

(2) HMRC replied, and asked for further information as to the identification of documents said to be covered by privilege.

(3) By the time of a meeting between Deloitte and HMRC in September 2008 (covering various taxpayers), the bank statements had still not been provided.

79. Between 20 July 2009 and 14 February 2017, HMRC sent "litigation updates" regarding the litigation of the UBS and DB appeals, eg:

(1) The Litigation Update of 20 July 2009 said that HMRC was progressing what it described as "s429 ITEPA 2003 avoidance schemes" to litigation in line with its Litigation and Settlement Strategy, and referred to a recent decision of the FTT.

(2) The FTT decision in *UBS AG v HMRC* [2010] UKFTT was handed down on 6 August 2010, and a further litigation update was issued on 7 October 2010.

(3) The FTT decision in *Deutsche Bank Group Services (UK) Ltd v HMRC* [2011] UKFTT 66 was handed down on 19 January 2011 and HMRC sent an update on 17 February 2011.

80. After the Supreme Court decision in *UBS* was handed down on 9 March 2016 (by which time the appeals of UBS and DB had been joined), Phil Hardy of HMRC wrote to WS (on 21 April 2016) stating that the Supreme Court had found for HMRC in both appeals, and attached a link to the judgement. In that letter:

(1) HMRC set out its position that it considered the judgement applied to the facts of the scheme as implemented by WS, and that the company now had to decide whether it accepted that the judgement applies to the scheme. If it did, it should withdraw its appeals against the PAYE and NICs determination and decision; if it did not think it applies, WS should write setting out the basis on which it considers it is distinguished.

(2) HMRC was seeking authorisation to issue a follower notice to WS.

(3) There is then a link to HMRC publications on APNs and follower notices, and Mr Hardy recommended WS read them. He drew attention to the potential penalty.

(4) He asked for a response within 30 days concerning the company's intentions with regard to the open appeals.

81. The FN was issued on 17 February 2017. The FN penalties were issued on 13 March 2018. In that intervening period:

(1) WS sent representations to HMRC in response to the FN on 12 May 2017.

(2) WS sent a letter before claim for JR to HMRC on 15 September 2017 and then issued a claim for JR on 3 November 2017.

(3) WS wrote to HMRC on 9 February 2018, responding to Mr Gebski's letter of 10 November 2017 requesting further information. That letter says it provides background (to the STEP Arrangements), the Turnover Comparison, stock transfer forms, and Elsworth bank statements. The bank statements were not attached to the copy of this letter in the hearing bundle (or at least not in a way in which it was apparent that they had been enclosed with this letter), but I infer that they were the ones that HMRC had been requesting back in 2007 and 2008.

Advice taken subsequent

82. Ms Heslop and the other directors (including Rajan and Sanjay) were not tax experts and relied on their advisers.

83. Chronologically, the overall picture of advisers is as follows:

(1) They were advised by Deloitte (where their main contacts were Brian White and John Tillotson) and Peter Trevett QC prior to implementation of the STEP Arrangements. WS had attended a conference with Mr Trevett in August 2003.

(2) HMRC opened enquiries in November 2006 but they did not obtain further advice on the merits at that time, or when they were instructing Deloitte to respond to HMRC's requests for information.

(3) HMRC's litigation updates from 2011 onwards referred to the appeals of UBS and DB. WS were being advised by Deloitte and Mr White (who had left Deloitte by this time). Ms Heslop's evidence was that WS were regularly asking questions, and were being told to continue to wait for the outcome but also that their forfeiture provisions were different to those of UBS and DB. They had been aware that HMRC had been successful at earlier stages of these appeals, and this had shaken their confidence, but WS had not considered obtaining a second opinion on the merits. There was no documentary evidence of meetings being arranged (with Deloitte or Mr White), written advice on the merits being given to them or discussions within WS (eg at board meetings) of the risks involved.

(4) After the Supreme Court decision in *UBS* was handed down, they obtained advice from Mr White and Michael Firth (counsel). Mr Firth had been instructed before then, as he had drafted representations responding to a follower notice received by WS in relation to the DOTAS Arrangements.

(5) WS instructed PwC in June 2019 for the purpose of agreeing the settlement with HMRC.

84. There was minimal documentary evidence of the actions taken by WS or advice obtained by WS following the release of the Supreme Court's decision in *UBS*. Ms Heslop's evidence was:

(1) They had been told of the Supreme Court decision by Mr White, before they received HMRC's letter of 21 April 2016. Ms Heslop's evidence was that "until then we had felt there had been genuine uncertainty". Even after HMRC's win, they believed their planning could be differentiated – there was a real possibility that turnover could fall and the targets would not be met. She said this was based on discussions with Mr White and Mr Firth.

(2) Ms Heslop acknowledged that HMRC were clearly stating in Mr Hardy's letter of 21 April 2016 that HMRC considered the decision in *UBS* applied to the STEP Arrangements. She couldn't recall if she had followed the link to the guidance on follower notices.

(3) Every time WS received a letter from HMRC in relation to the STEP Arrangements they forwarded that letter to Mr White or Mr Firth.

85. I accept that this evidence is a fair summary of the actions taken by WS at that time.

86. The FN was then issued on 17 February 2017. Ms Heslop's evidence was that they were concerned about the potential for penalties, sought advice from Mr Firth, who advised that they had strong arguments to support a review and that they should challenge HMRC's position. They were advised that a judicial review challenge was appropriate action to take and that such action was a valid reason not to concede their position to HMRC in response to the FN. The only documentary evidence in relation to this is the fact of the sending of the representations and the letter before claim, and subsequent claim for JR, and an email exchange from October 2003:

(1) The representations sent by WS to HMRC in response to the FN on 12 May 2017 - those representations had been drafted by their advisers and set out WS' position that there was no relevant judicial ruling (and thus no valid follower notice), referring to the guidance published by HMRC and what they described as the general principle established by *UBS*. They state that if HMRC maintain the FN and APNs then they will be seeking judicial review of that decision.

(2) WS issued a letter before claim for JR to HMRC on 15 September 2017 - that letter attached draft grounds for review (which were not in the bundle), but Ms Heslop accepted that they were in the same form as the grounds later issued (in November 2017). Those grounds were themselves very similar to the substance of the representations which had been made in May.

87. I accept that the representations sent in response to the FN and the grounds for review which were issued with WS's JR claim were drafted by WS' advisers, and from this (and Ms Heslop's evidence) infer that WS were taking advice in response to the issue of the FN. A difficulty, considered in the Discussion in the context of whether it was reasonable in all the circumstances not to comply with the FN, is as to the basis on which that advice was given (ie what information had been given by WS to Mr White and Mr Firth about the business, the setting of the Performance Condition and the likelihood of target being met) and as to the strength of the advice received.

88. HMRC had responded to WS's letter before claim for JR on 3 October 2017. That letter was forwarded by Ms Heslop to Mr Firth at 16.46 that day. He responded at 16.51, saying this is "as expected" and recommends that they begin judicial review shortly, asking if WS want a conference to discuss what this means and the potential consequences for the company. It goes on to say "I think we have reasonable arguments to support the claim for judicial review, but of course there is no guarantee of success and judicial reviews are always difficult."

89. Ms Heslop's evidence was that they did have a conference with Mr Firth, and I accept that evidence. WS then issued their claim for JR on 3 November 2017. The JR claim was stayed by agreement between the parties.

Settlement relating to STEP Arrangements

90. Mr Gebski's evidence (which was unchallenged and I therefore accept it) was that he was first approached about the possibility of WS reaching a settlement with HMRC by Mr White in September 2018. That approach comprised a phone call asking for settlement calculations for both the STEP Arrangements and the DOTAS Arrangements. There were then various without prejudice discussions until April 2019. There was a meeting between Mr White and HMRC in May 2019, but that did not result in a settlement

91. WS then appointed PwC in June 2019 to assist them in reaching a settlement agreement.

92. A meeting was held between HMRC and representatives from PwC on 28 August 2019. HMRC confirmed that Rajan and Sanjay would be able to use mixed funds held offshore to make good the PAYE tax without triggering a remittance. The settlement was agreed in September 2019.

DISCUSSION

93. HMRC issued the FN on 17 February 2017. The notice specified that corrective action was required to be taken by 23 May 2017, although that was subsequently extended to 28 September 2017 and then 30 October 2017. It was common ground that WS did not take corrective action by that date.

94. There are no appeal rights against a FN itself, but s214 FA 2014 sets out the right to appeal against a decision of HMRC that a penalty is payable or as to the amount of the penalty. The grounds on which an appeal may be made include that the judicial ruling specified in the notice is not one which is relevant to the chosen arrangements (s214(3)(b)) or that it was reasonable in all the circumstances for the person not to have taken the necessary corrective action in respect of the denied advantage (s214(3)(d)). Those are the grounds relied upon by WS against HMRC's decision that a penalty was payable by WS. WS also appealed against

the amount of the penalty which had been assessed, on the ground that the maximum reduction allowed for co-operation should have been given.

Whether a relevant judicial ruling

95. Section 204 defines the circumstances in which a follower notice may be given, including Condition C in s204(4) FA 2014 which is that "HMRC is of the opinion that there is a judicial ruling which is relevant to the chosen arrangements". Section 205 then defines "judicial ruling" and sets out the circumstances in which a judicial ruling is "relevant" for the purposes of the follower notice regime. WS accepted that the decision relied upon by HMRC, *UBS*, is a "judicial ruling", and that it relates to tax arrangements and is a final ruling. However, they submitted it was not "relevant" to the STEP Arrangements as s205(3)(b) was not satisfied – that sub-section requires that "the principles laid down, or reasoning given, in the ruling would, if applied to the chosen arrangements, deny the asserted advantage or a part of that advantage".

96. I have the benefit of two decisions of the Supreme Court. The decision in *UBS* is that which is relied upon by HMRC as being a "relevant judicial ruling", and the decision in *R (oao Haworth) v HMRC* [2021] UKSC 25 considers the threshold required by s205(3)(b). I consider the decision in *Haworth* first, before then considering the decision in *UBS* and whether the principles laid down or reasoning given therein would, if applied to the STEP Arrangements, deny the asserted advantage.

Haworth – threshold required for issue of follower notice

97. In *Haworth*, Lady Rose (giving the judgement of the Supreme Court) accepted that the purpose of the follower notice regime is to deter further litigation on points already decided by a court or tribunal and to reduce the administrative and judicial resources needed to deal with such unmeritorious claims (at [58]). In determining where the line falls between circumstances which are intended to be caught and those which are not, it is relevant to take into account the severe consequences for the taxpayer of the giving of a notice (at [59]). Lady Rose set out the threshold for a judicial ruling to be relevant at [61] as "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. Only then can they be said to have formed the opinion that the relevant ruling "would" deny the advantage. An opinion merely that is likely to do so is not sufficient." The Tribunal must apply that same "high threshold of certainty" when determining an appeal.

98. Guidance was then provided as to how to apply this threshold:

> "64. Whether HMRC can reasonably form the opinion that an earlier ruling is relevant to the taxpayer's asserted advantage will depend on a number of factors. First, it may depend on how fact sensitive the application of the relevant ruling is; in other words, whether a small difference in the fact pattern of the taxpayer's arrangements or circumstances as compared with the fact pattern described in the earlier ruling would prevent the principles or reasoning applying. A follower notice may be issued at different stages of the investigation into the taxpayer's affairs. According to Condition A in section 204(2), it may be given as soon as a tax enquiry has been opened into the tax return made by P or it may be given during the course of a tax appeal. If the application of the earlier ruling is very fact dependent, then it may be more difficult for HMRC to form the opinion that the relevant ruling would deny the advantage where HMRC is considering Condition C at the earlier stage. If the follower notice is being considered when the tax appeal is already underway it may be clearer whether the fact patterns are sufficiently similar.
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> 65. Secondly, the relevance of the earlier ruling may turn on HMRC's rejection of the taxpayer's evidence as being untruthful. HMRC will have to consider carefully whether it is satisfied that the untruthfulness of those factual

> assertions is so clear that it can reasonably form the opinion that the earlier ruling is relevant, despite that contrary evidence.
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> 66. Other cases may be less fact sensitive, for example where the taxpayer has entered into the same mass marketed tax avoidance scheme as the taxpayer in the earlier ruling so that the provisions applicable in his case are identical to those held to be ineffective by the earlier ruling. If it is clear that there is no material difference between the chosen arrangements and the arrangements considered in the earlier ruling, it will be easier in such a case for HMRC to form the opinion that Condition C is satisfied.
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> 67 Thirdly, HMRC will need to consider the legal arguments put forward by the taxpayer. The taxpayer may rely on an argument that was not raised in the earlier ruling. This is what happened in *R (Locke) v Revenue and Customs Comrs* [2019] EWCA Civ 1909; [2020] 1 All ER 459; [2019] STC 2543. In that case, the taxpayer Mr Locke relied on a different statutory provision as entitling him to the tax advantage he asserted as compared to the statutory provision that had been considered and rejected in the earlier case on which HMRC sought to rely as the relevant ruling. The novel argument he made had not been put forward by the other taxpayers who had entered into the same arrangements as Mr Locke. It had not therefore been determined by the earlier ruling so that earlier ruling did not satisfy Condition C. A similar situation might arise where the earlier ruling was based on a concession by a party to those proceedings as to some aspect of the legal framework, but the taxpayer whose asserted tax advantage is being considered has made clear that he does not make that same concession and wishes to argue the point.
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> 68. Fourthly, HMRC should also consider the nature of the earlier ruling. As Mr Stone pointed out, a ruling by the FTT can be a relevant ruling for the purposes of Condition C even though it has no precedential value. However, a ruling arrived at after a hearing where, for example, the taxpayer did not appear or was not legally represented or where the reasoning in the decision is brief or unclear is less likely to be capable of forming the basis for the necessary opinion required in Condition C."

99. WS emphasised that the Tribunal needs to decide that the decision in *UBS* would deny the advantage, and submitted that whilst that decision is of the Supreme Court the other matters identified in *Haworth* indicated that HMRC (and, on appeal, the Tribunal) cannot form the opinion that *UBS* is relevant – the decision in *UBS* is fact sensitive, and HMRC are relying on their challenge to the evidence of Ms Heslop, whereas in *UBS* it had been conceded by the taxpayer that the condition attached to the shares had no business or commercial purpose.

Decision in UBS

100. Lord Reed's judgement in *UBS* starts by recognising that the appeals in that case concerned composite transactions designed to avoid the payment of income tax on bankers' bonuses, and were among a number of cases concerning broadly similar schemes (at [2]). The decision then proceeds:

(1) Lord Reed set out an overview of Chapter 2 of Part 7 ITEPA 2003, including the operation of s426 and the exemption provided by s429 where a class of shares is subject to a restriction:

> "[19] Section 426 imposes a tax charge in relation to the securities if a chargeable event occurs. For present purposes, the relevant chargeable event is the securities ceasing to be restricted securities. Section 429, however, allows an exemption from the charge under s 426 where, put shortly, a whole class of shares in a company is affected by the same restriction, all the shares

of the class are affected in the same way by the chargeable event, and either (a) the company is employee-controlled by virtue of holdings of shares of the class, or (b) the majority of the company's shares of the class are held by persons unrelated to the company. It follows that where s 429 applies (as, for example, where the company is owned by its employees, or where most of the shares of the class awarded to the employees are held by members of the public, and the other requirements of the section are met), the recipient of the shares is given the same favourable income tax treatment as the recipient of shares under an approved share option scheme. Subsequent to the date of the schemes with which these appeals are concerned, s 429 was amended by para 6 of Sch 2 to the Finance (No 2) Act 2005 so as to exclude its application to tax avoidance schemes."

(2) Lord Reed then outlined the scheme:

"[24] Before considering in detail the facts of the individual appeals, it may be helpful to explain briefly how, in broad terms, schemes of the kind in issue were designed to work. The modus operandi can be summarised as follows. The bank decided to award discretionary bonuses to certain of its employees, but to pay the amount of the bonuses into a scheme designed to take advantage of the provisions of Ch 2, so that the employees would avoid liability to income tax. Rather than paying the bonuses directly to the employees, the bank instead used the amount of the bonuses to pay for redeemable shares in a special purpose offshore company set up solely for the purpose of the scheme. The shares were then awarded to the employees in place of the bonuses. Conditions were attached to the shares which were intended to enable them to benefit from the exemptions from income tax conferred by ss 425(2) and 429. Once the exemptions had accrued, the shares were redeemable by the employees for cash. Employees resident and domiciled in the United Kingdom, who were liable to capital gains tax, could however defer the redemption of their shares until they had held them for two years, by which time the rate of tax chargeable, with the benefit of business taper relief, was only 10%.

[25] A typical scheme therefore involved carrying out the following pre-ordained steps:

(1) The bank decided which of its employees would receive discretionary bonuses, and the amount of those bonuses.

(2) Company Z was created in an offshore jurisdiction. Care was taken that Company Z was not an associated company of the bank for the purposes of s 429.

(3) A special class of redeemable shares in Company Z was created. As shares, these were 'securities' as defined in s 420(1)(a). The shares were subject to a short-term restriction designed to satisfy the requirements of s 423(2).

(4) The restriction involved a contingency which was unlikely to occur but might conceivably do so. In cases where the occurrence of the contingency lay beyond the control of those involved in the scheme, hedging arrangements were entered into so that the employees were compensated in the event of the restriction being activated.

(5) Directly or indirectly, the bank paid the aggregate amount of the bonuses to Company Z as the price of the shares.

(6) The purchaser received the shares and allocated beneficial interests to the employees identified at step (1) in amounts equal to the amounts that the bank had decided to award them as bonuses. Exemption from a charge to income

tax on the employees' acquisition of the shares was asserted under s 425(2), on the basis that the shares were restricted securities by virtue of s 423(2).

(7) A short time later, the restriction was removed from the shares. Exemption from a charge to tax on this event was asserted under s 429.

(8) A short time after that, the employees became entitled to redeem their shares, and many did so. No liability to income tax arose by reason of the redemption.

(9) Some employees who were resident and domiciled in the UK continued to hold their shares for the two years necessary to mitigate a charge to capital gains tax using taper relief. They then redeemed their shares.

(10) In due course Company Z was wound up."

(3) Having set out these outlines, Lord Reed went on to consider in greater detail the facts of each of the appeals.

(4) Describing the UBS scheme:

(a) Lord Reed said at [27] that UBS designed an employee bonus scheme to take advantage of Chapter 2. It had no purpose other than tax avoidance, and such consequential advantages as would flow from tax avoidance.

(b) The share rights provided for an immediate and automatic sale of the shares to the UBS employee benefit trust if on any date during the three-week period from 29 January to 19 February 2004 the closing value of the FTSE 100 Index exceeded a "trigger level", defined as 6.5% above its closing value on 28 January 2004. In that event, the shares were to be sold for a price equal to 90% of their market value on the date of the sale "if no restrictions (including for the avoidance of doubt under [article 2(14)]) applied to those shares".

(c) It was not likely that the FTSE 100 would exceed the trigger level during the relevant period, but there was a genuine possibility that it might: the trigger level was set so as to create a probability of between 6 and 12%. It was a matter of agreement that the forced sale provision had the effect of reducing the market value of the shares when they were acquired by the employees by an amount which was more than de minimis. The only purpose of the forced sale provision was to make the shares "restricted securities".

(d) There were call options that hedged the risk of the trigger event occurring, such that employees would not be materially worse off.

(5) The DB scheme was described at [49] and involved the group using an off-the-shelf scheme devised by Deloitte. That scheme was described as being "generically similar to the UBS scheme, but differed from it in some respects":

(a) The shares were to be forfeited if, before 2 April 2004, the person who held or was beneficially entitled to them ceased to be employed by DB, or notice was given to or by that individual of termination of employment, for any reason other than redundancy, death or disability, or without cause. The shares could not be transferred during that period.

(b) For practical purposes, therefore, an employee would forfeit his shares if he voluntarily resigned or was dismissed for misconduct during a period of about eight weeks. Neither contingency was likely to occur, not least because its occurrence lay largely within the control of the employee, for whom it would have significant financial consequences. Furthermore, by virtue of s424(b) ITEPA 2003, shares are

not restricted securities by reason only of a provision for forfeiture in the event of dismissal for misconduct.

(c) In the event, there was no employee to whom the provision applied.

(6) Having considered both schemes, and the approach taken by the FTT, Upper Tribunal and the Court of Appeal, Lord Reed then considered the *Ramsay* approach, noting at [61]:

> "As the House of Lords explained in *Barclays Mercantile Business Finance Ltd v Mawson*, in a single opinion of the Appellate Committee delivered by Lord Nicholls, the modern approach to statutory construction is to have regard to the purpose of a particular provision and interpret its language, so far as possible, in the way which best gives effect to that purpose."

(7) Lord Reed considered the arguments as to a purposive construction of ITEPA 2003 and reached this conclusion at [85]:

> "85. In summary, therefore, the reference in section 423(1) to "any contract, agreement, arrangement or condition which makes provision to which any of subsections (2) to (4) applies" is to be construed as being limited to provision having a business or commercial purpose, and not to commercially irrelevant conditions whose only purpose is the obtaining of the exemption."

(8) Lord Reed then went on to apply this principle to the facts:

> "86. In the UBS case, the condition — whether the FTSE 100 rose by a specified amount during a three week period — was completely arbitrary. It had no business or commercial rationale beyond tax avoidance. Such a condition is simply not relevant to the application of section 423, if, for the reasons already explained, that section is concerned with "provision" having a genuine business or commercial purpose. Applying section 423 to the facts, viewed from a commercially realistic perspective, it follows that the condition to which the UBS shares were subject should be disregarded, with the consequence that the shares are not "restricted securities" within the meaning of that section.
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> 87. That conclusion is fortified by another aspect of the facts of the UBS case. The economic effect of the restrictive condition was in any event nullified by the hedging arrangements, except to an insignificant and pre-determined extent (namely 0.8% at most — see para 32 above). The fact that what the First-tier Tribunal described as "a deliberate near miss" was designed into the scheme, rather than a complete offsetting of the risk, is immaterial. Paras 22 and 23 of the opinion in *Scottish Provident*, cited at para 70 above, are in point. As the Committee stated, the effect of the scheme should be considered as it was intended to operate. So considered, the benefit to the employee was not truly dependent on the contingency set out in the condition.
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> 88. The restrictive condition in the DB case was simpler but equally artificial. "Leaver" provisions in employee benefit arrangements often serve a genuine business or commercial purpose. But that cannot be said of the condition attached to the Dark Blue shares. The forfeiture provision operated for only a very short period, during which the possibility that it might be triggered lay largely within the control of the employee who would be adversely affected. It had no business or commercial purpose, and existed solely to bring the securities within the scope of section 423(2). Paras 22 and 23 of the opinion in Scottish Provident are again in point. DB deliberately included a contingency which created a minor risk, but one which the parties were willing to accept in the interests of the scheme. The scheme should therefore be

> considered as it was intended to operate, without regard to the possibility that it might not work as planned.
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> 89. The appeals thus belong to the line of cases mentioned in *Barclays Mercantile*, where it was decided that "elements which have been inserted into a transaction without any business or commercial purpose did not, as the case might be, prevent the composite transaction from falling within a charge to tax or bring it within an exemption from tax" (para 35). That was the approach adopted, for example, in *Inland Revenue Comrs v Burmah Oil Co Ltd* in relation to what Lord Diplock described as "a pre-ordained series of transactions … into which there are inserted steps that have no commercial purpose apart from the avoidance of a liability to tax which in the absence of those particular steps would have been payable" (p 124). Where a purposive construction so requires, one can proceed in such a case in the manner described by Lord Brightman in *Furniss v Dawson* at p 527:
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> "…the inserted steps are to be disregarded for fiscal purposes. The court must then look at the end result. Precisely how the end result will be taxed will depend on the terms of the taxing statute sought to be applied.""

(9) The Supreme Court thus decided in favour of HMRC in both appeals.

Consideration and conclusions

101. Whilst the STEP Arrangements do not involve bankers' bonuses, they are a broadly similar scheme to the arrangements in issue in *UBS*. The decision sets out "in broad terms" how the schemes were designed to work (at [24]) and describes the "typical scheme" at [25]. I consider that the steps described therein are very similar to the STEP Arrangements, albeit with the key issue being whether Lord Reed's description at [25(4)] is apt, with that being "The restriction involved a contingency which was unlikely to occur but might conceivably do so. In cases where the occurrence of the contingency lay beyond the control of those involved in the scheme, hedging arrangements were entered into so that the employees were compensated in the event of the restriction being activated."

102. Section 205(3)(b) requires that "the principles laid down, or reasoning given, in the ruling would, if applied to the chosen arrangements, deny the asserted advantage or a part of that advantage". It is clear from *Haworth* that this requires a high threshold of certainty – I must form the opinion that there is no scope for a reasonable person to disagree that the earlier ruling denies the taxpayer the advantage.

103. It is notable that, notwithstanding that Lord Reed was able to describe the schemes in broad terms, and set out his conclusion in a clear statement of principle at [85], it is clear throughout the decision in *UBS* that the Supreme Court applied the relevant principles to the facts of each of the appeals (saying at [26] it was "necessary" to consider in greater detail the facts), dealing separately with the appeals of UBS and DB and the different restrictions which attached to the shares.

104. It cannot be enough for me to conclude that the STEP Arrangements are broadly similar to those considered in *UBS*. The Supreme Court in *Haworth* provided guidance as to how to determine whether the earlier case would deny the advantage, ie that there is no scope for a reasonable person to disagree that the earlier ruling denies the taxpayer the claimed advantage.

105. The Supreme Court set out four factors which I have taken into account. I address the fourth factor first, namely the nature of the earlier ruling. *UBS* is a decision of the Supreme Court, clearly reasoned, which set out a clear statement of principle at [85] and applied that principle to the facts of two appeals which were described as generically similar but differed

in certain respects. I have no doubt that this decision is one which is readily capable of forming the basis for the necessary opinion.

106. There is, in the context of the present appeal, a degree of overlap between the first three factors. I need to consider how fact sensitive the application of the ruling is, against the background that HMRC does challenge the reliability of Ms Heslop's evidence, and whilst the legal arguments being put forward by WS as regards what would have been its substantive appeal are those which were considered by the Supreme Court in *UBS*, that appeal had involved a concession by UBS that the only purpose of the condition was to make the shares "restricted securities"; it had no commercial purpose. (Whilst the condition in DB was described as equally artificial, there does not appear to have been a similar concession as regards the absence of a commercial purpose.)

107. WS submitted that it is implicit that *Haworth* requires the factual matrix of the target case to be materially identical to that of the earlier decision. WS submitted that the condition attached to the Redeemable Shares was wholly different from that in UBS or DB, and it was imposed for rational commercial purposes so as to incentivise all the key staff in the face of external commercial pressures.

108. I do not agree that *Haworth* requires that the factual matrix is materially identical. Fact sensitivity was one of four factors identified, and it is clear from [64] of Lady Rose's judgement that I need to consider whether a small difference in the fact pattern would prevent the principles or reasoning from the earlier ruling applying; and if the application of the earlier ruling is very fact dependent then it may be "more difficult" to form the required opinion.

109. In the present appeal both parties focused on the rationale for the Performance Condition, and whether it had a business or commercial purpose (which would include an incentivisation role) or whether it was simply inserted to ensure that the Redeemable Shares qualified as restricted securities. WS focused on the difference between the turnover target over a three-month period and the conditions which had been included by UBS and DB.

110. The steps implemented by WS are very similar to those which were implemented by UBS and DB, and I agree that the focus needs to be on the nature of the Performance Condition included in the rights attaching to the Redeemable Shares:

> (1) In UBS the condition related to the closing value of the FTSE 100 in a three-week period. There was a "genuine possibility" it might exceed the trigger level. This condition was described as "completely arbitrary", with no business or commercial rationale.
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> (2) In DB the condition applied if an employee voluntarily resigned or was dismissed for misconduct during an eight-week period. Neither contingency was likely, not least because the occurrence was largely within the control of the employee. This was described as equally artificial, and created a "minor risk".

111. Here, the Performance Condition was set by reference to the turnover of WS over a three-month period; optically, this does appear to avoid the criticisms in UBS that it was arbitrary (by reference to an index which had no bearing on the performance of the company itself) or artificial as in DB (as it is within the control of the relevant employees). On the basis of my findings of fact as to the decision of WS to implement the STEP Arrangements, its awareness of the need to include a condition with a genuine risk of forfeiture, the circumstances surrounding the setting of the Performance Condition and the timing of the award of the Redeemable Shares within the three-month period:

(1) I do not accept WS' submission that the Redeemable Shares (or the Performance Condition) operated to incentivise the key employees to whom they were awarded. The evidence adduced by WS was insufficient to support this conclusion; and

(2) when the majority of the shares were awarded on 17 December 2003, WS could be reasonably certain that the Performance Condition would be met.

112. Whilst the conditions attaching to the shares are different from those considered by the Supreme Court in *UBS*, the different fact pattern does not of itself preclude the principles or reasoning therein from applying to the STEP Arrangements. On the basis of my findings as to the facts, the principle set out at [85] of *UBS* can be applied, such that the Performance Condition is not a relevant provision as it has no business or commercial purpose and is instead a commercially irrelevant condition whose only purpose is the obtaining of the exemption.

113. Reaching this conclusion does bring into play the second factor identified in *Haworth*, namely that the relevance of *UBS* does turn on HMRC's (and, on appeal, this Tribunal's) rejection of WS's evidence as being untruthful (or, at least, not reliable). Ms Heslop's evidence on behalf of WS was that the Performance Condition did serve a commercial purpose, operating as an incentive, and was genuinely uncertain. I have already set out my conclusions on that evidence.

114. *Haworth* also makes clear that I need to consider the legal arguments being put forward by the taxpayer, and whether they rely on an argument that was not raised in the earlier ruling and had thus not been determined by that earlier ruling. WS drew attention to the concession which had been made by UBS that the condition attaching to the shares (ie the closing value of the FTSE 100) had no purpose other than to ensure the shares were restricted securities, emphasising that no such concession was made by WS and a positive case was being advanced that there was a commercial purpose. I am mindful of that difference in submissions, but note that this is not a difference in legal arguments, instead it is a submission relevant to my findings of fact and inferences drawn therefrom.

115. On the basis of my findings of fact, and taking account of the factors identified by the Supreme Court in *Haworth*, I am satisfied that there is no scope for a reasonable person to disagree that the principles laid down and the reasoning given in *UBS* would, if applied to the STEP Arrangements, deny the asserted advantage:

(1) The Supreme Court set out detailed reasoning and reached a principle of potentially general application.

(2) The application of that principle does require that the facts are sufficiently similar.

(3) However, the overall arrangement was very similar to the typical scheme described by Lord Reed; as with the UBS and DB appeals, the key difference was the nature of the Performance Condition.

(4) WS has not established that there was a business or commercial purpose to the Performance Condition. The fact that there remained a possibility that the condition might not be satisfied cannot of itself preclude the application of the principles and reasoning in UBS (as such a possibility or minor risk did not do so in either UBS or DB).

116. Accordingly, I am satisfied that the decision of the Supreme Court in *UBS* is a "relevant judicial ruling" for this purpose.

Whether reasonable in all the circumstances not to have taken the necessary corrective action

117. WS' second (alternative) ground of appeal against HMRC's decision to issue the FN penalties is that it was reasonable in all the circumstances for WS not to have taken the

necessary corrective action in respect of the denied advantage. Such necessary corrective action is taken if WS takes the steps set out in s208(5) and (6), which in the context of a FN given after an appeal has been made (ie s204(2)(b) applies) requires that WS takes all necessary action to enter into an agreement with HMRC (in writing) for the purpose of relinquishing the denied advantage and notifies HMRC that it has taken the first step and of the denied advantage and (where different) the additional amount which has or will become due and payable in respect of tax by reason of the first step being taken.

118. The question of what is reasonable in all the circumstances was considered by the Upper Tribunal in *HMRC v Comtek Network Systems (UK) Ltd* [2021] UKUT 0081 (TCC).

119. In *Comtek*, which is also relevant in the context of the approach to be taken to the mitigation of any penalty, HMRC issued a follower notice and APN (which required payment of £22,000) on 29 September 2017, which required action by 3 January 2018. The following then occurred:

(1) The company secretary spoke to HMRC on 13 October 2017 and she said she would take advice on them.

(2) HMRC wrote to the company on 21 November 2017 warning the company that if it did not take corrective action by 3 January 2018 in response to the follower notice it would be liable to pay a penalty.

(3) Comtek did not take the required corrective action by the specified time.

(4) On 15 January 2018 HMRC wrote to the company stating that it was liable to a penalty of 50%.

(5) On 22 January 2018 the company secretary agreed that the company would pay £22,000 in two instalments, on 15 February and 15 March 2018.

(6) HMRC wrote to the company on 23 January 2018 to record what had been agreed.

(7) Comtek paid the two instalments in accordance with the agreed timing.

120. HMRC issued a penalty assessment because of the company's failure to take the necessary corrective action on time, imposing a penalty equal to 50% of the disputed tax.

121. The FTT's findings included:

(1) the reason corrective action was not taken by 3 January 2018 was because the directors had decided to ignore the request in the follower notice to fill in a form to take corrective action or, if not to ignore it, to decide that the form should not be filled in; and

(2) the directors genuinely believed that, by entering into the agreement to pay £22,000, all outstanding issues arising out of the scheme, including the follower notice, the APN and the threatened penalty had been resolved. The FTT considered that belief to be reasonable having regard to the text of the letter of 23 January 2018. The FTT did not have a transcript of the call of 22 January 2018.

122. The Upper Tribunal determined that the phrase "reasonable in all the circumstances" involves the application of a straightforward test (at [32]) and the FTT should give that phrase its ordinary and natural meaning (at [33]). That required the FTT to do the following (but said this is not an exhaustive list of the examination required in all cases):

(1) The FTT needed to consider why the company chose not to take corrective action as its thought process formed part of the relevant "circumstances".

(2) The FTT also needed to take into account the fact that the question of whether it was "reasonable in all the circumstances" not to take corrective action operates as a

defence to a penalty that applies if corrective action is not taken by a deadline. Accordingly, the fact that the deadline was missed, and the company's reasons for missing it were highly relevant.

(3) The FTT needed to take into account the structure and purpose of the relevant provisions of FA 2014. Those provisions are designed to ensure that taxpayers who fail to take corrective action by the deadline in response to a follower notice are to suffer a penalty unless, among other defences, they can establish that it was reasonable in all the circumstances not to take the corrective action. Once a taxpayer fails to meet the deadline, even if that failure was not reasonable in all the circumstances, it is not pre-ordained that the maximum penalty of 50% will be charged, since s210 provides for the penalty to be mitigated if there has been "co-operation" as statutorily defined. But it would be quite contrary to the purpose of the legislation for a taxpayer who misses the deadline for no good reason to enjoy complete exemption from a penalty simply because of actions taken after the deadline has been missed.

123. The Upper Tribunal concluded that there was only one possible answer on the facts as found by the FTT, namely it was not reasonable in all the circumstances. In that case, the company's actions after the deadline passed "were of potential relevance" to the amount of the penalty, but did not entitle it to complete exemption. The Upper Tribunal then added the following:

> "35. ...We will say only that we consider that it may be possible, in some limited circumstances, for events taking place after the deadline for taking corrective action to have some bearing on the question whether it was "reasonable in all the circumstances" for a taxpayer not to take that action. The only example we have been able to think of, though it may be that with the benefit of full legal submissions from the Company we might have found more, is that of a taxpayer who, having received a follower notice, decides to continue to contest the underlying appeal considering that the "final judicial ruling" on which HMRC rely was either wrongly decided, or not determinative of the taxpayer's appeal. Such a taxpayer could be assessed to a penalty as soon as the deadline is missed. The question whether it was "reasonable in all the circumstances" for the taxpayer to continue to 12 contest the appeal could, in our judgment, be informed by an analysis of how that appeal ultimately fares. For example, if it is struck out as having no prospect of success, that might suggest that it was not "reasonable in all the circumstances" not to take corrective action; the conclusion might be otherwise if the taxpayer is ultimately successful."

124. WS's position was:

(1) WS had received advice from Mr White and Mr Firth to the effect that its case was materially distinguishable from those of UBS and DB so that it was not compelled to comply with the FN. WS considered and reasonably followed that advice.

(2) WS commenced JR proceedings seeking to quash the FN, and at no stage did HMRC suggest that they were spurious.

(3) Once a commercially-driven decision to settle was taken, WS took all appropriate steps (including payment of the tax) to take corrective action and withdrew both its appeals and its JR claim.

(4) It was reasonable for WS to decide to exercise its right to challenge the FN rather than to take irrevocable corrective action, and it is important that WS relied on advice that any JR claim and its grounds of review would be grounds of defence against any FN penalties.

125. The Upper Tribunal in *Comtek* made it clear that I should first consider why WS chose not to take the corrective action, as its thought process formed part of the relevant circumstances. Here, WS's argument is essentially that it relied on advice that it did not need to take such action (as it was arguing that there was no relevant judicial ruling and thus no valid FN) and was taking positive steps to seek to quash the FN (by bringing a claim for JR) and had been advised that this would be a defence to any FN penalties. The failure to take the necessary corrective action by the extended deadline was thus not an example of a missed deadline, or a misunderstanding of what was expected – it was a deliberate decision by WS, but one which they submit was reasonable in all the circumstances.

126. I have addressed the facts of the different appeals (ie UBS, DB and this appeal) in the context of reaching my decision that *UBS* was a relevant judicial ruling. That conclusion does not of itself mean that it could not have been "reasonable in all the circumstances" for WS to have not taken corrective action. It does, however, emphasise the need to assess the advice received (including the matters on which advice was sought and what was done in response to that advice). On the evidence before me, as to both the advice and the circumstances:

(1) The directors of WS were not tax experts; they were, however, used to instructing tax advisers, were familiar with receiving detailed tax advice from counsel, and Ms Heslop maintained relationships with key individuals from Deloitte.

(2) WS implemented transactions in both 2003-04 and 2004-05 (ie the STEP Arrangements and the DOTAS Arrangements) to extract cash from the company in a tax-efficient manner. Those transactions had been presented to them by Deloitte and required that WS effect a series of pre-ordained steps, including establishing EBTs and a new group company offshore.

(3) There is documentary evidence of the advice WS received ahead of the implementation of the STEP Arrangements, notably in the form of the note of conference with Mr Trevett and the email exchanges with Deloitte about setting the Performance Condition. Ms Heslop was aware of the need for a genuine risk of forfeiture.

(4) WS did not take further advice on the merits during the course of HMRC's enquiry into the STEP Arrangements.

(5) Ms Heslop rejected a description of the STEP Arrangements as "tax avoidance" on the basis that her understanding was that this phrase referred to a situation where tax was due but a person avoided paying it. However, irrespective of the label or description used, the presentation of the scheme, the pre-ordained steps, the crafting of the Performance Condition and the detailed analysis of the tax treatment and risks involved in the conference with Mr Trevett meant that WS either was or should have been aware that they would need to assess carefully the potential impact of developing case law on the prospects of success in relation to their substantive appeal. This would have been reinforced by the amount of money at stake once HMRC issued the determination and decisions.

(6) WS's appeal was stayed behind UBS, and they received regular litigation updates from HMRC over a number of years. It was apparent from those updates that HMRC considered that the outcome of the appeal in UBS would be determinative of WS's own appeal; and HMRC reiterated this when informing WS of the decision of the Supreme Court (in their letter of 21 April 2016), in which they said that if WS considered its facts were different they should write setting out the basis on which they were distinguished.

(7) There is minimal documentary evidence of the advice which was taken after the issue of the determination and decisions in February 2009. On the lack of documentation:

(a) Ms Manzano submitted that it was unfair to criticise WS for not waiving its privilege in its advice. In principle, I agree. However, when she was giving her evidence Ms Heslop did not state that WS had received written advice which was not in the bundle as such advice was privileged (or confidential or commercially sensitive). Instead, she referred to calls and meetings with Mr White and Mr Firth. Ms Heslop did imply that there was some written advice, but these references were very vague, she could not explain what it had related to, or why it was not in the bundle, and referred back to Mr Firth having drafted the representations to HMRC and the grounds for review.

(b) The time which has passed means that it is not surprising that documentary evidence from the implementation of the arrangements may no longer be available. Here, notably, most of the documentation had been exhibited by HMRC from papers provided to them during the course of the enquiry. However, whilst events from that time are part of "the circumstances" which I need to consider, they are of far less importance than the events since the decision of the Supreme Court in *UBS* in March 2016 and the issue of the FN in February 2017. WS knew their actions would be scrutinised as they were deciding not to comply with the FN, and I would expect that they would take care to preserve potentially relevant documentation.

(8) I infer that there was no detailed written advice on the impact of the Supreme Court decision in *UBS* on the substantive appeal (ie how this precedent might be applied to the STEP Arrangements, separate from the follower notice regime) or in relation to the validity of the FN. This means that the evidence of the advice received by WS is Ms Heslop's evidence, the representations made by WS in May 2017 and its grounds for review (the draft of which was sent to HMRC in September 2017) and the email exchange with Mr Firth in October 2017.

(9) Addressing that evidence (including the lack thereof) as to advice received and actions taken:

(a) Ms Heslop said that WS had been told of the Supreme Court decision by Mr White before they received the letter from Mr Hardy in April 2016. However, there was no documentation showing detailed advice received; or of internal discussions within WS of advice received and risks involved. This was against the background that Mr White had been consistently advising WS that HMRC would not be successful in UBS; he had been proved wrong, and had referred to HMRC as having won "against all odds", but WS did not consider obtaining a second opinion.

(b) WS had been instructing Mr Firth since around December 2015, as he had drafted the representations sent to HMRC in response to the follower notice issued regarding the DOTAS Arrangements. They did not seek advice from Mr Firth as to the merits of the substantive appeal in relation to the STEP Arrangements.

(c) WS were told that HMRC intended to issue a follower notice in April 2016, and the FN was issued in February 2017. Whilst Ms Heslop's evidence was that these letters would have been sent to their advisers, I consider that she had paid little attention to the detail of these letters herself. She confirmed that she had not read the decision in *UBS*, saying she would not have understood it. It is not unreasonable to rely on advisers; but in so doing it is important to try to understand HMRC's position in order to test and challenge advice received.

(d) Whilst the representations sent to HMRC and grounds for JR set out WS's position in relation to the FN, they cannot tell me anything about the instructions which had been given to Mr Firth, or his awareness of the details in relation to the

setting of the Performance Condition (including what had been known at various times as to its likelihood of its being met) or as to what advice had been received in relation to the substantive appeal (absent the FN). Indeed, although Ms Heslop said she thought that he would have been given the transaction documentation, the very uncertainty about this casts doubt on the extent to which he had been fully briefed on the transaction; this is particularly important in the context of whether he understood how the Performance Condition had been set, the information which had been available to WS at that time and other matters relevant to whether that condition had a business or commercial purpose.

(e) Ms Heslop said that, as regards the merits of the claim for JR, they were advised by Mr White that "100%" they had nothing to answer for. This is just not credible; either Ms Heslop's recollection is mistaken, or Mr White was demonstrably and unreasonably over-optimistic to an extent that this should have been readily apparent to WS.

(f) There is no substantive evidence of WS engaging with the responses they received from HMRC in August 2017 or October 2017. HMRC's letter of August 2017 had referred to WS's explanation that the restrictions in the shares were not arbitrary and did not lie largely within the control of the employees; HMRC said that the restrictions were artificial. HMRC's reasoning is very brief. However, HMRC's response to the letter before claim for JR is more detailed, and sets out HMRC's position on the grounds and deals with arguments put in relation to *UBS*. In particular, the grounds had set out WS' position that the issue in the decided case must be incapable of rational distinction (as a matter of law or fact) from that in the immediate case. This was directly addressed by HMRC in their response, setting out that FA 2014 contained no such requirement.

(g) It was this response from HMRC that was the subject of the exchange of emails with Mr Firth. Mr Firth said WS had "reasonable arguments" to support the claim for judicial review, but added that there is no guarantee of success and judicial reviews are always difficult. This is not a ringing endorsement of their prospects of success. In any event, it is clear that at this stage the subject-matter of the advice was the JR claim, not the substantive appeal.

(h) I recognise that this exchange, very shortly after receipt of the letter from HMRC, was likely to be only part of the story. However, WS have not provided me with more, either in terms of documentary evidence or a detailed explanation of how they considered the points raised by HMRC. Instead, all the evidence shows is that they filed a claim for JR using grounds for review which Ms Heslop acknowledged were the same as those which HMRC had addressed in its response.

(i) Ms Heslop's evidence was that WS relied on advice that any JR claim and its grounds of review would be grounds of defence against any FN penalties. Whilst bringing a JR claim is relevant, this must be considered in the light of the advice as to the prospects of success of such claim; and there is no evidence of any detailed discussion or challenge to this, at a time when there were no authorities on what might constitute "reasonable in all the circumstances", and moreover no evidence of any advice and discussion of the risks inherent in this approach.

(j) WS had opportunity after HMRC set out its position on 3 October 2017 to re-consider its position as to taking corrective action, as HMRC extended the deadline to 30 October 2017. However, there was no evidence of WS having considered such a course of action.

(10) WS sought to rely on HMRC not having said that the JR claim was spurious. However, that claim was at a very early stage when it was stayed by agreement, and HMRC had responded to the representations made by WS by upholding the FN and also said, in their letter of October 2017 responding to the letter before claim, that it did not accept that any of the grounds were sustainable in law. HMRC's position was clear.

(11) Once WS decided to settle the substantive dispute, WS took all steps to take corrective action and withdraw its appeals. WS did not approach HMRC about reaching a settlement until September 2018 and effectively decided to concede their appeals. They then complied with the terms of the settlement agreement in taking steps to withdraw their appeals. The fact of a settlement being reached means that the substantive appeal was never determined by a court or tribunal.

127. WS were faced with a decision of the Supreme Court in 2016 which unanimously found in favour of HMRC in relation to the appeals of two taxpayers, behind which their own appeal had been stayed, and which had addressed the differences in the conditions attached to the shares, and a follower notice from HMRC setting out HMRC's position that *UBS* was a relevant judicial ruling and requiring WS to follow it.

128. Taking account of all the circumstances, the advice received and actions taken by WS fall significantly short of establishing that it was reasonable in all the circumstances for them not to take the necessary corrective action. I bear in mind the draconian nature of the regime, and that taking corrective action is the permanent abandonment of an appeal; but on the basis of the evidence before me, despite having their own appeal stayed behind the appeals of UBS and DB for several years on the basis that their appeal was similar, WS did not grapple with the impact of the *UBS* decision on their substantive appeal, and the representations made to HMRC and the claim for JR demonstrate a desire to quash the FN but do not address he prospects of the JR claim succeeding (the only clear evidence of prospects being Mr Firth's reference to "reasonable arguments"). The timing of the steps taken in relation to the settlement agreement, which only started almost a year after the extended deadline for taking corrective action, means that they are at best neutral when considering the reasonableness of WS' actions before the specified date.

129. I recognise that robust advice as to the prospects of succeeding in a JR claim to quash the FN, against a backdrop of advice that the taxpayer should succeed on the substantive appeal, may form a successful basis for arguing that it was reasonable in all the circumstances not to take the necessary corrective action required by a follower notice. But that was not the evidence of the position on the facts in this appeal.

130. WS's appeal against the imposition of the FN penalties is dismissed.

Level of mitigation of the penalty

131. HMRC gave notice of the assessment of the FN penalties on 13 March 2018. The amounts assessed were £1,607,791.30 for PAYE and £554,466.31 for NICs. These were calculated as 50% of the value of the denied advantage. Section 210 FA 2014 enables HMRC to reduce the amount of the penalty to reflect the quality of co-operation given by the person liable to pay the penalty.

132. When assessing the penalties HMRC did not give any reduction for co-operation. In May 2020 HMRC informed WS that 20% mitigation would be allowed for co-operation within s210(3)(a), ie assisting quantifying tax. HMRC's position is that no further mitigation should be allowed – the only action taken by WS in the period which can be taken into account was the letter of 9 February 2018 (which had been reflected in allowing 20% mitigation), and no steps had been taken by WS towards settlement or counteraction before the penalty was

assessed. There had been no indication from WS prior to September 2018 that it was willing to consider settlement. This contrasts with the facts in *Comtek* where there had been a phone call prior to the assessment of the penalty.

133. WS submit that they have co-operated fully with HMRC (referring to their compliance with requests for information) and should be allowed the maximum reduction, which would reduce the penalty to the minimum specified, ie 10% of the denied advantage. WS submit that the only pointer towards a lack of co-operation was the decision not to comply with the FN itself, but this was not an example of wilful disregard of the FN but as a result of exercising its rights to pursue JR.

134. In *Comtek* the Upper Tribunal confirmed (at [8]) that "co-operation" has by s210(3) a limited and specific meaning, and not everything that might in ordinary usage be referred to as co-operation is to count. Furthermore, "counteraction" can count even if it is provided after the deadline specified by s208 but must be provided before the penalty is assessed.

135. HMRC had initially assessed the penalty in *Comtek* at the maximum 50%, but its position before the Upper Tribunal was that the company had co-operated within s210(3)(a) (providing HMRC with reasonable assistance in quantifying the tax advantage) and HMRC were prepared to give the maximum credit within their internal policy of 20% of the mitigation available. This meant that HMRC's position in that appeal, as here, was that the penalty should be 42% of the disputed tax.

136. The Upper Tribunal thus proceeded on the basis that there was co-operation within s210(3)(a) as this had been accepted by HMRC (at [41]).

137. The Upper Tribunal stated that "counteraction" in s210(3)(b) embraces a "broader category of action" than the similar concepts referred to in s208(5) (at [43]), as Parliament has chosen not to replicate the concept of taking all necessary steps to reach agreement with HMRC, and s210(2) requires the nature and extent of any counteraction to be considered (which would be redundant if a taxpayer had to have done everything that was required). The concept of counteraction needs to be understood purposively, and full counteraction occurs if the taxpayer gives up the appeal and communicates that fact to HMRC. However, mere payment of the amount in dispute or of any APN does not of itself amount to full counteraction – that amounts to compliance with a statutory obligation (at [46]).

138. The Upper Tribunal considered at [50] that the combination of the company's agreement of a payment plan for the APN, honouring that plan and its subjective belief that it was thereby compromising all outstanding disputes with HMRC, represented "a step on the way to counteraction".

139. When considering how much credit to give the company for the co-operation it gave the Upper Tribunal set out the following:

> "51. …We have seen some decisions from the FTT that have approached this as a largely arithmetic exercise: for example allocating a notional 20% amount of maximum mitigation to each of the five categories of "co-operation" specified in s210(3) and then deciding how much mitigation to award in each of those five categories in order to reach an overall penalty total. We consider that such an approach risks losing sight of the holistic nature of the exercise and also the fact that, given the overall purpose of the follower notice legislation to which we have referred, "counteraction" of the tax advantage should in most cases tend to attract greater credit than the other categories. It also gives rise to conceptual difficulties. To take an example, in some cases the "tax advantage" at issue might be so straightforward to quantify that HMRC have no real need of assistance that could constitute co-operation

> falling within s210(3)(a). If a notional 20% of maximum mitigation was available for that category, the question would arise whether the taxpayer should obtain no credit at all (which might operate harshly since if it provided all necessary co-operation in other categories it could still not obtain maximum mitigation) or whether it should obtain the full 20% of maximum mitigation (which might appear generous when HMRC in fact needed no assistance).
>
> 52. We will, therefore, apply the following approach when deciding what level of penalty to impose:
>
> (1) We will approach the question holistically. Recognising that not all of the categories of "co-operation" set out in s210(3) are relevant in this case, we will not seek to allocate an overall level of discount to each of those categories, but rather will seek to give the Company credit for the overall level of "co-operation" afforded.
>
> (2) We will recognise that the overall purpose of the regime is to discourage taxpayers from pursuing, without good reason, disputes about tax advantages which HMRC reasonably consider to have been determined in their favour in other final decided cases. Co-operation that comes closest to addressing that purpose should, accordingly, attract the greatest credit and conversely, if the Company's actions, even if technically meeting the definition of "co-operation", have done relatively little to meet the statutory purpose, correspondingly lower credit should be given.
>
> (3) Where the Company took steps falling within s210(3), we will consider the overall effectiveness of those steps in meeting the purpose of the provisions, recognising that even if those steps were not fully effective, and more could reasonably have been done, some partial credit may still be appropriate."

140. Applying that approach, the Upper Tribunal considered an appropriate penalty rate would be 30% (raising the level of mitigation from 20% awarded by HMRC to 50%). That recognises the company's genuine attempt to effect some late counteraction, whose effect was that no more HMRC resources in practice needed to be allocated to the appeal relating to the scheme, whilst recognising that it fell a long way short of what was needed to achieve full counteraction and was based on an unreasonable belief (see [53]).

141. The parameters for determining whether there has been co-operation are thus set out in s210 itself, and the approach to be taken thereto has been considered by the Upper Tribunal in *Comtek*. In particular:

> (1) It is clear from s210(1)(b) that the co-operation in question must be before the penalty was assessed.
>
> (2) The quality of the co-operation includes its timing, nature and extent.
>
> (3) Section 210(3) then sets out the only forms of co-operation which may count towards mitigation.
>
> (4) When deciding the level of penalty to impose I follow the approach set out at [52] of *Comtek* and approach the question holistically, recognising the purpose of the regime and looking at the overall effectiveness of any steps taken in meeting the purpose of the provisions.

142. Mr Hardy had informed WS that he was seeking authorisation to issue follower notices on 21 April 2016. They were issued on 17 February 2017 and the deadline for taking corrective

action was 23 May 17 but subsequently extended to 28 September 2017 and then 30 October 2017. HMRC did not give notice of the penalty assessments until 13 March 2018.

143. Looking at the actions taken by WS during this period, the only acts were:

(1) the making of representations in May 2017;

(2) those related to the commencement of JR proceedings, including the letter before claim, the issuance of proceeding and the agreement of a stay; and

(3) WS' letter to HMRC of 9 February 2018 which, whilst it appears to have been sent in the context of the DOTAS Arrangements, did include information relevant to the STEP Arrangements, in particular background (which had been set out before in the representations on the FN) and the Turnover Comparison.

144. However, these actions must be viewed against the backdrop that WS had responded to requests for information from HMRC and, whilst I do not accept the submission that WS had provided everything that had been asked for (as explained below), I do consider that HMRC already had all the information they needed to quantify the tax advantage and did not need this to be provided during the relevant period:

(1) Mr Gebski's evidence was that after *UBS* decision had been handed down by the Supreme Court in March 2016 Mr Hardy reviewed the scheme documents; his approach was to look at the facts of each case and determine whether it was appropriate to issue a FN. He decided to seek authorisation to do so (saying as much in his letter to WS on 21 April 2016). He had not asked for any additional information to conduct this exercise. Nor did they ask for any additional information in order to issue the APNs.

(2) It is notable that the APNs issued by HMRC on 17 February 2017 were for the same amounts as the Regulation 80 Determination and Section 8 Decisions that had been issued on 4 February 2009. Neither party adduced any evidence that these numbers were incorrect.

(3) In an e-mail of 12 September 2019 Mr Hardy stated:

> "During the FN process period we did not ask your client for any information to enable the tax advantage to be quantified because all parties already knew what the quantum of the tax advantage was and had known that quantum for many years. There was nothing therefore for your client to co-operate with in that context."

145. The caveat referred to above relates to a request which had been made by HMRC for bank statements of the trusts. On the basis of the evidence before me, it is clear that HMRC had requested bank statements in relation to the transactions which had been entered into, and those that were in the possession of WS had been provided to HMRC in June 2007. There was no evidence of the remainder being provided until the letter of February 2018 which refers to certain bank statements being enclosed. However, whilst this shows that HMRC did not, contrary to WS' submission, have all the information they had requested, I consider that they did have all the information they needed to quantify the tax advantage.

146. Whilst WS did initiate settlement discussions with HMRC in relation to the STEP Arrangements (as well as the DOTAS Arrangements), the first indication that it might be willing to do so was in September 2018, after the penalties had been assessed. That step cannot therefore count as relevant co-operation for the purpose of mitigating the penalties. However, I recognise that s210(3)(d) provides for co-operation to include providing information to HMRC to enable HMRC to enter an agreement for the purpose of counteracting the denied

advantage. That limb of the definition is distinct from s210(3)(a) but I take account of the level of information which had previously been provided by WS.

147. Section 210(3)(b) provides that co-operation includes counteracting the denied advantage, and it is clear from *Comtek* that this limb should attract greater credit than the other categories of co-operation. WS's submissions on counteraction focused on the reasons why WS had not taken steps during the relevant period – they had taken advice and were exercising their legal rights to challenge the FN by way of JR. I have addressed that in the context of considering whether the actions were reasonable, but those actions reinforce my conclusion that WS did not take steps to counteract the denied advantage during the relevant period, even construing that phrase broadly. That failure is significant when considering the purpose of the follower notice provisions.

148. Having regard to WS's actions in the relevant period in the light of all the circumstances, I consider that HMRC have not given enough credit to the level of co-operation which was provided by WS, in that WS could do no more to provide information which was reasonably necessary to HMRC. However, the failure to take steps on the way to counteraction is a significant limitation on the level of mitigation that can be afforded. I consider that WS should be given credit of 40% in respect of the quality of its co-operation, thus reducing the penalty to 34% of the denied advantage.

DISPENSATION

149. WS's appeal against its liability to a penalty is dismissed. Its appeal against the quantum is allowed in part; the penalty is reduced to 34% of the denied advantage.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

150. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

JEANETTE ZAMAN
TRIBUNAL JUDGE

Release date: 23 MAY 2022