TC01920

Appeal number: TC/2011/06101

INCOME TAX – Appellant leaving employment as senior civil servant in April 2007 – Payment by former employer made in December 2007 – Whether a payment in consideration or in consequence of, or otherwise in connection with, the termination of the Appellant's employment (ITEPA s.401) – In the circumstances of the case, no – Whether "earnings" (ITEPA s.62) – In the circumstances of the case, yes – Appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

PHILIP BOVEY **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE CHRISTOPHER STAKER
MR NIGEL COLLARD

Sitting in public in London on 17 February 2012

The Appellant in person

Mr W Kelly, Presenting Officer, for the Respondents

DECISION

Introduction

1. The Appellant appeals against a closure notice amending his 2007/08 self-assessment tax return under s.28A(1) and (2) of the Taxes Management Act 1970.

2. The Appellant was formerly a senior civil servant employed with the Department of Trade and Industry ("DTI") which subsequently became the Department of Business, Innovation and Skills ("BIS"). He retired from that employment on 5 April 2007. In December 2007, some 8 months after his retirement, he received a payment from the Department of £6,500, from which income tax and National Insurance contributions were deducted. This amount was declared in his tax return as an exempt lump sum.

3. The closure notice appealed against concluded that the payment of £6,500 was assessable as earnings under s.62 of the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA"). That position is maintained by HMRC in the present appeal.

4. The position of the Appellant in his dealings with HMRC, and in this appeal, is that the payment of £6,500 was assessable under s.401 ITEPA as a payment received in connection with the termination of his employment, and is therefore tax exempt.

Applicable legislation

5. Part 3 of ITEPA is entitled "Employment income: earnings and benefits etc treated as earnings". Chapter 1 of Part 3 is entitled "Earnings". Section 62 ITEPA, which is in Chapter 1 of Part 3, provides in relevant part as follows:

> (1) This section explains what is meant by "earnings" in the employment income Parts.
>
> (2) In those Parts "earnings", in relation to an employment, means—
>
> (a) any salary, wages or fee,
>
> (b) any gratuity or other profit or incidental benefit of any kind obtained by the employee if it is money or money's worth, or
>
> (c) anything else that constitutes an emolument of the employment.

6. Part 6 of ITEPA is entitled "Employment income: income which is not earnings or share-related". Chapter 3 of Part 6 is entitled "Payments and benefits on termination of employment, etc". Section 401(1) ITEPA, which is in Chapter 3 of Part 6, relevantly provides as follows:

> (1) This Chapter applies to payments and other benefits which are received directly or indirectly in consideration or in consequence of, or otherwise in connection with—
>
> (a) the termination of a person's employment,
>
> (b) a change in the duties of a person's employment, or

(c) a change in the earnings from a person's employment,

by the person, or the person's spouse or civil partner, blood relative, dependant or personal representatives.

…

(3) This Chapter does not apply to any payment or other benefit chargeable to income tax apart from this Chapter.

7. Section 403(1) ITEPA then provides as follows:

(1) The amount of a payment or benefit to which this Chapter applies counts as employment income of the employee or former employee for the relevant tax year if and to the extent that it exceeds the £30,000 threshold.

The evidence and submissions of the parties

8. At the hearing, the Appellant represented himself, and HMRC was represented by Mr Kelly. The Tribunal had before it a bundle of documents prepared by HMRC, the case file, and some additional documents produced for the hearing.

9. The documents in the case include amongst other items the following.

10. There is what appears to be an extract from Hansard for 2 March 2007, containing a statement from the Prime Minister concerning the Government's response to the recommendations contained in the 29th Report of the Review Body on Senior Salaries. It is stated here amongst other matters that "*The recommendation for bonus awards is also being accepted, but payment will be delayed until 1 November 2007*".

11. There is a letter dated 31 May 2007 from BIS to the Appellant, headed "2007 PAY AWARD", which states: *"The Department's Pay Committee has now made final decisions on 2007 SCS pay, and I'm now writing to you with the result. I am pleased to say that you have been awarded a bonus of £6,500 in recognition of your excellent work on company law reform. The bonus will be paid in November in line with the Government's response to the Senior Salaries Review Report*". There is a handwritten annotation on this letter, stating "*Paid Nov 07 [illegible] 3/12/07*".

12. There is the payslip for the payment of £6,500 made in December 2007, which describes the payment as being "Special merit bo".

13. There is a letter from the Pay and Records Office (the "Cardiff office") of BIS dated 4 February 2010, responding to an enquiry from HMRC, stating that the Cardiff office had the Appellant's payslip records from 31 October 2004 until his last payslip on 30 April 2007, and confirming that the Appellant had received special merit bonuses on 30 April 2005, 28 February 2006 and 31 January 2007. The letter went on to say as follows: *"The special merit bonuses are payments awarded by the individual departments and can widely vary in what they are awarded for, it is basically down to the discretion of the managers of the departments, however all special merit bonuses are taxable."* *The letter concluded that "We do not have a record of a payslip with a one off payment of £6500*".

14. HMRC followed up this enquiry by providing the Cardiff office with a copy of the payslip for the £6,500 payment. There is a further letter from the Cardiff office dated 7 April 2010, responding to this, stating: *"As long as we receive the request at pay and records and it has been approved by the manager, we do not go back and request further confirmation. The 'special merit bonus' is just a code that we use to enter these various bonuses on to our systems. I'm afraid as this goes so far back to 2007, that I do not have information stating exactly what the bonus was issued for.*"

15. There is an exchange of correspondence (both mail and e-mail) between the Appellant and the human resources department of BIS ("BIS HR"). On 7 June 2010, BIS HR advised "*The aforementioned bonus payment was due to your performance on company law reform*". On 22 June 2010, BIS HR advised: "*It appears that the payment in question is your CSS Pay Award, as awarded in accordance with the guidelines supplied by your department at the time. This award was taxable, and the sum of £1,430 was deducted as a result*".

16. On 3 July 2010, the Appellant followed up with an e-mail to BIS HR stating the following: "*As I understand it, the SCS Pay Award arrangements had two elements: an increase (or not) in basic salary, by reference to top, middle and bottom performance tranches, and a possible performance bonus. The notification which I received dated 31 May 2007, a further copy of which you kindly forwarded to me, makes no mention of salary or tranches. It referred only to a bonus. As I understand it from the Department's Annual Report for 2007, only those in the top tranche and some of those in the middle tranche were eligible for a bonus under the arrangements. They do not seem to cover the case of someone who was not put in a tranche at all, and certainly not in the middle or top tranche*". There are further e-mails to December 2010 in which the Appellant chases up a response to this enquiry, although the Appellant's evidence is that no response was ever provided.

17. The Appellant gave evidence as follows.

18. Having received the payment in December 2007, the Appellant was unsure how to treat it when it came to completing his tax return. He was by then not in employment, and there was no box in the tax return to put it in. As the deadline for completing the tax return was approaching, there was no time to call HMRC. He included it in box 9 ("Compensation and lump sum £30,000 exception") of the "Share schemes and employment lump sums, compensation and deductions" page of the tax return. He then subsequently received a tax refund.

19. Subsequently, HMRC got in touch with him, opening an enquiry into his tax return for the year ended 5 April 2008 and expressing the view that the payment was taxable under s.62 ITEPA. The Appellant asked for a review. In a decision on 27 July 2011, at the end of the review, HMRC upheld the decision that the sum was taxable under s.62 ITEPA. The Appellant disagrees with HMRC's conclusion.

20. The Appellant is not aware of a bonus ever having been paid in the civil service to a person who had ceased their employment, or to a person who was in their notice period. HMRC has no information from DTI/BIS as to the nature of the payment.

The Cardiff office has confirmed that they do not know the details. The statement in the closure notice that "*your previous employer has confirmed this payment was in respect of a special merit bonus*" is simply incorrect.

21. Of the three bonuses that the Cardiff office said that the Appellant had previously received (paragraph 13 above), the two smaller ones were team bonuses, and the largest one was an individual bonus.

22. The Appellant gave detailed evidence of the circumstances of his employment, and of his decision to take early retirement, and of the procedure for the award of bonuses to members of the senior civil service. The Appellant's position, as set out in his letter of 30 May 2010 to BIS HR, is as follows: *"I am not aware of anything I could have done in the period between January and March 2007 to justify a further award. I does not appear that the award was under that scheme … Rather, my understanding is that the award was made centrally, that it related to the circumstances of my leaving employment and that it would not have been awarded but for the fact of my leaving*". The Appellant referred to the terms of the 31 May 2007 letter from BIS. He said that if the payment had been a bonus under the senior civil service pay scheme, the letter would have said what tranche he was in, and that he had received a pay increase. It would not have said that the bonus was being paid for a specific reason, but would have stated more generally that it was for exceeding objectives. The Appellant submitted that this was not a bonus under the senior civil service pay scheme. He considered that the appropriate explanation was that it was a one off *ex gratia* payment that had been made because he had left his employment, and that it was appropriately to be considered as falling under s.401 ITEPA.

23. For HMRC, Mr Kelly submitted as follows. By virtue of s.401(3) ITEPA, Chapter 3 of Part 6 does not apply to any payment or other benefit chargeable to income tax apart from that Chapter. The real issue is therefore whether s.62 ITEPA applies to the £6,500 payment, since, if it does, s.401 by its own terms does not apply. (The Appellant indicated that he did not dispute this.) The 31 May 2011 letter from BIS stated expressly that the payment was "*a bonus of £6,500 in recognition of your excellent work on company law reform*". The Appellant wants the Tribunal to accept that the payment was for something other than what this letter expressly says it was for. There is no evidence that the letter was connected to the Appellant's departure from his employment. Even if the bonus was in respect of the 2006/07 tax year, it is taxable in 2007/08 as it was paid in 2007/08. There is nothing to show that it was outside the discretion of the Department to award such a bonus. It is irrelevant that the payment was not referred to in the letter confirming termination of the employment. The fact that there was no custom or practice of making such payments is not a matter on which any great weight should be placed. Even if the payment was *ex gratia*, that would not mean that s.62 ITEPA does not apply as that section expressly applies also to a "gratuity" (s.62(2)(b)). There is no reason to think it would not have been paid if the Appellant's employment had continued. The payment was made because the Appellant was a former employee of DTI/BIS. It was paid for his "excellent work on company law reform" and was therefore a reward for his services in his employment. The terms of ITEPA ss.6, 7, 16 and 18 were also referred to.

24. In reply, the Appellant submitted as follows. Although s.62 ITEPA may be very broad, it must have limitations. Payments by DTI/BIS are subject to public law and must comply with applicable rules. The rules prescribe the types of payments that can be made. In the civil service, a Department cannot make a payment just because it feels like it. This payment could not have been made under the civil service performance scheme, and therefore was not a performance bonus. Although s.62(2)(b) refers to a "gratuity", the expression "gratuity" means for instance a tip, and does not have the same meaning as "*ex gratia*". The Appellant worked on company law reform for many years, so the statement that the payment was for this work could be characterised as a kind of gold watch for a person leaving employment rather than a payment for particular services. The Appellant received a bonus in January 2007 and did nothing thereafter until he left in March 2007 that would have justified a further bonus. It was therefore not a bonus for particular services. It is accepted that the line between s.62 and s.401 is unclear, but this case falls on the s.401 side of the line.

The Tribunal's findings

25. The Tribunal has considered the evidence as a whole. Failure to refer to particular items of evidence in this determination does not mean that they have not been considered.

26. The Tribunal is required to make findings of fact on the basis of the evidence before it, on a balance of probabilities.

27. The Tribunal finds that the 31 May 2007 letter from BIS is clear in its terms. It stated that the payment is the result of the Department's Pay Committee's final decision on 2007 SCS (Senior Civil Service) pay. It stated that the payment is a bonus, in recognition of excellent work undertaken by the Appellant, and it stated that the payment would be made in November 2007 in accordance with the Government's response to the Senior Salaries Review Report. The fact that the payment was ultimately made in December 2007 is consistent with this.

28. The Tribunal is not satisfied on the evidence before it that it was beyond the discretion of the Department under applicable rules to award such a bonus to the Appellant in his particular circumstances, given that he had left his employment in April 2007. The fact that the payment was made is strong evidence that it was within the discretion of the Department to make it. In any event, even if the Department did exceed its discretion in awarding a bonus to the Appellant in the circumstances, the Tribunal is not persuaded that this would affect its tax treatment when received by the Appellant. The fact is that the Department paid a bonus to the Appellant, whether or not it was entitled to do so, and the Appellant received that bonus.

29. On the evidence before it, the Tribunal finds that the payment was a bonus falling within s.62 ITEPA. It was common ground that, if that is so, s.401 is inapplicable by virtue of s.401(3).

30. It follows that the appeal must be dismissed.

31. 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.

DR CHRISTOPHER STAKER

TRIBUNAL JUDGE

RELEASE DATE: 28 March 2012