TC08010

Discovery assessment – could hypothetical officer reasonably be expected to be aware of insufficiency- untaxed gain included in STRGL not P&L - information provided by other group companies to HMRC – whether provided on behalf of Appellant -

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2010/ 09176

BETWEEN

BALL EUROPE LIMITED **Appellant**

-and-

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

TRIBUNAL: JUDGE RACHEL SHORT
PATRICIA GORDON

The hearing took place on 1 – 3 December 2020. With the consent of the parties, the form of the hearing was V (video) through the Tribunal video platform.

Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.

Ms Nicola Shaw QC of Gray's Inn Tax Chambers for the Appellant

Ms Rebecca Murray, of Devereux Chambers instructed by the General Counsel and Solicitor to HM Revenue and Customs for the Respondents

DECISION

INTRODUCTION

1. This appeal by Ball Europe Limited ("BEL") concerns whether HMRC's discovery assessment issued to BEL on 12 July 2006 was valid and fulfilled the conditions at paragraph 44 of Schedule 18 Finance Act 1998 ("FA 1998"). In particular whether, by reference to the information which had been provided by BEL to HMRC in its CT600 tax return, computation and accounts for the relevant period (28 November to 31 December 2003) a hypothetical officer could not have been reasonably expected to be aware of the fact that an amount which ought to have been assessed to tax had not been assessed to tax, by reference to paragraph 44(1)(a) of Schedule 18.

2. It also considers whether material other than BEL's CT600, tax computation and accounts should be treated as provided to HMRC for these purposes under paragraph 44(2)(d)(ii) of Schedule 18 FA 1998 when that material had been provided in response to correspondence which concerned other members of the Ball group of companies in the UK.

BACKGROUND FACTS

3. The parties provided an agreed statement of facts, of which the relevant background facts are set out here:

BEL

(a) BEL is a UK incorporated and tax resident company. It is part of an international group with a US incorporated head company. BEL was incorporated on 28 November 2002.

(b) BEL prepared statutory accounts for the 13 month period ended 31 December 2003.

(c) BEL's corporation tax period for which the discovery assessment was made was the one month period from 28 November 2003 to 31 December 2003.

The Promissory Note

(d) An inter-company loan facility was entered into on 21 January 2003 between Ball UK Holdings Limited ("BUKH" BEL's parent company) as lender and Ball Company Limited ("BCL") as borrower. The consideration given by BCL in respect of the loan was the repayment of the principal by BCL to BUKH and the issue by BCL to BEL of a loan note ("the Promissory Note").

(e) The Promissory Note was issued by BCL to BEL on 18 December 2003 in the amount of £10,812,449.

BEL's accounts and tax return

(f) BEL's tax return for the period ending 31 December 2003 did not include any reference to the Promissory Note or show its amount as taxable income.

(g) BEL's accounts for the relevant period included:

(a) In the Statement of Recognised Gains and Losses (STRGL) "Unrealised gain on promissory note due from group undertaking 10,812,449"

(b) In the balance sheet "Debtors: Amounts falling due after one year 10,812,449.

(c) At Note 6 (Debtors) "Amounts falling due after one year 10,812,449

(d) At Note 9 (Reserves) "Other recognised gains 10,812,449"

(e) At Note 10 (Reconciliation of movement in shareholders' funds) "On 18 December 2003 the company made an unrealised gain by receiving a promissory note due from fellow group undertaking of £10,812,449".

Discovery Assessment

(h) HMRC issued a discovery assessment to BEL on 12 July 2006 assessing the principal value of the Promissory Note to tax.

(i) PWC appealed against that assessment on behalf of BEL on 1 August 2006.

(j) HMRC set out their analysis of the basis of their assessment by a letter to PWC dated 24 August 2010 stating that the £10,812,449 was taxable income of BEL either under Case VI Schedule D, or s 84(1) Finance Act 1996 or s 786 Income and Corporation Taxes Act 1988 ("ICTA 1988")

(k) PWC requested a review of HMRC's decision on 24 September 2010, including the basis for the discovery assessment.

(l) HMRC confirmed their position by letter on 4 November 2010.

(m) BEL appealed to this tribunal on 2 December 2010. That appeal was stayed behind the decision in *Versteegh Ltd & Ors v HMRC* [2013] UKFTT 642 (TC). In 2015 a UKUT decision in the lead case *Spritebeam Limited* upheld the earlier decision of the FtT that the Promissory Note received by BEL was taxable income.

(n) It was agreed on 27 February 2019 that the question of whether the discovery assessment issued to BEL was valid should be brought before the FtT.

Correspondence with HMRC

(o) HMRC wrote to BCL on 30 September 2005 stating their intention to open an enquiry into BCL's corporation tax returns for the accounting periods ending 27 November 2003 and 31 December 2003.

(p) Colin Hedley of the Ball group responded on 13 October 2005 on paper headed Ball Packaging Europe Limited stating that PWC "who advise me on tax issues" would reply.

(q) PWC wrote to HMRC on 22 November 2005 setting out details of the interest payments made by BCL, including payment of £11,057,888 to BEL and saying

"The interest payable to BEL arose as a consequence of an inter-company loan facility provided by Ball UK Holdings Limited to Ball Company Ltd.... It was repaid by Ball Company Ltd on 18 December 2003 by the issue of the two loan notes to BEL." and "The principal value of one of the loan notes to Ball Europe was £10,812,449 and forms part of the £11,057,888 above".

(r) HMRC wrote to PWC on 15 December 2005 saying

"The only additional point is with respect to the promissory notes claimed as an expense of the loan relationship by virtue of s 84(1)(b) Finance Act 1996. This appears to be in place of interest as the loan is interest free. Obviously I am aware of the fact that the corresponding accounts of the lending company Ball UK Holdings Ltd do not contain a credit in the same period" and made a request to see a copy of the loan agreement and "a copy of the note confirming the conditions of the promise".

(s) PWC provided the requested inter-company loan facility and the loan note (the Promissory Note) issued by BCL to BEL by letter to HMRC on 17 January 2006.

THE LAW

4. It is not disputed that the statutory period for HMRC to open an enquiry into BEL's tax return for the period ending 31 December 2003 was 31 January 2006. No enquiry was opened by HMRC during that period. A discovery assessment was issued on 12 July 2006.

5. The rules which set out the conditions which HMRC must fulfil in order to issue a discovery assessment are set out at Schedule 18 FA 1998, of which the relevant provisions are:

"**Assessment where loss of tax discovered**

41(1) If an officer of Revenue and Customs discovers as regards an accounting period of a company that –

(a) an amount which ought to have been assessed to tax has not been assessed or (b) ..... or (c) .....

he may make an assessment (a "discovery assessment") in the amount or further amount which ought in his opinion to be charged in order to make good to the Crown the loss of tax."

"**Restrictions on power to make discovery assessment**

42(1) The power to make –

(a)a discovery assessment for an accounting period for which the company has delivered a tax return

(b).....

is only exercisable in the circumstances specified in paragraph 43 or 44 and subject to paragraph 45 below"

"**Situation not disclosed by return or related documents**

44(1) A discovery assessment for an accounting period for which the company has delivered a company tax return....., may be made if at the time when an officer of Revenue and Customs –

(a)ceased to be entitled to give a notice of enquiry into the return, or

(b).....

they could not have been reasonably expected, on the basis of the information made available to them before that time, to be aware of the situation mentioned in paragraph 41(1)....

(2)For this purpose information is regarded as made available to an officer of Revenue and Customs if –

(a)it is contained in a relevant return by the company or in documents accompanying any such return, or

(b).....

(c)..... or

(d) it is information the existence of which, and the relevance of which as regards the situation mentioned in paragraph 41(1) –

(i)could reasonably be expected to be inferred by an officer of Revenue and Customs from information falling within paragraphs (a) to (c) above, or

(ii) are notified in writing to an officer of Revenue and Customs by the company or a person acting on its behalf.

(3)In sub-paragraph (2) –

"relevant return" means the company's company tax return for the period in question or either of the two immediately preceding accounting periods"

6. We were also referred to the following authorities:

(a) *Langham v Veltema* [2004] STC 544

(b) *Lansdowne Partners LP v HMRC* [2012] STC 544

(c) *HMRC v Charlton* [2013] STC 866

(d) *Spritebeam Ltd & Othrs v HMRC* [2015] STC 1222

(e) *Sanderson v HMRC* [2016] STC 638

(f) *Beagles v HMRC* [2019] STC 54

(g) *Clark v HMRC* [2020] STC 589

THE EVIDENCE SEEN AND HEARD

Oral evidence

Mr Hedley

7. Mr Hedley was the UK finance director of the Ball group in 2003. His witness statement of 30 September 2019 was taken as read. Mr Hedley was not cross-examined by Ms Murray.

8. Mr Hedley's witness statement dealt with the correspondence between the Ball group companies and the information which had been provided to HMRC about BEL's tax position.

(a) Mr Hedley described his correspondence with HMRC in response to their enquiries into BCL's tax returns, including about the interest payments paid by BCL during the accounting periods ended 27 November 2003 and 31 December 2003.

(b) He explained that he responded to HMRC's questions on Ball Group Europe headed paper, telling HMRC that PWC would be dealing with these queries. HMRC seemed to be asking about the group structure which had been put in place after the Schmalbach-Lubeca group acquisition and this covered all the Ball group companies, including BEL. Mr Hedley said:

> "As such, when responding to Mr Birkett's letter, PWC were representing the group generally, and specifically all the holding companies which had been introduced as part of the Ball acquisition and had participated in the relevant transactions: BCL, BEL and BUKH."

(c) Mr Hedley referred to PWC's letter of 22 November 2003 which referred to BEL as part of the explanation provided to HMRC about the interest payments which were made by BCL:

> "The total interest payable by Ball Company Ltd in the period of account to 31 December 2003 was as follows: Ball Europe Ltd £11,057,888 [...] The interest payable to Ball Europe Ltd arose as a consequence of an inter-company loan facility [...] it was repaid by Ball Company Ltd on 18 December 2003 by [...] the issue of two loan notes to Ball Europe Ltd. The principal value of one of the loan notes to Ball Europe Ltd was £10,812,449 and forms part of the £11,057,888 above."

(d) Mr Hedley also referred to a letter from HMRC to PWC dated 15 December 2005 requesting copies of the Loan Facility Agreement and the Loan Note and a letter from PwC to HMRC dated 17 January 2006 enclosing the requested documents.

(e) Mr Hedley asserted that he instructed PWC to correspond with HMRC on behalf of all relevant Ball companies, including BEL. He believes that HMRC understood at that time that they were corresponding on behalf of all of the group companies.

Mr Chandler – expert accounting evidence

9. Mr Chandler is a partner in KPMG's Accounting Advisory Services Group. We found Mr Chandler to be a clear and helpful expert witness.

10. His expert report of 28 April 2020 stated that the disclosures in the 2003 Financial Statements of BEL indicate that:

(a) BEL received the Promissory Note on 18 December 2003.

(b) BEL recognised a gain from doing so, of an amount equal to the value of the Promissory Note, i.e. £10,812,449.

(c) BEL did not receive the Promissory Note as a "capital contribution" or a distribution from a subsidiary or non-subsidiary investment, (because nothing was recorded in shareholder funds).

(d) The gain relating to the Promissory Note would have been recorded in BEL's profit and loss account but for the gain not being "realised". Because the gain was not a realised gain, it was recorded in BEL's STRGL.

(e) Whether the gain is recorded in the P&L or STRGL does not affect the conclusion that Ball Europe made a gain.

(f) The Promissory Note was received by BEL in exchange for the "disposal" of an "asset" and

(g) That asset was carried at £nil in the balance sheet and was received as a capital contribution.

11. These conclusions could be derived from a combination of the information provided in BEL's accounts and some basic accounting knowledge.

12. BEL's 2003 Financial Statements contain only a narrow set of disclosures and notes to the financial statements. The disclosures and notes relating to the Promissory Note are readily apparent.

13. In response to questions from Ms Murray, Mr Chandler further explained why the £10,812,449 had appeared in the accounts as a recognised but unrealised gain in the STRGL:

(a) The gain was not included in BEL's P&L because in accounting terms it was not "realised" ie it was not cash or nearly cash. The directors of BEL would have come to a decision about whether to treat the gain as realised and the accounting treatment reflected that decision. Once the decision had been made to treat the gain as unrealised, it was a legal requirement for that gain to be taken to reserves and appear in the STRGL.

(b) The relevant question for accounting purposes is not whether something is income or capital, but whether it is a gain and whether that gain should be treated as recognised.

(c) As a gain, it must have derived from something; to work out what "asset" this gain might relate to, a process of elimination would be required; knowing about BEL's activities, it clearly could not relate to any kind of licence, real property or employee rights.

(d) Mr Chandler agreed that there was nothing in BEL's accounts which clarified what the Promissory Note was received in exchange for, or that it represented a payment in lieu of interest.

(e) If it had been a capital contribution, it would have appeared in shareholders' funds rather than the STRGL and it would not appear as a gain in the STRGL.

(f) The sum has increased the assets of BEL and so it appears in the notes to the reconciliation statement.

(g) If the sum had been a gift, it would not have been accounted for as an unrealised gain in the STRGL.

14. As regards what a tax inspector may have been able to deduce from BEL's accounts, Mr Chandler accepted that looking at BEL's P&L would have been the natural starting point for ascertaining its profits, but added that it was basic accounting knowledge that there are lots of gains and losses which appear outside the P&L saying

> "It would be a pretty limited single eye view of life just to look at the P&L to work out the gains that might be taxed in a company"

Correspondence between the parties

15. We were also provided with the following

(a) Correspondence between HMRC and BEL from the notification of the opening of the enquiry into BEL's tax return on 30 September 2005 up to and including HMRC's issuing of the discovery assessment to BEL on to 12 July 2006

(b) Correspondence and notes of telephone conversations between PWC and HMRC on behalf of the Ball group of companies from 15 November 2005 up to and including BEL's appeal notice of 2 December 2010.

(c) HMRC internal notes from 3 May 2006 to 30 August 2006 including notes made by Ms Kerrigan CPT trainee of (i) 17 May 2006, setting out her understanding of the transactions through which BEL acquired the Promissory Note and suggesting the need to issue a discovery assessment and of (ii) 3 July 2006 stating;

> "Whilst these (Ball Europe's statement and computations) show that a gain has not been taxed (and perhaps we should have questioned why not) there wasn't enough information at that stage to suggest that on the face of matters this could be incorrect (We still don't know that is it incorrect!).
> The judgement in Langham v Veltema does I think show that any insufficiencies should be made clear and didn't require "time consuming scrutiny" by HMRC to prevent Para 44 applying.
> I would like to issue a discovery assessment that tax BE on both £10.8m and £214, 208 for 2003. I do have my doubts about being able to include the tax relating to the first loan note but given the amount involved I think that we should not be "letting the opportunity go"".

Tax computation and accounts

16. BEL's CT600 computation and accounts for the short accounting period 28 Nov 2003 to 31 December 2003, Including:

(a) In STRGL "Unrealised gain on promissory note due from group undertaking: 10,812,449"

(b) Balance sheet: "Debtors – amounts falling due after one year:10,812,449. Capital and reserves: profit and loss account £10,812,449.

(c) Note 6 (debtors) "Amounts falling due after one year: 10,812,449"

(d) Note 9 (Reserves) "Other recognised gains:10,812,449"

(e) Note 10 "On 18 December 2003 the company made an unrealised gain by receiving a promissory note due from a fellow group undertaking of £10,812,449".

AGREED MATTERS

17. The burden of proof is on HMRC to demonstrate to the normal civil standard that the conditions for the raising of a discovery assessment were met on 12 July 2006.

18. The gain made on the income from the Promissory Note is properly taxable under Schedule D, Case VI, on the basis of the decision in *Spritebeam*.

19. A discovery was made by HMRC in July 2006.

20. There is no question of that discovery being "stale".

21. The discovery assessment which was issued in July 2006 charged BEL to tax on £11.05 million of "non-trading loan relationship profits under Schedule D case III", including the gain arising from the Promissory Note.

22. The decision in *Beagles* at paragraph 100 sets out the correct and detailed approach to the question of determining what a hypothetical officer may reasonably be expected to know for the purpose of paragraph 44(1)(b) Schedule 18 FA 1998.

HMRC'S ARGUMENTS

Information in the tax return and accounts

23. The critical question is whether a hypothetical officer would have been justified in raising an assessment on BEL as at 31 January 2006 on the information then available to the officer.

24. HMRC's position is that a hypothetical officer could not reasonably have been expected to know that there had been an under-assessment of tax on BEL on the basis of the information provided in BEL's tax return, computation and accounts for the 28 November to 31 December 2003 accounting period

What is the appropriate level of knowledge and skill which should be attributed to the hypothetical officer?

25. In HMRC's view, a hypothetical officer is expected to have knowledge of the law, but not of technical accounting issues.

> (a) He is expected to apply his knowledge of the law to the facts but he should not be attributed expert knowledge of facts, and there must be some basis for the officer's knowledge of the law.
>
> (b) It would require a published decision or at least a technical view within HMRC that a particular legal argument can be run in relation to known facts.
>
> (c) There was no such published decision or technical view in respect of the transaction undertaken by BEL, at least until the decision in *Spritebeam*.
>
> (d) The officer should not be attributed with competence or skill from professional fields other than law.

26. Ms Murray pointed out that there are no authorities which establish that a hypothetical officer has to have attributed to him non-tax expertise, or a case in which expert accounting knowledge has been attributed to a hypothetical officer. In particular *Charlton* is not authority for the proposition that a hypothetical officer should be expected to have any expertise other than tax expertise.

27. The information provided by BEL must be more than would be sufficient to raise an enquiry, it must be sufficient to enable HMRC to make a decision about the taxability of an amount which has not been included in the tax return and so whether to raise an assessment.

> (a) In this situation, in order to decide that an amount of tax which ought to have been assessed had not been assessed a hypothetical officer would have needed to understand technical accounting issues including (i) Why the gain arising from the Promissory Note was not in the P&L and (ii) The reason why the gain was in the STRGL and (iii) The legal analysis which was applied in *Spritebeam*.
>
> (b) To establish the basis of taxability required technical accounting knowledge, as demonstrated by Mr Chandler. This level of technical knowledge cannot be attributed to the hypothetical officer, as stated in *Langham v Veltema* and approved in *Sanderson*.
>
> > "that there is nothing in the Act that obliges a Revenue officer to enquire into a return, for example in a case such as this, to obtain expert

valuation evidence for the purpose of checking the accuracy of a valuation indicated in a return."[32]

The technical basis under which the gain arising from the Promissory Note was taxable under D Case VI was not apparent to the officer. There was nothing in the accounts provided by BEL to HMRC to draw attention to the gain from the Promissory Note, to suggest that it was income or that it was taxable income.

Is this case so complex that the hypothetical officer could not reasonably have been expected to be aware of the insufficiency?

28. This is a "complex case" of the type referred to in *Lansdowne* where it was said that:

> "As the Chancellor points out (at [56]), awareness of an insufficiency does not require resolution of any potential dispute. After all, once an amendment is made, it may turn out after complex debate in a succession of appeals as to the facts or law, that the profits stated were not insufficient. I have dwelt on this point because I wish to leave open the possibility that, even where the taxpayer has disclosed enough factual information, there may be circumstances in which an officer could not reasonably be expected to be aware of an insufficiency by reason of the complexity of the relevant law" [69]

So the hypothetical officer should not reasonably be expected to be aware of the fact that there was an insufficiency of tax at the relevant date. The analysis which the UT adopted in *Spritebeam* to conclude that the gain from the shares (equivalent to the Promissory Note in this case) was taxable under Schedule D Case VI required detailed technical legal analysis, even though the starting point in that case was that the gain was income.

Was the information available sufficient to make the hypothetical officer aware of the actual insufficiency?

29. The circumstances here are unlike the situation in *Charlton*, where HMRC were already aware of the details of the tax avoidance scheme which the taxpayer had entered into.

(a) BEL made no disclosure on its tax return which would have indicated to a hypothetical officer that it had untaxed income or gains. Without that knowledge, an officer could not make an assessment, whatever his level of tax technical expertise.

(b) BEL did not provide, and HMRC did not have, any details of the tax planning which had been entered into by BEL which gave rise to the gain on the Promissory Note. No DOTAS (Disclosure of Tax Avoidance Schemes) disclosure or other detailed disclosure was made by BEL.

(c) By including the gain in the STRGL rather than the P&L, BEL's accounting information suggested that any taxable sum was a capital amount, since it was not presented in the accounts as an income profit. If it had been presented in the P&L the inspector would have identified it as income which had been taken out of the tax computation as non-taxable income and would have recognised that it should have been subject to tax.

Was the information provided sufficient to enable HMRC to make a decision whether to raise an additional assessment?

30. The *Lansdowne* decision sets out the criteria for deciding what is sufficient information for these purposes:

> "The question is whether the taxpayer has provided sufficient information to an officer, with such understanding as he might reasonably be expected to have, to justify the exercise of the power to raise the assessment to make good the insufficiency."[70]

31. In the *Spritebeam* decision the UT relied on two crucial facts to come to its conclusion:

(a) The shares represented consideration for the use of the money lent to the group borrower

(b) The share recipient (in the equivalent position to BEL) was the named beneficiary of a legal obligation to have the shares issued.

32. Unlike the circumstances in *Lansdowne* (in which the officer knew that deductions had been claimed and what those deductions related to), the information provided by BEL in its accounts did not provide information about critical facts which determined the taxability of the sum in question, namely that;

(a) It had arisen from the disposal of a promissory note under which BEL was indebted to a third party (another group company).

(b) The commercial issues surrounding the disposal of the Promissory Note.

The hypothetical officer in this case could not have been aware of these critical facts on 31 January 2006 and even if he or she had been aware of them, they could not reasonably be expected to know that as a consequence as a matter of law BEL was in receipt of taxable income.

33. The information provided by BEL in its tax return, computations and accounts for 28 November to 31 December 2003 was not enough to ensure that a hypothetical officer could have been aware of an insufficiency of tax.

Information provided from correspondence with other group members

34. HMRC do not accept that information provided by other Ball group members can be taken account of to decide what information the hypothetical officer had available on 31 January 2006:

(a) This additional correspondence was not provided by BEL so should be disregarded.

(b) Even if the Appellants believed that their agent (PWC) was dealing with HMRC queries on behalf of all the group companies, that is not how HMRC operates or how it operated in this case.

(c) The mechanisms for opening enquiries and assessments operate on an entity by entity basis. Information should not be provided for an entity other than that for which an enquiry had been opened. HMRC and PWC both operated on the basis of this understanding.

(d) The correspondence and telephone conversations referred to by the Appellant;

(a) Letters of 30 September 2005, 15 and 22 November 2005, 15 December and 17 January 2006 and phone conversation of 24 July 2006,

(b) Note (Susan Kerrigan) of 3 July 2006,

(c) Telephone conversation between Mr Birkett of HMRC and PWC of 15 November 2005,

Do not suggest that HMRC was receiving information other than on behalf of the entities for which enquiries were being made in November 2005 and January 2006.

(e) All of PWC's correspondence with HMRC in respect of BCL is specifically headed with BCL's name and reference. In fact PWC specifically refused to respond to questions about BEL in their letter of 3 May 2006, saying:

> "We note that you have asked about the accounting entries in Ball UK Holdings Ltd and Ball Europe Ltd in respect of the enquiry into Ball Company Ltd. We consider that this is not relevant to the tax affairs of Ball Company Ltd and would suggest that these questions are addressed to the relevant companies."

(f) Even if it can be argued that this information was provided on behalf of BEL, the relevant information about the Promissory Note and the loan were not provided until 17 January 2006. The hypothetical officer has to be given sufficient time to consider the information before the end of the enquiry period on 31 January 2006. The two week time period here was not sufficient time to consider the relevant information.

BEL'S ARGUMENTS

Information in tax returns and accounts

35. BEL argues that the hypothetical officer had enough information from BEL's tax return, computation and accounts to reasonably have been expected to be aware of an insufficiency of tax.

36. The only real issue here is not whether a gain has been made or whether that gain has not suffered tax, this is evident from BEL's tax return and accounts, but whether a hypothetical officer should have been aware that this was a taxable gain.

What is the appropriate level of knowledge and skill which should be attributed to the hypothetical officer?

37. The hypothetical officer must be assumed to have sufficient knowledge to enable him or her to deal with the matters with which they are charged, including reviewing company accounts as part of dealing with a company's tax returns. (*Charlton* [65]):

> "Our conclusion on this point, therefore, is that s 29(5) does not require the hypothetical officer to be given the characteristics of an officer of general competence, knowledge or skill only. The officer must be assumed to have such level of knowledge and understanding that would reasonably be expected in an officer considering the particular information provided by the taxpayer. Whilst leaving open the exceptional case where the complexity of the law itself might lead to a conclusion that an officer could not reasonably be expected to be aware of an insufficiency, the test should not be constrained by reference to any perceived lack of specialist knowledge in any section of HMRC officers. What is reasonable for an officer to be aware of will depend on a range of factors affecting the adequacy of the information made available, including

complexity. But reasonableness falls to be tested, not by reference to a living embodiment of the hypothetical officer, with assumed characteristics at a typical or average level, but by reference to the circumstances of the particular case"

38. In this case the hypothetical officer must be assumed to have a reasonable understanding of accounting principles and practice. The level of accounting knowledge required in order to understand that an amount in BEL's accounts had not been subject to tax is basic (as explained by Mr Chandler) and requires only an understanding that:

(a) A gain has been received.

(b) That gain has not been taxed.

(c) That gain does not relate to a financial asset.

(d) With the result that the gain should be taxed under Schedule D case VI.

39. The fact that the gain appeared in the STRGL rather than BEL's P&L should not have been taken to indicate that it was either not income or not taxable.

***Is this case so complex that the hypothetical officer could not reasonably have been expected to be aware of the insufficiency*?**

40. BEL's position is that this is not one of the "exceptional" cases, referred to in *Charlton* which are so complex that it is not reasonable to expect a hypothetical officer to be aware of an insufficiency of tax.

41. The references to the *Spritebeam* decision and the fact that it was appealed to the UT do not indicate that this is a complex case, but is more akin to the situation in *Lansdowne* where Moses LJ stated:

"The legal points were not complex or difficult. As the Chancellor points out (at [56]), awareness of an insufficiency does not require resolution of any potential dispute. After all, once an amendment is made, it may turn out after complex debate in a succession of appeals as to the facts or law, that the profits stated were not insufficient. "[69]

42. The fact that in *Spritebeam* there was a lengthy dispute about the taxpayer's liability which entailed an appeal to the UT indicates disagreement, not necessarily complexity.

43. In any event, the discovery assessment was issued to BEL many years before the *Spritebeam* decision was published so cannot have depended on the technical analysis in that case.

***Was the information available sufficient to make the hypothetical officer aware of the actual insufficiency*?**

44. The "insufficiency" does not have to be disclosed on the face of the tax return itself. The test is whether the hypothetical officer could have deduced that there was an insufficiency of tax from the information made available to him, by applying his knowledge of the law and accounting principles and practice. See *Sanderson*:

"The decision in Lansdowne confirmed that the officer was not required to resolve (or even be able to assess) every question of law (particularly in complex cases) but that where, as Moses LJ expressed it, the points were not complex or difficult he was required to apply his knowledge of the law to the facts disclosed and to form a view as to whether an insufficiency existed. That is a matter of judgment rather than the

application of any particular standard of proof. And the reference to the officer needing to reach a conclusion which justified the making of a discovery assessment has to be read in that context." [23]

45. On this basis the reasons given for the assessment in the discovery assessment are not relevant to the analysis; the only issue is whether an insufficiency of tax has been discovered. (The parties now agree that Schedule D III is not the correct head of charge for the gain generated on the Promissory Note).

46. There are three potential heads of charge which could have been relevant to this gain:

(a) Income – D case III

(b) Income – D case VI

(c) Capital – under the wide scope of s 21 TCGA 1992.

47. The information provided to HMRC was sufficient to form the basis for an assessment under any one of these heads of charge. It is not necessary for the hypothetical officer to be aware of the precise reasons why this gain is taxable, or the specific head under which that tax charge may arise, he or she simply needs to be aware that the gain is taxable.

Was the information provided sufficient to enable HMRC to make a decision whether to raise an additional assessment?

48. It is not necessary for the hypothetical inspector to understand all the technical arguments or the basis on which the tax treatment of the amount could be challenged. All that is required is that the hypothetical officer applies his or her mind to the available information and is able to form a view about whether there is an insufficiency of tax. (see *Clark* and *Lansdowne*)

> "In the present case the commissioners asked whether HMRC had sufficient information to make a decision whether to raise an additional assessment. That seems to me to be the right test" *Lansdowne* [48]

The question is whether the hypothetical officer had sufficient information to make a decision to raise an assessment. How that question is answered is a question of judgment not a standard of proof. (See *Sanderson*)

49. HMRC's reference to *Spritebeam* and the analysis of the UT explaining the tax treatment of a similar transaction is misconceived.

Information provided from correspondence with other group members

50. BEL argues that information provided to HMRC, particularly in the letters dated 22 November 2006 and 17 January 2006 should be treated as made available on behalf of BEL because**:**

(a) Both Mr Hedley and HMRC understood that when they were dealing with HMRC they were dealing with the affairs of the Ball group, including BEL.

(b) It is clear from correspondence between Mr Hedley and PWC and PWC and HMRC that this was their common understanding. HMRC are confusing the "prompt" for the request of the information and the basis on which the provider of the information (PWC) is acting, which was on behalf of all the Ball group companies.

(c) The information provided to HMRC by letters of 22 November 2005 (containing information about inter-company loan agreement and the Promissory Note issued to represent interest on that loan agreement) and 17 January 2006 (containing reference to the terms of the loan agreement) was provided on behalf of BEL as well as other group companies and should be taken into account under paragraph 44(2)(d)(ii).

(d) The decision in *Lansdowne* is analogous; in that case HMRC used information provided by the general partner in its review of the individual partners' tax returns.

DECISION

Findings of fact

51. The entries and notes in BEL's computation and accounts indicated a large sum which had not been included in BEL's tax return.

52. The notes to BEL's accounts indicated that this sum derived from an intra-group transaction concerned with a group debt.

53. The technical analysis leading to the decision in *Spritebeam* would not have been available to the hypothetical officer at any time before the discovery assessment was issued.

Information provided in tax return and accounts of BEL

54. Would a hypothetical officer have reasonably been expected, on the basis of this information, to be aware that an amount which ought to have been assessed to tax has not been assessed?

55. We have started by asking, what is an "insufficiency" of tax for these purposes. We have adopted Ms Shaw's definition: something which is within the tax net which has not been subject to any, or the correct amount of tax. That could arise because profits have been charged at the wrong rate, the level of profits have been misstated, deductions have been wrongly claimed, the valuation of assets has been miscalculated or, as here, because a gain has not been brought into tax at all.

56. It is worth noting at this stage that none of the authorities to which we were referred concern a situation in which a gain stated in the company's accounts has simply not been included in the company's tax return.

57. The starting question is: Would the hypothetical officer have been aware that there was an amount in the accounts which had not been brought into tax? We think that the answer to this must be yes:

(a) A recognised but unrealised gain is included in BEL's accounts provided to HMRC, despite not being in the P&L, it is very clearly stated in the STRGL.

(b) It is clear that this amount is not included in BEL's tax return; there is nothing in the tax return of this quantity.

58. Given that the amount in question, (£10,812,449) had not been subject to tax at all, if the hypothetical officer can identify a head of charge, there is clearly an insufficiency of tax.

59. In our view, the critical question is whether a hypothetical officer should reasonably have been aware that this amount ought to have been brought into tax? To answer that

question, we have followed the criteria set out in *Beagles*. The relevant criteria set out at paragraph 100 are:

> 1.The hypothetical officer is expected to apply his knowledge of the law to the facts disclosed to form a view as to whether or not an insufficiency exists. The hypothetical officer will apply the appropriate level of knowledge and skill to the information that is treated as being available before the level of awareness is tested. The test does not require that the actual insufficiency is identified on the face of the return.
>
> 2. The question of the knowledge of the hypothetical officer cuts both ways. He or she is not expected to resolve every question of law particularly in complex cases. In some cases, it may be that the law is so complex that the inspector could not reasonably have been expected to be aware of the insufficiency.
>
> 3. The hypothetical officer must be aware of the actual insufficiency from the information that is treated as available. The information need not be sufficient to enable HMRC to prove its case but it must be more than would prompt the hypothetical officer to raise an enquiry.
>
> 4. The level of awareness is a question of judgment not a particular standard of proof The information made available must 'justify' raising the additional assessment or be sufficient to enable HMRC to make a decision whether to raise an additional assessment.

***What is the appropriate level of knowledge and skill which should be attributed to our hypothetical office*r?**

60. Taking the test as enunciated in *Charlton*, "The officer must be assumed to have such level of knowledge and understanding that would reasonably be expected in an officer considering the particular information provided by the taxpayer" our view is that given that the "particular information provided by the taxpayer" in this instance included its accounts, the officer must be taken to have at least a basic understanding of accounting. We reject HMRC's contentions that nothing other than a knowledge of law can be expected from a hypothetical officer in these circumstances.

61. In these circumstances the "appropriate level of knowledge and skill" of our hypothetical officer must include accounting knowledge because:

(a) Accounts make up part of tax return material for all UK companies

(b) Accounting and legal issues are not discrete in the tax code, especially for companies who since 1996 have been taxable on debt by reference to their accounting treatment (through the tax rules applying to loan relationships). We do not accept HMRC's suggestion that a hypothetical officer should only be assumed to understand tax law. This is a false dichotomy by 2005, and arguably even before the move to tax companies by reference to their accounts in the mid 1990's, accounting knowledge has always over lapped with tax law.

(c) Dealing with large UK group companies, our hypothetical officer should appreciate standard inter-group financing arrangements at the very least.

(d) Authorities such as *Langham v Veltema* can easily be distinguished since the specialist information which was obtained in that case (property valuation) was clearly outside the scope of the type of core knowledge and expertise which could be expected of a tax inspector.

62. We then have to consider, assuming that our hypothetical officer has an appropriate basic level of accounting knowledge, would that have been sufficient to allow him or her to recognise that tax had been under-assessed on the gain recorded in BEL's STRGL.

63. Following Mr Chandler's analysis of the accounting steps required to properly analyse the unrealised gain in BEL's STRGL, we agree that only basic accounting knowledge and knowledge of tax law would be required:

(a) To recognise that not all taxable income is included in a company's P&L.

(b) To recognise that something which is in the "capital" or "reserves" section of the company's accounts may still be taxable as income.

(c) To recognise that if something is not income, but is a gain, it is likely to be taxed as "derived from an asset" under TCGA rules in the UK, which have a wide scope. This is basic tax law.

(d) To understand that Schedule D case VI is a "catch all" provision which could apply if no other head applied.

64. If this reasoning had been applied by our hypothetical officer, it must have indicated at the very least the need for a more detailed consideration of whether the recognised but unrealised gain in the STRGL ought to be subject to tax and several potential heads of taxation.

65. Mr Chandler suggested that it was also clear for accounting purposes that this gain did not derive from a financial asset, because of its lack of base cost. We are less certain that this is basic accounting knowledge. So, if we stop here with what our hypothetical officer could work out. Is this enough?

66. For the reasons set out below, our view is that this is enough information for our hypothetical officer to reasonably have been expected to be aware that there was an insufficiency of tax, despite the fact that this gain appeared neither in BEL's tax return nor its P&L.

Is this case so complex that the hypothetical officer could not reasonably have been expected to be aware of the insufficiency?

67. The parties disagreed over whether the transaction in this instance should be treated as a "complex case". Cases can be complex because they relate to complex facts or because they relate to complex areas of tax law, or, in some instances both. HMRC argued that this case must be complex because it took lengthy debate as far as the UT in *Spritebeam* to determine the correct tax treatment of a similar sum.

68. In our view, the technical arguments which were utilised in *Spritebeam* demonstrated that a multitude of technical arguments could be deployed in order to attempt to argue that a gain of this nature was not taxable. However, the question of whether a large recognised but unrealised gain recorded in a company's accounts arising from a debt related transaction with

a member of the same UK group ought to be subject to tax does not seem to us to be a particularly complex question. It depends on a basic understanding of the loan relationship code, that all recognised gains appearing in a taxpayer's accounts are taxable, or a basic understanding of the capital gains tax legislation, that gains derived from assets are chargeable gains.

69. Most of the authorities in this area demonstrate a less straightforward analysis in order to conclude that an amount has been under-assessed to tax. They concern deductions which have been claimed reducing the level of tax stated to be payable by the given company, either because of the allowability of the deductions (*Lansdowne* and *Clark*), the tax free character of a financial instrument (*Beagles*), or the creation of capital losses (*Charlton* and *Sanderson*). In all of these cases a hypothetical officer would have had to make some deductions about the proper availability of losses in order to ascertain whether tax had been under-assessed.

70. That is simply not the case here; the only thing which a hypothetical officer had to do was to decide whether a large amount which appeared in BEL's STRGL as a recognised gain with reference to the acquisition of a debt instrument from a group company should be taxable. In our view it is much more straightforward to identify a sum stated in the accounts and decide whether it is taxable or not as is required here, than to consider the basis on which certain deductions should be available.

***Was the information available sufficient to make the hypothetical officer aware of the actual insufficiency*?**

71. The level of awareness required of our hypothetical officer is a matter of judgment as per *Sanderson*. In our view, it must have been clear that the £10,812,449 ought to be chargeable under at least one of the potential heads of charge identified. This would be enough information to enable our hypothetical officer to have decided to raise an assessment either under one of cases DIII or DVI or as a capital gain, even if at this stage he or she could not identify which of those was the more technically correct basis for a tax charge.

72. HMRC attempted to persuade us that in order to make his or her judgment about an insufficiency of tax the hypothetical officer would have needed to understand the legal and commercial details concerning the Promissory Note issuance. We disagree. Those details, if anything, were relevant to arguments made by the taxpayer about why the gain should not be taxable. The much more straightforward information available to the hypothetical officer; the existence of a recognised but unrealised gain arising from a debt transaction in BEL's STRGL should have been sufficient to make a hypothetical officer aware of an insufficiency of tax.

Was the information provided sufficient to enable HMRC to make a decision whether to raise an additional assessment?

73. On the basis of the authorities, our view is that even if we stop at this point in the analysis, our hypothetical officer does have enough information to understand that there was an insufficiency of tax and enough information to decide whether to raise an assessment.

(a) We agree with the Appellant that the hypothetical officer does not need to understand the detailed specifics of the head of charge.

(b) The hypothetical officer does not have to resolve every question of law, particularly in complex cases.

(c) The information provided has to be enough to allow the hypothetical officer to make a decision that an amount is taxable, but that decision does not need to be a completely correct or absolutely certain technical analysis.

74. We have considered the difference, stressed by HMRC and referred to in *Beagles*, between having sufficient information to raise an enquiry and having sufficient information to make an assessment. In our view, if it is possible to identify a specific head of charge which could be applied to a profit or gain, that is sufficient for an officer to make an assessment, not merely raise an enquiry.

75. In this case a large recognised gain had been recorded in BEL's STRGL which related to an intra-group debt instrument and had not been charged to tax, that is enough information to allow a hypothetical officer to make a decision about whether to raise an assessment on at least one of three relatively straightforward heads of charge.

Conclusion on the Beagles tests:

76. Our conclusion on each of these points suggests that our hypothetical officer should have had enough information at the relevant time to enable him to decide whether to raise an additional assessment.

77. We have asked ourselves two additional questions in order to test this conclusion:

Would it have been reasonable for the hypothetical officer to conclude that the £10,812,449 should not be subject to tax?

78. It must be a logical corollary of HMRC's conclusion that it would have been reasonable to expect the hypothetical officer to decide that this amount ought not to be subject to tax. We have asked ourselves:

(i) What analysis would have been done in order to decide that this amount was outside any potential head of charge?

(ii) What could its character be such that it was a tax nothing?

79. Our conclusion is that the analysis which would have been required in order to conclude that this amount ought not to be subject to tax (or that sufficient tax of nil had been paid) is significantly more difficult than the analysis which leads to a conclusion that the sum ought to be taxable. The only straightforward basis on which this could have been concluded would be on the (erroneous) basis that because the amount did not appear in the company's P&L it was automatically outside the UK tax net. As we have explained above, we do not consider that any reasonable (or competent) officer could have come to that conclusion, even if he or she only understood some basic capital gains tax law and the fundamentals of the loan relationship code.

What other information could have been provided to HMRC at the relevant time?

80. Finally, we have considered the question from the perspective of the purpose of the discovery provisions as explained by Chadwick LJ in *Langham v Veltema*:

> "It seems to me that the key to the scheme is that the Inspector is to be shut out from making a discovery assessment under the section only when the taxpayer or his representatives, in making an honest and accurate return or in responding to a s 9A enquiry, have clearly alerted him to the insufficiency of the assessment, not where the Inspector may have some other information, not normally part of his checks, that may put the sufficiency of the assessment in question" [36]

81. In the Appellant's situation, what additional information could or should the taxpayer have provided to HMRC at the relevant time ?

(a) This was not a situation in which the DOTAS rules were in point. HMRC stressed that no information was included in the "white space" of the tax return, but aside from providing the documents which related to the transaction, which would not be usual as part of a tax return, it is hard to understand what other information could have been provided to HMRC to make the insufficiency of tax clear.

(b) HMRC seemed to suggest that the profits should have appeared in the P&L, but we were told by Mr Chandler that it was a decision of the directors, made in accordance with the law and accounting practice, that since this gain was unrealised, it should be in the STRGL not the P&L.

Conclusion

82. This analysis supports our conclusion that our hypothetical officer, even on the basis only of the information in BEL's tax return, computation and accounts, should reasonably be expected to have been aware that there was an insufficiency of tax in BEL's tax return for the November 28 to 31 December 2003 accounting period.

The other information provided to HMRC

83. Having decided that it was reasonable for a hypothetical officer to have been aware of an insufficiency of tax in BEL's tax return on the basis of its CT600 tax computation and accounts, we do not need to consider what other information could be treated as available to HMRC.

84. For completeness, our conclusion on this point would be that the other information provided (about the loan note, (by letter of 22 November 2005) and the relevant loan documents (by letter of 17 January 2006)) could not be treated as provided to HMRC by BEL for these purposes.

85. We have concluded this because:

(a) The provisions of s44(2)(d)(ii) are very specific, as one would expect them to be, referring to "documents, accounts or information produced or provided **by the company** to an officer of HMRC for the purposes of an enquiry into any such return"

(b) We agree with HMRC that aside from some very specific circumstances, UK tax law, including the law relating to enquiries and assessments, operates on an entity by entity basis. We do not accept BEL's suggestion that *Lansdowne* provides a precedent for relying on information provided in a different capacity;

that decision concerns the relationship between partners in a partnership the legal analysis of which is quite different than companies within a group.

(c) The test is the basis on which information has been made available to HMRC, in our view this is an objective test. The fact that Mr Hedley and/or PWC may have believed that they were providing information on a group basis is not relevant.

(d) We saw no evidence, other than Mr Hedley's assertions, that the information was provided to HMRC on behalf of BEL.

DECISION

86. We allow the Appellant's appeal against HMRC's discovery assessment of 12 July 2006.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

87. 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.

RACHEL SHORT

TRIBUNAL JUDGE

Release date: 28 JANUARY 2021