Neutral Citation: [2023] UKFTT 722 (TC)

Case Number: TC 08912

FIRST-TIER TRIBUNAL
TAX CHAMBER

By remote video hearing

Appeal reference: TC/2018/06774

PENALTY – Schedule 24 Finance Act 2007 – Employee Benefit Trust ('EBT') Clavis Scheme whereby EBT contributions made via a service provider – allocations to sub-trusts for loans to be advanced to directors – Scheme ineffective to avoid income tax and national insurance on contributions into sub-trusts following Rangers *– inaccuracies in returns for omission of PAYE and NICs on loans made via the sub-trusts – whether inaccuracies 'careless' due to failure to take reasonable care – the nexus for a 'careless' inaccuracy for Sch 24 purposes distinguished from 'causation' have derived from the repealed s 95 TMA penalty regime – whether inaccuracy in relation to the last tranche 'deliberate' – appeal dismissed*

Heard on: 10-12 October 2022
10-11 November 2022
& 28 February 2023
Judgment date: 18 August 2023

Before

TRIBUNAL JUDGE HEIDI POON
MOHAMMED FAROOQ

Between

DELPHI DERIVATIVES LIMITED

Appellant

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Michael Sherry, Ximena Montes Manzano, of counsel, instructed by Reynolds Porter Chamberlain LLP

For the Respondents: Sadiya Choudhury, of counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

The hearing was held in private on HMCTS platform.

DECISION

INTRODUCTION

1. The appellant, Delphi Derivatives Limited ('**Delphi**' or the '**Company**') appeals against two penalty assessments issued by the respondents ('**HMRC**'), which are pursuant to Schedule 24 to the Finance Act 2007 ('**Sch 24'**), and are respective of:

    (1) Year ended 5 April 2009 in the sum of £525,484.99 (the '**first penalty**'); and

    (2) Year ended 5 April 2010 in the sum of £1,046,775.17 (the '**second penalty**').

2. The penalty assessments were both issued on 23 March 2018 and in relation to Delphi's Pay As You Earn returns on form P35 (the '**P35 returns**') submitted for the two tax years, which HMRC found to have contained a 'careless' inaccuracy in the 2008-09 return, and a 'deliberate' inaccuracy in the 2009-10 return. The errors in the P35 returns were related to Delphi's participation in a 'tax planning' scheme (the '**Scheme**').

3. The total quantum of penalties under appeal as concerns both tax years is £1,572,260.16. There is no dispute between the parties on the quantification of Potential Lost Revenue ('**PLR**') on which the penalty assessments were based.

EVIDENCE

4. The parties produced a joint bundle of documents of 2,035 pages, and called the following witnesses, who appeared in the order of:

    (1) Officer Nathan Barraclough for HMRC;

    (2) Mr Peter Tucker for the appellant;

    (3) Mr Mark Langran for the appellant.

5. The Tribunal heard witness evidence over two diets of sitting. The first diet in October 2022 covered the parties' opening submissions, followed by the evidence session of Officer Barraclough (concluded), and of Mr Tucker (part-heard). The second diet in November 2022 concluded the evidence of Mr Tucker and Mr Langran.

6. Officer Barraclough is the decision maker of the penalty assessments, and his evidence covered in the main the process which led to his views that the inaccuracies were to be assessed respectively as 'careless' and 'deliberate'. We find Officer Barraclough a credible witness, and accept his evidence as to matters of fact.

7. Mr Tucker is a tax partner at Dickinsons Chartered Accountants, which acts for Delphi in relation to its accountancy and tax matters. Mr Tucker was instructed by Delphi to review the Scheme. Mr Langran has been a director of Delphi since July 2001, and is the Managing Director and majority shareholder. We have no issue with the credibility of Mr Tucker and Mr Langran, and we find both to be co-operative in answering questions put to them in cross-examination and by the Tribunal. Aspects of their oral testimony inevitably involved recall and reconstruction of what happened some 14 years ago, and of the factors which might have predominated in the various decisions taken at different junctures. In areas which represent the pivotal aspects of the evidence for determining the appeal, we have not taken their evidence at face value, and have corroborated their testimonies with primary facts ascertainable from contemporaneous records, and on known and probable facts and inferences drawn therefrom.

HEARING IN PRIVATE

8. By application of 17 July 2019, HMRC applied to the Tribunal for the hearing to be in private, on the ground that the Scheme used by Delphi was the subject matter of a criminal investigation by HMRC. The criminal investigation was into the designers and promoters of the Scheme (and not into Delphi), but it is considered that there was 'a close link' between

Delphi and the promoters of the Scheme, given that Delphi discussed the scheme directly with the promoters without an intermediary.

9. The ground of application for the hearing to be in private is that the civil case is likely to use evidence that is considered sensitive in light of a pending criminal prosecution. If this evidence is tested in open court, then it will risk aspects of the criminal prosecution against third parties not subject to this civil action.

10. The Tribunal (Judge Poole) granted the application on 29 July 2019, but 'limited in time so that it only applies until the conclusion of any related criminal proceedings', with direction:

> 'HMRC are directed to update the Tribunal, at intervals, of not less than three months, on the current status of such proceedings. As and when the risk of prejudice has passed, any decision of the Tribunal on this appeal is to be published in the usual way.'

11. By letter dated 7 October 2022, Ms Emily Bridges, as instructing litigator for HMRC, updated the Tribunal on the 'current status' of the criminal proceedings. By that stage, HMRC were no longer a participant in the criminal investigation. HMRC's decision to leave the team conducting the criminal investigation, however, had led to a judicial review claim served on HMRC. The judicial review claim was brought by one of the directors of Clavis on 29 September 2022 with the ground being 'that investigation team having been exposed to privileged material in the course of an unlawful sift and examination of digital material'.

12. The alleged 'unlawful sift and examination of digital material' is a reference to the procedure and subsequent examination of the digital material seized from Clavis' premises. The claimant has not applied for: (a) an order for the return of any documents forming part of the seized digital material, or (b) for any interim relief preventing HMRC from retaining and using any of those documents in relation to the ongoing investigation into the directors. According to HMRC, the claimant 'does not even ask for the material to be returned to him if he succeeds in his claim provided HMRC make an application under [section 59 of the Criminal Justice and Police Act 2001] allowing them to retain it'.

13. HMRC have not sought to adjourn the hearing since no application for interim relief has accompanied the judicial review claim to prevent the use of the documents pending the outcome of the claim. In terms of the timing of the judicial review claim, it was brought over six years after the searches were carried out and shortly before the scheduled hearing. Although the original ground for the application of the hearing to be in private has changed, the hearing proceeded on the basis that it would be in private due to the judicial review claim served on the respondents, which remains extant at the time of the third diet of sitting on 28 February 2023.

14. With the hearing being in private, there was no official recording of the proceedings. The parties had arranged for the attendance of a stenographer to cover the evidence sessions in October and November of 2022, and the transcript was made available to the Tribunal. Parties confirmed to the Tribunal at the third diet of hearing that the dispositive Decision can be published without any redaction.

WRITTEN SUBMISSIONS

15. With the parties' agreement, the Tribunal directed for closing submissions to be furnished sequentially in writing after the conclusion of evidence. The proceedings resumed on 28 February 2023 for parties' closing submissions, with the Tribunal having the benefit of reading the parties' detailed written submissions beforehand.

RELEVANT LEGISLATION

Schedule 24 to FA 2007

16. The appeal is concerned with the penalty regime under Schedule 24 to FA 2007, entitled 'Error in taxpayer's document'. The provisions relevant to this appeal are the following:

(1) The assessments under appeal are raised pursuant to paragraph 1, which states:

> '(1) A penalty is payable by a person (P) where –
>
> (a) P gives HMRC a document of a kind listed in the Table below, and
>
> (b) Conditions 1 and 2 are satisfied.
>
> (2) Condition 1 is that the document contains an inaccuracy which amounts to, or leads to –
>
> (a) an understatement of a liability to tax,
>
> (b) a false or inflated statement of a loss, or
>
> (c) a false or inflated claim to repayment of tax.
>
> (3) Condition 2 is that the inaccuracy was careless (within the meaning of paragraph 3) or deliberate on P's part.
>
> (4) Where a document contains more than one inaccuracy, a penalty is payable for each inaccuracy.'

(2) Paragraph 3 defines the 'Degrees of culpability', whereby:

> '3(1) For the purposes of a penalty under paragraph 1, inaccuracy in a document given by P to HMRC is –
>
> (a) "careless" if the inaccuracy is due to failure by P to take reasonable care,
>
> (b) "deliberate but not concealed" if the inaccuracy is deliberate on P's part but P does not make arrangements to conceal it, […].'

(3) Paragraph 4 provides for the standard amount of penalty imposable as a percentage of the potential lost revenue ('PLR'): (a) 30% of PLR for careless action; (b) 70% of PLR for deliberate and not concealed action; and (c) 100% for deliberate and concealed action.

(4) Paragraph 5 defines PLR as the additional amount due or payable in respect of tax as a result of correcting the inaccuracy or assessment.

(5) In terms of penalty mitigation, paragraph 9 provides for reductions for disclosure in terms of 'telling HMRC about it', 'giving HMRC reasonable help in quantifying the inaccuracy' and 'allowing HMRC access to records for the purpose of ensuring that the inaccuracy' is fully corrected. The 'quality' of disclosure includes 'timing, nature and extent': sub-para 9(3).

(6) Paragraph 10 sets the 'standard percentage' for a penalty imposable according to the degrees of culpability, and the maximum and minimum penalty range (after allowing for mitigation) according to whether the disclosure is 'prompted' or 'unprompted'.

(7) Paragraph 11 provides HMRC with the discretionary power to reduce a penalty because of 'special circumstances'.

(8) Paragraph 13 provides for the procedural aspects for raising a valid penalty:

> '(1) Where a person becomes liable for a penalty under paragraph 1 … HMRC shall –
>
> (a) assess the penalty,
>
> (b) notify the person, and
>
> (c) state in the notice a tax period in respect of which the penalty is assessed
>
> [...]

(3) An assessment of a penalty under paragraph 1 … must be made before the end of the period of 12 months beginning with –

(a) the end of the appeal period for the decision correcting the inaccuracy, or

(b) if there is no assessment to the tax concerned within paragraph (a), the date on which the inaccuracy is corrected.'

(9) Paragraph 14 provides that 'HMRC may suspend all or part of a penalty for careless inaccuracy under paragraph 1 by notice in writing to P' by setting suspensive conditions.

(10) Paragraph 15 provides 'A person may appeal against a decision of HMRC that:

(a) a penalty is payable by the person: sub-para 15(1).

(b) as to the amount of a penalty payable by the person sub-para 15(2).;

(c) not to suspend a penalty payable by the person sub-para 15(3);

(d) setting conditions of suspension of a penalty payable by the person sub-para 15(4).

(11) The Tribunal's jurisdiction on an appeal, so far as relevant, is set out at para 17:

'(1) On an appeal under paragraph 15(1) the tribunal may affirm or cancel HMRC's decision.

(2) On an appeal under paragraph 15(2) the tribunal may –

(a) affirm HMRC's decision, or

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

(3) If the tribunal substitutes its decision for HMRC's, the tribunal may rely on paragraph 11 –

(a) to the same extent as HMRC (which may mean applying the same percentage as HMRC to a different starting point), or

(b) to a different extent, but only if the tribunal thinks that HMRC's decision in respect of the application of paragraph 11 was flawed.'

(12) Paragraph 18 (under Part 4 for Miscellaneous) provides for the extent P is to be assessed for culpability where agency is involved. The relevant sub-paragraphs are:

AGENCY

18(1) P is liable under paragraph 1(1)(a) where a document which contains a careless inaccuracy (within the meaning of paragraph 3) is given to HMRC on P's behalf.

[…].

18(3) Despite sub-paragraphs (1) and (2), P is not liable to a penalty under paragraph 1 or 2 in respect of anything done or omitted by P's agent where P satisfies HMRC that P took reasonable care to avoid inaccuracy (in relation to paragraph 1) or unreasonable failure (in relation to paragraph 2) […].

Section 1290 of Corporation Tax Act 2009 (CTA 2009)

17. The provisions for a corporation tax deduction for contributions into EBTs as enacted at the relevant time under s 1290 of CTA 2009 stated as follows:

1290. Employee benefit contributions

(1) This section applies if, in calculating for corporation tax purposes the profits of a company ("the employer") of a period of account, a deduction would otherwise be allowable for the period in respect of employee benefit contributions made or to be made (but see subsection (4)).

(2) No deduction is allowed for the contributions for the period except so far as –

(a) qualifying benefits are provided, or qualifying expenses are paid, out of the contributions during the period or within 9 months from the end of it, or

(b) if the making of the contributions is itself the provision of qualifying benefits, the contributions are made during the period or within 9 months from the end of it.

(3) An amount disallowed under subsection (2) is allowed as a deduction for a subsequent period of account so far as –

(a) qualifying benefits are provided out of the contributions before the end of the subsequent period, or

(b) if the making of the contributions is itself the provision of qualifying benefits, the contributions are made before the end of the subsequent period.

(4) This section does not apply to any deduction that is allowable –

(a) for anything given as consideration for goods or services provided in the course of a trade or profession, …'

THE FACTS

Background

18. Mr Langran has a background in metal trading, and he started with Amalgamated Metal Corporation in physical trading of metals. The Corporation was forced to close after incurring loss of some £27m during the tin crisis in 1987. Instead of physical metal trading, Mr Langran went into trading in futures in 1988. Delphi was incorporated on 12 July 2001, with its principal trade was to broker and trade futures and options on the London Metal Exchange.

19. Mr Langran was the Managing Director and majority shareholder at the relevant time. The other two directors were James Kelland and Bruce Martin, and all three directors were involved in the day-to-day running of the business. There were only two other employees in the business (and around six employees at the relevant time).

20. At the hearing, Mr Langran informed the Tribunal that Delphi went into voluntary liquidation in June 2022.

Entities and personnel

21. The entities and personnel playing a role in the implementation of the Scheme are:

(1) Clavis Tax Solutions Limited ('**Clavis**'), the creator and promoter of the Scheme;

(2) Herald Employment and Recruitment Services Limited, trading as Herald Resource ('**Herald**'), a human resources company based in Jersey;

(3) Mark Langran ('**Langran**'), director of Delphi, and beneficiary of the Scheme;

(4) James Kelland ('**Kelland**'), director of Delphi, and beneficiary of the Scheme;

(5) Bruce Martin ('**Martin**'), director of Delphi, and beneficiary of the Scheme;

(6) John Forbes of Forbes Accountants ('**Forbes**'), introducer of the Scheme;

(7) Peter Tucker FCA CTA TEP ('**Tucker**'), partner of Dickinsons Chartered Accountants ('**Dickinsons**').

The Scheme in outline

The tax advantage

22. The Scheme as created and marketed by Clavis with an intention to obtain a tax advantage in the following manner:

(1) By virtue of Schedule 24 to Finance Act 2003 (and later s1290 of Corporation Tax Act 2009), corporation tax relief was denied in relation to contributions paid by an employer company into an employee benefit trust ('**EBT**').

(2) The employer company could claim corporation tax relief when the EBT contributions were applied to benefit an employee, at which point income tax under PAYE and national insurance contributions ('**NIC**') would become payable in respect of the benefits so applied.

(3) The Scheme purported to enable tax-free remunerations of employees via the use of an offshore EBT, and to procure an immediate deduction for corporation tax for contributions made to the EBT and the fees for the use of the Scheme.

(4) The Scheme relied on the *exception* provision under sub-section 1290 (4)(a) CTA 2009 to claim the CT deduction.

(5) The main feature of the Scheme was to secure an immediate CT deduction, while claiming that no PAYE and NICs arose on the contributions made by the employer to the EBT which would be allocated to sub-trusts designated for the appellant's directors.

The operation of the Scheme

23. The entities involved in the operation of the Scheme are as follows:

(1) Herald was a human resources company based in Jersey, and would offer a taxpayer company a service in the form of a review for the purpose of making recommendations as to how key employees, such as the company's directors, ought to be 'rewarded and incentivised'.

(2) Herald outsourced that service to a UK limited liability partnership by the name Herald Employment Services LLP ('**HES**'), whose members included Clavis' directors.

(3) The findings of HES' review were to form the basis of the recommendations made by Herald in a report, which would detail various methods of reward such as the payment of a dividend or bonus.

(4) Invariably HES would recommend that rewards be provided by the taxpayer company settling an amount equal to the sum which the review had found would reward and incentivise the directors into an offshore EBT from which the directors could benefit.

(5) Herald Trustees Limited ('**Herald Trustees**') was the trustees of the EBT, and the directors of Herald Trustees were the same as Herald's directors.

The movement of funds and CT deduction

24. The movement of funds to implement the Scheme would follow the steps whereby:

(1) Herald would send an invoice at the same time as the recommendation report for an amount which equated to its fees for implementing the recommendation, plus the sum which it had recommended be made to the EBT; that is, the amount invoiced by Herald was inclusive of the sum to be paid into the EBT.

(2) To implement the recommendation, the company would pay the full amount invoiced directly to Herald. This was supposedly to ensure that the total amount would qualify for the exception under sub-section 1290(4)(a) CTA 2009.

(3) Herald's fees for each implementation exercise was approximately 10% of the invoice total. The balance of approximately 90% of the invoice total would be settled on the EBT in the company's name.

(4) Herald would deduct its fees form the invoice total before settlement contribution into the employee benefit trust in the company's name.

(5) A sub-trust would be set up for each employee who was to benefit from the arrangements, and a share of the balance settled into the EBT would be allocated to each sub-trust.

(6) The funds in the sub-trust would be used to benefit the employee, such as, by making loans from the sub-trust designated for the benefit of the particular employee.

(7) The company would then claim a corporation tax deduction for the payment it had made under the invoice, on the basis that the invoice payment constituted fees paid to Herald under sub-section 1290(4)(a) CTA 2009.

Introduction of the Scheme

25. In July 2008, the directors were introduced to the Clavis/Herald SPV remuneration arrangements (the '**Arrangement**' or the '**Scheme'**) by Kevin McNally (an IFA), who is James Kelland's financial adviser. McNally then introduced the directors to John Forbes of Forbes Accountants ('Forbes'), who was part of the Probiz network of accountants. There followed:

(1) On 17 July 2008, Langran and Kelland attended a presentation by Forbes in respect of the Scheme. Langran understood the Arrangement as a 'a form of remuneration tax planning', and would involve 'advice from a remuneration consultant and the use of an Employee Benefit Trust'.

(2) Also on 17 July 2008, Langran asked Tucker to contact Forbes in relation to the Arrangement. Forbes asked Tucker to sign a non-disclosure agreement (for Probiz), and also confidentiality agreements (from Clavis) on behalf of Dickinsons on 21 July 2008, prior to arranging a meeting for a full presentation of the Arrangement to Tucker.

(3) On 31 July 2008, a meeting was held at Dickinsons' office in Rickmansworth, attended by Tucker, Forbes, and David Cowen of Clavis, wherein the Arrangement was explained ('the first/July meeting').

(4) Following the first meeting, Tucker had a half-hour telephone conversation with Langran and Kelland wherein he explained his understanding of the Arrangement. Dickinsons was then instructed by Delphi to 'formally review the Clavis remuneration strategy'.

(5) On the morning of 4 August 2008 ('the second/August meeting'), Tucker met with representatives of Clavis in Jersey, accompanied by David Cowen. Tucker was given sight of the tax opinions of Andrew Thornhill KC on the Arrangement.

(6) On the afternoon of 4 August 2008, Tucker was emailed further documents including: (i) a spreadsheet showing the comparison of various methods of profit extraction from the company, (ii) confirmation regarding the level of Professional Indemnity cover for Herald Trustees, and (iii) a copy of the latest trust instruments.

(7) Several follow-up meetings between Tucker and Clavis' representatives took place between 4 and 7 August 2008, including one at the trustees' office in Jersey. Tucker was provided with copies of the draft documentation used for the Scheme.

Tucker's credentials as reviewer of the Clavis Scheme

26. Mr Tucker is a Chartered Accountant and a Chartered Tax Adviser ('**CTA**') and has specialised in tax since 1978. He is also a member of the Society of Trust and Estate Practitioners ('**STEP**').

27. Mr Tucker qualified in 1979 with a BigFour firm. He was a partner of Saffery Champness at its Guernsey Office (1987 to 1993) before becoming a tax partner at Dickinsons, which he currently holds. He has served as a Member (2007 to 2019) of the Council of the Institute of Chartered Accountants in England and Wales ('**ICAEW**'), and the Tax Committees of the Tax Faculty of ICAEW for more than 25 years; the committees' work included making representations in relation to tax legislation on behalf of ICAEW.

28. Prior to the review of Clavis' Scheme, Tucker had been similarly instructed to evaluate tax planning arrangements for Delphi on two previous occasions, which were both rejected by Tucker on the basis that the arrangements were not 'technically sound (i.e. from a tax perspective)'. One of these arrangements was identified as a 'Share Incentive Plan' arrangement which Tucker reviewed in December 2006. The directors followed Tucker's advice and did not proceed with those schemes.

29. In evidence, Mr Tucker emphasised that his advice in relation to tax planning arrangements was focused on the 'technical aspects of a tax arrangement' and not 'on the commercial implications of undertaking the same'. That distinction applied to his advice in respect of the review on the Share Incentive Plan in 2006, as with the Clavis Scheme in 2008.

Thornhill's Opinions

30. In his meeting with Clavis on 4 August 2008, Tucker was shown a selection of opinions dated 28 June 2007 provided by Andrew Thornhill KC in relation to the Arrangement. The first in the selection of opinions shown to Tucker (the 'Opinion') was on the 'Structure' and gave a 'Tax Analysis', and was relied upon by the appellant as giving assurance of the effectiveness of the Scheme. The opinions were shown to Tucker at his meeting with Clavis on 4 August 2008, but he was not given a copy of the opinions at the time.

31. The opinions are no longer subjected to legal privilege, and were obtained by the appellant for inclusion in the bundle. (The opinions were provided to the appellant upon request to Clavis after Delphi had completed the first two tranches according to Tucker's evidence.)

32. The instruction for which the Opinion was produced is stated in the introduction, namely:

> 'I am instructed by Clavis Solutions Ltd/ Clavis Tax Solutions LLP ("Clavis") in relation to the use of a Human Resources Consultancy Company ('**HRC**') and a special purpose trust to provide discretionary benefits to employees of UK companies in a similar way to an employee benefit trust.'

The Structure Contemplated

33. Under the heading 'The Structure Contemplated', the Opinion describes the Arrangement in four paragraphs in terms of:

(1) Intentions of the Scheme:

> 'The intentions would be for the Directors of a trading company to outsource to HRC, a completely independent party, the function of evaluating the performance of key personnel and providing reward packages based on that evaluation with awards then made in a tax efficient manner.'

(2) The contractual arrangement between the trading company and the HRC:

> 'The trading company would enter into an outsourcing contract with HRC, a completely independent body to the trading company. The contract would identify the requirements of the trading company, and the services to be provided by HRC. No fee would be payable at the point of the company entering into the outsourcing contract. A fee would be determined once a report had been submitted and would be payable prior to implementation. HRC would meet with the Directors of the trading company and the selected

employees and by a process of thorough interviews assess what benefits of what approximate value would best meet the objective of the company and the aspirations of the employee.'

(3) The role of a HRC is set out by Thornhill in the following terms:

'HRC would compile a report setting out recommendations, in the light of all relevant circumstances including tax and proposing an overall fee to cover the provision of all the services as defined in the agreement. VAT is likely to be chargeable under the "reverse charge" provision. HRC would identify a range of possible reward and incentive arrangements for employees. The report would be provided to the company which would settle the invoice.

(4) The timing of payment of an 'overall fee' is described as follows:

'Once the proposal is accepted and an overall fee agreed the report would be implemented, quite probably with minor variations in type of benefit and quantum of expenditure.'

Tax Analysis

34. Under the heading 'Tax Analysis', Thornhill set out the legislative provisions cited as being engaged by the Scheme as follows:

'The relevant legislation governing the corporation tax deductibility of payments for employee benefit contributions is Schedule 24 to the Finance Act 2003 as amended by draft legislation introduced in the budge on 21st March 2007. The broad aim of these measure is to restrict deduction for EBT contributions until such time as those contributions are applied to benefit employees in a form which gives rise to an employment income tax charge and an NIC charge.'

The 'goods and services exemption': para 8(a) Sch 24 FA 2003 (sub-s 1290(4)(a) CTA 2009)

35. The Scheme relied on the goods and services exemption under para 8(1) of Schedule 24 to the Finance Act 2003, 'in respect of anything given as a consideration for goods or services provided in the course of a trade or profession' – this exemption for EBT purposes is incorporated under subsection 1290(4)(a) CTA 2009 as set out above.

36. According to Thornhill, the proposed Scheme was supposed to be effective in securing an *exemption* from income tax and NIC charges pursuant to para 8(a) of Schedule 24 FA 2003 in the following manner:

'The Finance Act 2007 will introduce further measures to restrict the availability of corporation tax deductions for contributions to an EBT.

However, the anti-avoidance measures as they currently stand do not apply "in respect of anything given as consideration for goods or services provided in the course of a trade or profession". See FA 2003 Schedule 24, para 8(a). Clearly, the services envisaged must concern the provision of employee benefits. Otherwise the legislation would not apply. The services envisaged do of course, directly concern the provision of benefits. It is difficult to see how any limitations could be implied so as to bring the services here outside the protection of paragraph 8(a).'

37. The effectiveness of the Scheme was staked on invoking the 'goods and services' exemption under para 8(a) of Sch 24 FA 2003 via the engagement of an HRC, as Thornhill continued by stating:

'In my opinion, therefore, properly implemented, the proposal outlined above should allow the employer company to claim a corporation tax deduction for the amount paid to the HRC. Subject to the points outlined below, I confirm

> that in my view the payments should fall into the exclusion from Schedule 24 FA 2003 set out at paragraph 8(a) of that Schedule – "the goods and services exemption".'

Directions on 'properly implemented' arrangements

38. Thornhill gave further directions as to what he meant by 'properly implemented':

> 'For the proposal to work, it is vital that the HRC does not act as agent for the company. Payment must be made unconditionally to the HRC for the functions it is to perform and HRC must have complete freedom to then perform those services as it sees far within the confines of the report. These decisions must be taken – and be seen to be taken – by HRC. In my view, documents confirm that this is indeed what will happen.
>
> The fee paid to HRC will encompass both work to be undertaken by HRC in assessing the rewards to be provided and the cost of making those rewards. Should the situation arise whereby HRC is paid significantly more than HRC ultimately pays out to employees, HRC must be free to retain the excess.'

Anti-avoidance legislation

39. The only anti-avoidance aspect of the Arrangement covered by Thornhill was in relation to the specific anti-avoidance provision under paragraph 33 of the 2007 Finance Bill:

> 'I further confirm that it is my view that the anti-avoidance legislation set out at paragraph 33 of the 2007 Finance Bill further restricting deductions for employee benefit contributions would not affect the proposal set out above.
>
> A deduction would be claimed on the grounds that the payment was made wholly and exclusively for the purpose of the trade. If the payment is made after the year end, it is vital that a liability is established in terms of FRS 12 during the period of account. It does not seem that payment needs to be made within nine months of the year end (see FA 1989 s. 43(2)) though it might be sensible to make it within that time.'

The cohort of Thornhill's opinions

40. The Opinion related above represented one among the 6 opinions by Thornhill shown to Tucker on 4 August 2008. The advice from the other opinions included:

(1) One dated 28 June 2008 advised on 'the tax effectiveness of providing benefits through the use of trusts and sub-trusts' in the Clavis Arrangement.

(2) One dated 9 July 2007 was on 'the use of a Human Resources Consultancy Company to provide discretionary benefits to employees of UK companies in a similar way to an [EBT]'.

(3) A conference meeting between Thornhill and Clavis on 4 October 2007 at Pump Court Tax Chambers in London, was followed by Thornhill's opinions stating that:

(a) the proposal would not be disclosable to HMRC pursuant to Tax Avoidance Schemes (Prescribed Description of Arrangements) Regulations SI006/1543;

(b) the relevant amount paid to the HRC should be included as an expense in 'director's remuneration' in the company's profit and loss account in respect of a benefit passing to a director;

(c) a corporation tax deduction for the amount paid to HRC should be claimed;

(d) a note to provide something 'more precise' of the nature of the transaction in the following terms:

> 'This figure includes the sum of £[ ] which was paid to a human resources company. The payment was made in order that he human resources company could develop and implement a remuneration plan for the purposes of rewarding key employees of the company for their performance over a specified period.'

(4) On 3 March 2008, a further opinion was provided by Thornhill on the issue 'beneficial loans' with reference to section 720 ITA 2007.

(5) On 10 March 2008, a 5-page opinion was given on 'further income tax issues relating to the outsourcing strategy'.

Tucker's advice letter of 7 August 2008

41. The letter of 7 August 2008 was authored and delivered by Tucker in person to the three directors of Delphi during a meeting which took place on the same day. This letter came to be pivotal in Officer Barraclough's decision to assess the penalties and in setting the penalty percentage. The central significance accorded to this letter in HMRC's decision making merits a full citation of its material content.

42. Tucker confirmed that this was not a generic letter, but a bespoke piece of advice, and had been reviewed by two other partners in Dickinsons who assisted in editing it.

43. The letter is formally addressed to Mark Langran of Delphi Derivates Ltd, with 'Dear Mark' as the salutation, and entitled '*Review of Clavis Tax Arrangements*'. The letter contains 14 paragraphs and are summarised in line with the paragraph numbering below.

(1) The letter starts with: 'In accordance with your instructions', and relates the two meetings Tucker had with Clavis Solutions Ltd (Frank Harris and David Cowen) on 31 July and 4 August 2008) who explained the structure of the Arrangement in the first meeting, along with 'a selection of Counsel Opinions'. In the second meeting, Tucker was shown the 'Instructions to Counsel', 'a "Bible" showing the documents which make up the arrangements', and 'a file explaining the status and regulation of the Jersey based Human Resources Company'.

(2) This paragraph relates the documents made available to Tucker, noting that he had 'only been shown the paperwork for a sub-trust' (and not the main trust document).

(3) The third paragraph is short and contains the caveat: '*I have not as yet taken up any external references on the scheme with other accountants*.'

(4) Paragraph 4 summarises the Scheme in the following terms:

> 'The planning has the merit of simplicity and uses an exemption within the anti-avoidance rules which were brought in to counter the use of Employment Benefit Trusts (EBT's). Whilst the direct use of an EBT by paying money into such an entity will not succeed in obtaining a Corporation Tax deduction, the use of the payment by way of sub-contracted services appears to circumvent the rules. This is the opinion of Andrew Thornhill a well respected QC at Pump Court Tax Chambers.'

(5) Paragraph 5 goes on to refer to another opinion on DOTAS reporting:

> 'An Opinion has also been obtained dealing with my concern that no report of the scheme had been made under the "DOTAS" rules which require most tax planning arrangements to be reported. This scheme has not needed to be reported as it existed at the time when the rules were introduced. Counsel has confirmed that this is still the case.'

(6) Paragraph 6 sets out the attending features of the Scheme using sub-trusts and the loan mechanism:

> 'There are various refinements to the arrangements including the use of an offshore bank account as a means to pay interest on the loan from the EBT sub-trust and thus avoid any tax liabilities or with holding tax on the payment of interest to an offshore entity.'

(7) Paragraph 7 is a cost-benefit analysis, pitching the costs of entering the Scheme against the anticipated tax savings:

> The projections of tax saving based upon a profit of say £1,000,000 as prepared by Clavis do give a substantial tax saving of approximately 35% in year one but is should be noted that ongoing costs of £1500 to £2000 will be incurred per annum in each subtrust and will continue as long as the structure is required. Broadly this will be at least until the cessation of employment with the principal company and may be for 10 to 20 years or longer. I can explain the impact of that if required.

(8) Paragraph 8 summarises the economics of the cost-benefit analysis as setting a minimum entry level:

> Although the minimum level set for bonuses is £100,000, the more effective level would be £250,000 should ongoing costs require to be funded for many years.'

(9) Paragraph 9 identifies 'possible areas of risk' as follows:

> 'There are a number of possible areas of risk: –
>
> 1) The possible introduction of retrospective legislation.
> 2) A possible attack on the principal shareholder under the Inheritance Tax legislation – I have seen that line of attack used on EBT's in a way which has caused the breakdown of such arrangements.
> 3) The use of this scheme might be blocked at the time of the Pre-Budget report which may be in October 2008 if not sooner. This would mean that any planning would have to be implemented before then. I understand that total planning through these arrangements may be approaching £100,000,000.
> 4) Should the Corporation tax planning fail but the "income tax" side of the planning prove successful, the result would not be completely fatal but would make the savings only marginal.
> 5) The VAT status of a company using these arrangements is most important. The company must be able to fully recover all VAT as the payment made to the Human Resources company will be within the reverse charge mechanism.'

(10) Paragraph 10 recommends obtaining a second opinion:

> 'My normal and usual advice for any such scheme would be to ask that another Counsel Opinion from a barrister other than the original one is obtained if the Promoters of the arrangements are prepared to permit this.'

(11) Paragraph 11 contains the caveat that the Scheme is open to challenge from HMRC:

> 'Whilst the scheme seems to be most effective any aggressive tax planning will always be open to attack from HMRC and their current policy is to litigate everything. Enquiries have been raised into the computations of companies which have utilised these arrangements but I understand that HMRC are just at the collection of information stage.'

(12) Paragraph 12 relates the promoters' agreement to fund the first stage of litigation:

> 'The promoters undertake to fund the scheme to the first stage of any appeal process which would be to the new style Tax Tribunal form October 2008. If the tax payer won at the first stage, the promoters have not agreed to fund the matter to higher courts and the cost of such a case at the High Court or Court of Appeal is very expensive. If HMRC took the matter to the higher courts, that is a possible cost which you might have to bear. In other schemes, promoters have created a fighting fund which would allow the costs to be covered if the case went all the way through the appeal system.'

(13) Paragraph 13 assesses the chance of success in litigation and reiterates recommendation for advice from independent tax counsel:

> 'This scheme appears to have a stronger chance of success than many more convoluted schemes but considering the amount you may wish to place in these arrangements I would recommend that the matter be put before independent Tax Counsel.'

(14) Paragraph 14 is the final paragraph with conclusions and a disclaimer:

> I can not [*original as two words*] formally recommend such a scheme to you as there is certainly a risk in entering such arrangements. Should you wish to proceed having taken a commercial view, I would assist to try to ensure that the arrangements are properly implemented. Dickinsons will not be held responsible should you incur losses by entering into these arrangements.'

44. In evidence, Mr Tucker elaborated on aspects of his letter of 7 August 2008, such as: (a) in carrying out his review of the Arrangement, he had telephone conversations and email exchanges with David Cowen of Clavis. In particular, he had questioned why the Arrangement did not fall within the DOTAS regime and was provided with a copy of counsel opinions on this specific issue; and (b) on 5 August 2008, he was sent a fax by Cowen with notes of a further conference with Thornhill (held on 5 July 2008) which covered additional points not included in the written opinion.

Transcript of Tucker's telephone call to Cowen on 7 August 2008

45. Tucker telephoned Cowen in the course of the meeting with Delphi's directors on 7 August 2008, and the transcript of this telephone call to Cowen is one of the exhibits. It would appear to have taken place after Tucker's meeting with Delphi's directors on 7 August 2008, as Tucker referred to having 'spent an hour or two running through these arrangements with our clients'. Other facts emerged from the telephone conversation include:

(1) John Forbes would receive commissions for introducing Delphi.

(2) Tucker remarked on '*a certain artificiality*' from '*the very narrow gaps when something was forced through in about 10 days in December on the bridle*', and Cowen reassured Tucker that '*in terms of your case I would obviously by time-phasing the way we would suggest there will be a much larger gap*'.

(3) Tucker then commented on the formulaic nature of the reports:

> PT [Tucker]: … would you personalise [the report] to pick up on the nature of what our client actually deals with? … It is purely the fact that one of the concerns was that these reports are too much of a standard with any tiny bits added …'

(4) Tucker's view on his involvement (as regards reports) if Delphi took the Scheme:

> PT: And if I am getting involved with it and our clients are going to … we want to make sure that we've not spoilt the ship.

(5) When Cowen tried to impress Tucker on the importance of *Sempra* as supporting the Clavis Scheme 'more than anything else', Tucker arrested the flow by saying:

> '– sorry, my role in all of this is really to review the way you put the scheme together. Can I ask if you were going to go forward on this, would it be acceptable to you that I actually had sight of your tax report before it is finalised? … Because there were certain issues and thresholds. … [such as] the EMI levels were wrong.'

On the economics of going in for the Scheme

46. Tucker asked Cowen questions on the level of insurance cover (being £10 million for each and every case), of the annual fees to the trustees ('the costs will kill it'[sub-trust]), and Tucker then remarked:

> PT: … I wouldn't recommend it for any amount less [than £250,000] and I'm actually pushing it to a higher level although there is nothing sort of in it for us because we are not involved in your commission arrangements on this one at all.
>
> PT: … my discussion here I think, there was a guy at this client that originally talked of a figure of £1 million… I'm looking at if they're going to do it then I'd go in for £2 million, or two and a half.

47. Tucker admitted to Cowen of the fee-earning prospect to his firm if Delphi got involved in the Scheme:

> PT: I don't know if it is appropriate and I don't sort of float this as a thought to you to sort of consider but we will be charging our client because we will be getting involved in making sure all the documentation is done at the time and not all pre-signed and the like.

On the offshore aspects and 'downsides'

48. On the offshore aspects of the Arrangement, Tucker said to Cowen: '*My heart dropped*' when he realised from the documents sent to him that he had '*a full blown Jersey discretionary trust for all nine yards of it*', and that thought he knew '*what beast [he is] now dealing with*'.

49. Tucker then related the possibility of 'retrospective legislation' as a downside:

> PT: But they've got to take a decision on it. … I've given them a downside, I've sort of gone through, I've looked at the retrospective legislation point and said my view on it, it's a personal view, is that its [sic] below 50% because it's a specific exemption –
>
> PT: … the chances are less than 50% and much slimmer than if it was some other more complex scheme you had then you could be at risk because –
>
> PT: Back in 03/04, when they blocked employment schemes, they said they would block them all from that date back then and retrospectively block everything. But it's not retrospective because they had announced in advance but here we're talking about a corporation tax deduction point.
>
> PT: And not an employment point. … So it's not – not caught within that.

On the point of loan being written off without it being benefit

50. Tucker's phone call started with a question to Cowen on the exit out of a sub-trust as a point that he had not 'bottomed out', and the following aspects were discussed:

(1) What happens at the point of employment ceasing:

> 'PT: The sub trusts have got to continue effectively whilst […] in employment. Can they actually be wound up when they cease employment or do the trusts need to be there until they die?
>
> D [David Cowen]: We have been to Counsel on that very point, the legislation is a bit woolly in parts but the suggestion … is that, let's just say for example that a client ceases employment on 31 August 2008. … At that point, let's just say there is a loan on foot from the sub trust so essentially they had their money out of the sub trust. […]

(2) Cowen then suggested having a 'fallow year' between cessation of employment and exit from a sub-trust:

> D: … – at that point the P11 D situation ceases because there's no employment. … The recommendation from, well should I say a suggestion from Counsel has been that you then leave a fallow tax year after the … year following he cessation of employment.
>
> D: And in the year following the fallow year you then request the trustees to write a loan off. The Counsel was fairly okay with that happening and following through with a write off not being employed as income.
>
> PT: Sorry, can you just run that past me? You can write the loan off because it is not employment income then after you left a gap year?
>
> D: … that is the inference from Counsel, yes.

(3) Tucker then queried whether a 'distribution' (instead of advancing a loan) could be made out of the sub-trusts on exit:

> PT: Oh hang on, so that's a point, so you could have a distribution after you ceased employment.
>
> D: If you've never taken the loan in the first place.
>
> PT: And that's not caught by anything.
>
> D: No.

(4) Tucker ended the phone call with a summary of his understanding:

> PT: … I think you've answered in part the position on ongoing Trusts, leave a fallow year and then the loan can be written off without being benefit. Or if no money had been taken out but that should never be the case. … *Not what I can see if it is worthwhile.* (Italics added)

Delphi entering into the Scheme

51. After Tucker's review letter of 7 August 2008, there were further discussions between Tucker and Delphi's directors and with representatives of Clavis. In terms of documentary records, the following events took place that led to Delphi's entering the Scheme. Delphi used the Scheme in the years 2008-09 and 2009-10 by making four tranches of payments to Herald.

(1) On 21 August 2008, Delphi's board of directors held a meeting at which they agreed to set up an employment committee with responsibility for the appellant's strategy for the establishment of an incentive, reward and retention arrangement for the benefit of its employees. On the same day, the appellant sent a letter to Herald asking for details of the services they provided to which Herald responded on 28 August 2008.

(2) On 1 September 2008, the appellant entered into an outsourcing arrangement with Herald under which Herald agreed to provide certain services specified in Schedule 1 to that agreement, which included: (i) the evaluation of the duties of the employees specified by the appellant; (ii) conducting interviews with the employees and the appellant; (iii) production of a report to the appellant recommending the types of benefits to be provided and their approximate costs; (iv) a proposal for an overall fee which should cover the

benefits to be provided to the employees as well as Herald's costs, and (v) the implementation of the agreed proposals.

The first tranche – September 2008

52. The details in relation to the first tranche of payment are as follows:

(1) On 2 September 2008, David Cowen and Sally Fuller, as representatives of HES (both of whom were also employees of Clavis) attended the appellant's premises and met with Delphi's directors.

(2) Herald prepared a report dated 30 September 2008 including an evaluation of all three directors, and recommended that all three directors be provided benefits by either cash bonuses or a special purpose trust and that a budget of £1.8m be made available to reward, incentivise and retain them.

(3) Herald issue an invoice for £1.8m to Delphi on 30 September 2008, the same date as the report.

(4) At a board meeting on 6 October 2008, the contents of the report were considered and Delphi's directors agreed to settle the invoice.

(5) Delphi paid £1.8m to Herald, of which £1,651,376.15 (after deduction of fees payable to Herald) was settled on the Delphi Derivates Limited Special Purpose Trust ('**Delphi's EBT**') on 7 October 2008.

(6) The beneficiaries of the Delphi EBT included the three directors of Delphi.

(7) A proportion of the sum £1,651,376.15 was allocated to a sub-fund for the benefit of each of the directors in accordance with the recommendations in Herald's report.

The second tranche – November 2008

53. The second tranche was implemented two months after the first in November 2008.

(1) Frank Harris on behalf of HES (Harris was also a director of Clavis) met with the appellant's directors on 11 November 2008.

(2) Herald prepared a report dated 19 November 2008 which recommended that the three directors be provided benefits by either cash bonuses or a special purpose trust and that a budge of £3.9m be made available to reward, incentivise and retain them.

(3) Herald issued an invoice for that amount to the appellant on the same date.

(4) The contents of the report were considered at a board meeting on the same date and the directors agreed to settle the invoice.

(5) On 20 November 2008, Delphi paid £3.9m to Herald.

(6) On 24 November 2008, the sum of £3,611,111 was settled on Delphi's EBT.

(7) On 25 November 2008, allocations to the directors' sub-trusts were made in accordance with the recommendations in Herald's report.

The third tranche – February 2009

54. The third tranche was implemented in February 2009.

(1) Frank Harris on behalf of HES met with the directors on 12 February 2009.

(2) Herald prepared a report dated 20 February 2009. This report was *identical* to the 19 November 2008 report save that the employee evaluations did not include the profit for the period and the recommended was changed to £1.35m.

(3) Herald issued an invoice for £1.35m to Delphi on the same date.

(4) The contents of the report were considered at a board meeting on the same date and the directors agreed to settle the invoice.

(5) On 24 February 2009, Delphi paid £1.35m to Herald.

(6) On 24 February 2009, the sum of £1.25m was settled on Delphi's EBT.

(7) On 25 February 2008, allocations to the directors' sub-trusts were made in accordance with the recommendations in Herald's report.

The fourth tranche – November/December 2009

55. The evaluation report for the fourth and final tranche was produced on 27 October 2009. The correspondence in the run-up to 27 October 2009 in the bundle shows the following:

(1) On 17 September 2009, Officer Walker received a telephone call from Sally Fuller of **Clavis Solutions** (Clavis Solutions being the 'tax advisers to Herald Resource') in response to Walker's letter of 15 September 2009. The note of the call (by Walker) recorded the following:

> 'Fuller explained that she had spoken to Dave Jones at SI Liverpool regarding Walker's letter as Jones was overseeing a review of the remuneration scheme provided by Clavis Solutions which had been used by several other companies including Delphi Derivatives.
>
> Fuller said that she would confirm the details in writing to Walker and provide a "bible" of documents regarding use of the remuneration arrangement.'

(2) On 21 October 2009, Dickinsons responded to HMRC's letter of 15 September 2009 under the heading '*Check of CTSA Tax Return for Delphi Derivatives Limited/ Period ended 30th June 2008'*. The letter opened by referring to Officer Walker's 'recent discussion' with Sally Fuller of Clavis Solutions, and enclosed 'a complete bible of documents' said to support 'the key employee reward and incentivisation arrangement undertaken' by Delphi in the accounting period ended 30 June 2008, together with the correspondence and minutes contained in the 'bible'. Dickinsons' letter also refers specifically to being aware of HMC's enquiries into other scheme users:

> 'We understand that you [i.e. Officer Walker] have agreed to liaise directly with Mr David Jones from Specialist Investigations in Liverpool who is coordinating all enquiries into this arrangement.'

(3) On 22 October 2009, Sally Fuller emailed Kerry Hall (and two others) at Clavis Solutions under the subject heading of 'Delphi Derivates new sign up pack for SPT4':

> 'Can one of you please produce Delphi Derivates new sign up pack for SPT4? David [Cowen] going down to London next Tuesday for sign up, so he'll need it ready before then. They're doing £3m and will relate to their year ended 30 June 2009.'

56. The 'sign-up pack for SPT4' in Sally Fuller's email was a reference to the evaluation report to be produced *after* the scheduled meeting on 27 October 2009 when Cowen would have met with Delphi's directors to carry out the 'services' to be performed by HES. The sign up pack SPT4 version was completed with a recommendation of a bonus of £1m gross per director with an invoice total of £3m.

57. The final report with the cover title being: '*Company Information Sheets and Employee Performance Evaluation Sheets prepared by Herald Employment and Recruitment Services*

Limited' changed the recommended budget amount from the initial of £3m to £5.4m. The significant dates of events leading to the amendment in the budgeted amount are as follows:

(1) On 27 October 2009, David Cowen for HES met with the appellant's directors.

(2) The employee evaluation documents supposedly completed on 27 October 2009 stated the recommended budget to be £3m.

(3) On 31 October 2009, Langran's short email to Cowen stated in full as follows:
'Have spoken to Peter Tucker and he thinks we should do £5.4m – I imagine this is ok with you?!'

(4) Herald's report produced on 19 November 2009 recommended a budget of £5.4m.

58. The following correspondence (after Cowen's meeting of 27 October 2009) gives some indication as to the circumstances surrounding the implementation of tranche 4 due to cashflow issues faced by Delphi at the time. While there was this amendment by Herald of the initial £3m to £5.4m, Delphi was unable to pay the invoice total of £5.4m in one go. A 'loan back' arrangement was made between Delphi and Herald Trustees, whereby the first instalment was loaned back to the directors to fund the payment of the second instalment of the invoice.

(1) A letter dated 16 November 2009 by Herald Employment Services LLP (HES in Cheshire) to Christina Kiely of Herald Resource (in Jersey) regarding Delphi, states:

> 'Following our meeting with the above clients we are pleased to set out our findings for your consideration:-
>
> On the basis of the company and employee evaluations we have carried out, our preliminary view is that an overall benefit and incentive budget of approximately £5,000,000.00 to £5,500,000.00 should be able to provide a sufficient level of benefits and incentives to motivate, reward and retain the employees.'

(2) By email dated 20 November from Langran to Pauline Egan of Herald Trustees:

> 'As discussed please could you send me the necessary paperwork for me to borrow £200,000 from the trust on an interest paying basis (which I think means we have to do slightly more so that I have enough money left in my […] Jersey account to pay the interest when it becomes due).'

(3) By email dated 23 November 2009 from Langran to Cowen:

> 'I have paid £2.7mln to Herald today – then I need to arrange for the three of us to borrow it back so we can pay the balance of the invoice. Please could you ask whoever does the paperwork to organise the loan documents for us – we will need to do a loan of £900,000 each as cash flow a bit of an issue at the moment.'

59. Following the discussion of the 'loan-back' arrangement by Langran's email of 23 November 2009, the steps in terms of payment to implement tranche 4 took place as follows.

(1) On 23 November 2009, Langran emailed Cowen that the invoice would need to be paid in two instalments with the first instalment being loaned back to the directors.

(2) On 23 November 2009, the appellant paid £2.7m to Herald.

(3) On 24 November 2009, £2,522,429 was settled into Delphi's EBT.

(4) On 25 November 2009, the settled amount was allocated into the sub-trusts.

(5) On 3 December 2009, the appellant paid the second instalment of £2.7m to Herald.

(6) On 4 December 2009 , the sum of £2,523,364 (net of fees deducted by Herald) was settled into Delphi's EBT.

(7) On 7 December 2009, amounts were allocated to the sub-trusts.

The case of *Sempra Metals v HMRC*

60. Around the time when the third tranche was being implemented in February 2009, an email from David Cowen of Clavis on 18 February 2009 set out to relate to Delphi what was described as the view of the law following the case of *Sempra Metals v HMRC*. In this email, Cowen referred to *Sempra Metals* as 'the first significant case relating to Employee Benefit Trusts since *Dextra*' and Cowen's email started as follows:

> 'I am pleased to say that our Counsel [i.e. Thornhill] who in fact appeared for the Sempra Company at the hearing has confirmed to us that their strategy was completely distinct from ours. There were six issues at stake and the one point that HMRC were successful on concerned deductibility within the company. I can confirm that there are no negative implications for the Clavis Strategy. In fact, it is exactly the opposite.'

61. Cowen then distinguished the Clavis Special Purpose Trust ('**SPT**') strategy from Sempra's EBT as follows:

> 'In the Sempra case the company argued that Schedule 24 could not apply as its employees were not beneficiaries of the trust (completely different from ours), rather members of their immediate family were. This argument was rejected by the Special Commissioners and so the contribution was not allowable.
>
> The Clavis SPT strategy works because the invoice raised by the HR Co for the outsourced evaluation process is deductible because of the exemption contained within paragraph 8a Schedule 24 FA 2003, it passes the wholly and exclusively test on general principles and the allocation of funds to sub trusts does not constitute earnings.

62. Cowen's email finished with a positive evaluation of the Clavis SPT strategy in terms:

> 'I would reiterate that the decision was very good news for us and Counsel has confirmed this in conference – we await the outcome of the High Court Appeal which is being heard next month and our Counsel is again leading for Sempra.'

HMRC's Corporation Tax enquiries

63. In the corporation tax return ('**CT return**') for the accounting period ended 30 June 2008, the appellant claimed a deduction of £1.8m (on an accrual basis) in respect of the first tranche payment to Herald in September 2008.

64. In the CT return filed on 9 June 2010 for the accounting period ended 30 June 2009, the appellant claimed a deduction in respect of the second, third and fourth tranches paid to Herald.

65. The following enquiries were opened into the CT returns:

(1) On 15 September 2009, HMRC issued a letter to Delphi to open an enquiry into the 2008 CT return under para 24(1) Schedule 18 to the Finance Act 1988.

(2) On 12 January 2011, HMRC opened an enquiry into the 2009 CT return.

Special Investigations into Clavis as promoter

66. Between 2010 and 2015, HMRC also carried out centralised enquiries into the Clavis EBT arrangements, which were handled by Clavis, and Dickinsons were not directly involved in these centralised enquiries.

67. In respect of HMRC's enquiries into Clavis, Delphi was issued with a letter by Officer David Jones of Specialist Investigations unit on 16 July 2010, wherein it is stated:

> 'I am writing to you because your company has been identified as a current or past user of tax avoidance arrangements promoted by Clavis Tax Solutions LLP and administered by Herald Employment and Recruitment Services Limited. …(The Promoter has claimed that there was no obligation to disclose these arrangements to HMRC's Anti-Avoidance Group; this claim may be revisited once HMRC enquiries have been resolved.)

68. The letter was a briefing on how the enquiries into Clavis would be co-ordinated with the enquiries into the users of the Scheme.

> 'You and other users of the arrangements should know that HMRC is exploring through the Promoter potential challenges to the arrangements with regard to, amongst other things, the validity of the corporation tax deduction claimed for payments for services and whether or not PAYE and NIC should have been applied to payments received by beneficiary employees of the Company usually by way of interest free loans from an Employment Benefit Trust. HMRC is also looking at similar schemes marketed by other Promoters.'

CT enquiries resulted in PAYE and NIC assessments

69. The enquiries resulted in Determinations under regulation 80 of the Income Tax (PAYE) Regulations 2003, and Decisions under section 8 of the Social Security (Transfer of Functions) Act 1999 being issued by HMRC:

(1) On 3 December 2012, PAYE Determinations and NICs Decisions were issued for 2008-09. These were appealed by Dickinsons on behalf of Delphi on 6 December 2012.

(2) In November 2013, HMRC issued PAYE Determinations and NICs Decisions in relation to the year 2009-10, which were appealed on 19 November 2013.

EBT Settlement Opportunity

70. By letter dated 27 February 2015, HMRC wrote to Delphi to follow up on an earlier letter sent in December 2014 which advised that the EBT Settlement Opportunity ('**EBTSO**') was closing and if the company wanted to take advantage of the terms of the opportunity it must register its interest with HMRC by 31 March 2015 and settled with HMRC by 31 July 2015. The letter went on to note that Delphi had expressed interest in settlement, and a questionnaire with 64 questions was attached for completion to take the matter forward.

71. By email dated 23 March 2015, Tucker wrote to Officer David Taylor of HMRC in relation to the settlement opportunity, wherein it was stated:

> 'Further to our telephone conversation you asked that I provide details of payments into trusts/subtrusts to enable you to work out a possible settlement figure for the company.'

72. Officer Taylor's note of the telephone conversation on 30 March 2015 to Tucker regrading reaching a settlement for Delphi recorded, inter alia, as follows:

> 'I confirmed that I had studied the schedule provided and was able to reconcile the amounts, which would enable me to produce indicative calculations of the liability arising. However, I still did not have details of any loans taken by the directors subsequent to 31/3/2009, and I would need this information for the purposes of asking colleagues to calculate any IHT liabilities. Agent will try to get this information, however, in the interim, he will accept computations which exclude any IHT. … Agent also confirmed that none of these loans have

> been shown on P11Ds and, therefore, there would be no credit available for tax paid for class 1A NIC.'

73. Officer Taylor's note of the telephone conversation also explained the working of the EBTSO in relation to the questionnaire.

> 'I advised the agent that the questions asked in our letter dated 27/2/15 would need to be answered because, if the EBTSO was not taken up, we need to compile as much information as possible prior to potential litigation of these types of case. Agent understood this and said that, as Clavis Solutions (Mr Cowen) had been appointed to act for the company in respect of the EBT only, they should be providing answers to these questions.'

74. By letter dated 10 April 2015, Officer Taylor wrote to Dickinsons in relation to Delphi entering into settlement under the EBTSO. The letter enclosed computations showing a total amount payable for PAYE and NICs of £5,312,599.39, with interest calculated to 31 May 2015. The calculations were provided without prejudice, and did not take into account the inheritance tax payable, or potential liability under Part 7A of ITEPA 2003. The computations were based on a settlement date on or before 31 July 2015.

75. The directors of Delphi considered the costs for settling under the EBTSO too high after the indication given by HMRC's computations. In April 2015, the litigation of the *Rangers* EBT appeal was still ongoing, and HMRC had been unsuccessful at the First-tier and Upper Tribunals which was another reason for Delphi not opting to settle within the EBTSO.

76. On 8 June 2015, Office Taylor wrote to Tucker to follow up on the letter of April 2015, and advised that HMRC would need the agreement to the figures per computations provided or details of any adjustments proposed. If no response was received by 19 June 2015, HMRC could not guarantee to get Delphi's settlement finalised by the cut-off date for Delphi to take advantage of the EBTSO terms. Any settlement after 31 July 2015 would be outside of the EBTSO terms.

77. Officer Taylor telephoned Tucker on 13 July 2015 to follow up the matter. Tucker confirmed that due to the amount involved, Delphi would not be settling under the terms of EBTSO. Office Taylor explained that he would shortly be issuing information notice under Schedule 36 FA 2008 to progress with the enquiries.

Liechtenstein Disclosure Facility

78. On 15 December 2015, Tucker was copied a communication from JTC (Trustees) Limited based in Jersey ('**JTC**') raising concerns in relation to the Herald EBTs. The communication was sent with the approval of the Royal Court of Jersey highlighting potential issues and suggested that the Liechtenstein Disclosure Facility ('**LDF**') may need to be used. The important point which required consideration for Delphi was whether there were any tax defaults or errors which would permit the use of the LDF.

79. Tucker was asked to review the JTC communication. After considering the steps taken in setting up the Arrangement and having checked that Delphi had no other matters which would require disclosure, it was decided that the LDF was not applicable. Tucker's view was that there had been no appropriate default by Delphi.

80. A concern was raised in relation to the generic trust operations that the Arrangement was not set up or operated correctly by Herald Trustees Ltd. It was decided that Tucker should visit the offices of JTC in Jersey to review all of the files and papers pertaining to the establishment of Delphi's EBT, and the sub-trusts and their operation since they were set up. Tucker visited JTC on 13 and 14 January 2016, and was given full access to the files relating to Delphi's EBT

and the three sub-trusts. Tucker's review included an examination of the trustees' files, permanent files, minute books, correspondence files, bank statements and investment files.

81. On the basis of the examination, Tucker concluded that the trust and sub-trusts had been created on the dates shown and aligned with the 'Bibles' of documents provided for each of the four special purpose trusts. All bank payments and receipts for the individual trusts aligned with the payments made by Delphi. The review is documented on 31 pages of manuscript notes and showed from the documentation that the trustees were correctly running the trusts and operating 'in the normal fashion of diligent offshore trustees'.

82. According to Tucker, the files reviewed on his visit 'covered everything from the establishment of the trusts and the sub-trusts to December 2015'. So far as the trusts established for Delphi are concerned, there was nothing to indicate that the correct process had not been followed: (i) all the minutes, trust deeds and provision of the initial settled funds had been dealt with in timely fashion; (ii) the flow of funds to the trust and onward transfers to the sub-trusts had taken place as intended; (iii) the flow of funds were all traced through the bank statements and tied in with the trustees minutes and documentation; (iv) the correspondence files including the ongoing investment decisions showed the sub-trusts being managed in the manner expected of the trustees; (v) trustees meetings were held to approve transactions. Based on his review, Tucker was satisfied that the trusts had been correctly established and operated by the trustees.

Voluntary settlement process

83. On 4 November 2015, the judgment from the Inner House of the Court of Session allowed HMRC's appeal in the *Rangers* case. The litigation development caused Delphi to approach HMRC with a view of reaching a voluntary settlement. On 22 December 2015, Dickinsons emailed HMRC to initiate the settlement process. A holding reply from HMRC was received on 22 February 2016 to say that HMRC were reviewing the terms for settlement of EBT cases.

84. The timeline of the process to reach a settlement agreement is summarised as follows:

(1) 30 June 2016 – Dickinsons sent Officer Taylor a follow-up email which went unanswered.

(2) 22 July 2016 – Directors of Delphi were issued with Code of Practice 9 ('**COP 9**') enquiry letters. COP 9 procedure was for 'investigations where [HMRC] suspect tax fraud'. Tucker consulted with a number of professional advisers on the response which would best protect Delphi.

(3) 26 August 2016 – Dickinsons confirmed to HMRC that Delphi's directors would not be accepting the COP 9 invitation but would cooperate with their enquiries.

(4) 14 September 2016 – Tucker emailed Officer Atkinson waiver letters for Delphi directors to communications to be effected with HMRC by email.

(5) 26 September 2016 – Tucker wrote to Atkinson making a settlement proposal on behalf of Delphi, with a schedule of payments, and received an acknowledgement on 27 September that: 'Following the response received by your client's concerning my letter dated 22 July 2016, I am not (at present time) in a position to discuss the matter further.'

(6) 27 September 2016 – Tucker asked Atkinson to provide a reference number for Delphi to make the first payment on account in respect of the proposed settlement. The reference was provided on 28 September with the caveat: 'any payment on account is completely without prejudice to the rights of the Board of HMRC to take such action as it thinks appropriate in dealing with this case'.

(7) On 28 October 2016 – Tucker advised that the first payment on account of £1m had been made and receipt confirmed.

(8) On 7 December 2016 – Atkinson emailed Tucker to confirm that tax on investment gain issue was relevant and that he had escalated the matter as settlement needed to be made by 31 March 2107.

(9) On 25 January 2017 – a second payment on account of £2m was made to HMRC.

(10) On 9 February 2017 – Atkinson emailed Tucker that HMRC were prepared to proceed on a civil basis, and to request copies of the 'bibles' of documents relating to the four tranches of the remuneration planning, and an urgent meeting on 20 or 23 February.

(11) 10 February 2017 – the meeting date was confirmed for 20 February 2017 at Delphi's premises in Colchester.

(12) 13 February 2017 – Atkinson confirmed that the basis of the meeting was continuing under COP 9, but HMRC would not be bound by the terms of Contractual Disclosure Facility ('**CDF**').

85. Apart from the 'bibles' of documentation, Officer Atkinson requested additional information in February 2017 which, according to Mr Tucker, would not have formed part of the 'bibles' but was a request to obtain 'further information that was mainly not within the documents which would have been within the company's possession'. The additional information requested included:

(1) Company Information sheets and Employee Performance evaluation sheets prepared by Herald Employment and Recruitment Services Ltd (for each transaction i.e. x4);

(2) Documents regarding each payment made to the trust, allocation to the sub-trusts and loan applications/payments made to each director from the sub-trusts again for each transaction;

(3) Also the company bank statements confirming the date each payment was made (x4) to Herald Resources.

86. For the additional information requested, Tucker sought the assistance from Clavis and with the requisite authorisation provided from JTC in Jersey, together with copies of bank statements provided by the directors of Delphi, the additional information was provided on 13 February 2017, ahead of the meeting scheduled on 20 February 2017.

87. On 1 March 2017, Atkinson emailed Tucker with his calculations of the tax settlement. From 3 to 20 March 2017, a firm of lawyers were also involved to advise Delphi directors on the terms of the settlement agreement. The proposals submitted on 20 March 2017 were made on a full and final basis 'without admission of any guilt or wrongdoing' as Tucker described.

88. On 22 March 2017, HMRC issued a detailed response which set out an agreement that could be entered into regarding income tax, NICs, inheritance tax and interest due, with the calculation being updated to allow for forward interest and time-to-pay arrangements.

89. Delphi's proposal in relation to penalties was rejected by HMRC in their offer of settlement, and Atkinson's email of 24 March 2017 made it clear: 'By entering into the agreement your clients are not accepting any culpability whatsoever, quite simply the agreement allows the issue of whether any penalties will be charged in this case to be concluded separately.'

90. The settlement agreement was signed by Langran for Delphi and Atkinson for HMRC on 29 March 2017 whereby:

(1) The deductions claimed for the tranches of payments to Herald in the CT returns were allowed to stand.

(2) Delphi agreed to pay: (i) the income tax due under PAYE and employer's NICs on the amounts contributed to Delphi's EBT under the Scheme, (ii) interest on the PAYE and NICs, (iii) the inheritance tax due of £527,209 on the collapse of the EBT.

(3) The parties agreed that the issue of penalties would not form part of the settlement.

Penalty Determinations

91. After the settlement agreement of 29 March 2017, the appellant and HMRC exchanged correspondence and had further meetings. On 15 November 2017, Tucker was notified by Officer Barraclough that he had taken over the case from Atkinson and suggested a meeting, which was not taken up. Barraclough indicated that he would issue a letter with his view on the penalties in due course, which was issued on 17 January 2018.

92. Following receipt of the view of matter letter on penalties, Delphi involved Smith & Williamson and a meeting was held on 16 February 2018 with Barraclough and two other officers for HMRC and Kelland of Delphi, Tucker (and another) of Dickinsons and Andrew McKenna of Smith & Williamson. HMRC's position was that the third and fourth tranches were the subject of 'deliberate' actions, which was not accepted by Delphi and the meeting closed with 'the parties far apart'.

93. The raising of the penalty notices had to be agreed by the Dispute Resolution Board ('**DRB**') and Barraclough set out the various time constraints for submission of documents to the DRB by 27 February 2018 for the determinations to be raised before 28 March 2018.

94. On 28 February 2018, Tucker sent Barraclough a five-page letter with further representations to be put forward to the DRB.

95. On 23 March 2018, Barraclough issued the penalty assessments with a cohort of documents, which together were referred to as the 'Penalty Determinations'.

(a) Penalty Explanation Letter;
(b) Notice of Penalty assessment;
(c) Schedule of penalties;
(d) Schedule 1 for careless penalty;
(e) Schedule 2 for deliberate penalty; and
(f) CC/FS10 – Fact sheet on suspending penalties for careless inaccuracies.

96. The Penalty Determinations were sent by post to Dickinsons and Delphi, and were received by Dickinsons on 3 April 2018. Also on 23 March 2018, the Penalty Determinations were forwarded as email attachments by Barraclough to Tucker and Langran. The email of 23 March 2018 has as its subject heading 'Penalty Determinations', in which the two changes reflected in the final Penalty Determinations were summarised:

(a) Tranche 3 was moved to careless from deliberate;

(b) Tranche 4 has changed from 35% to 38.5% due to HMRC having to use information obtained through third parties to establish the culpable behaviour.

Penalty explanation on 'careless' inaccuracy

97. For tranches 1 to 3, the schedule explaining the penalty percentage states in terms of:

(1) *Behaviour* which led to the inaccuracy categorised as 'careless': '*Customer's failure to follow the advice provided by professional advisor to the customer.'*

(2) *Disclosure* was prompted '*because you did not tell us about the inaccuracy before you had reason to believe we had discovered it, or were about to discover it*'.

(3) *The penalty range* for careless inaccuracy with prompted disclosure is from 15% to 30%.

(4) *Reduction for quality of disclosure*: maximum for Telling 30%, for Helping 40% and for giving access to records 30%, total 100%.

(5) *Penalty percentage* after maximum reduction given is at the minimum of 15%.

(6) *Special reduction*: HMRC do not consider that there are any special circumstances.

(7) *Suspension*: no amount of penalty can be suspended.

98. The total PLR from tranches 1 to 3 is assessed at £3,503,233.26, and the penalty thereon at 15% is £525,484.99.

Penalty explanation on 'deliberate' inaccuracy

99. For tranche 4, the schedule explaining the penalty percentage states in terms of:

(1) *Behaviour* which led to the inaccuracy categorised as 'deliberate':

> 'The customer e-mailed promoter of scheme following review to double contribution. This is evidence that the directors of the company were aware that the paperwork was merely provided to enable the directors to take out funds without paying PAYE and NICs.'

(2) *Disclosure* was prompted '*because you did not tell us about the inaccuracy before you had reason to believe we had discovered it, or were about to discover it*'.

(3) *The penalty range* for deliberate inaccuracy with prompted disclosure is from 35% to 70%.

(4) *Reduction for quality of disclosure*:

(a) Telling 20% (max. 30%): '*The customer deny any culpability in light of evidence provided by third party source. Full reduction cannot be given where information used obtained through third parties is used.*' (The third-party information from Clavis/Herald referred to includes Langran's email to Cowen of 31 October 2009 requesting £5.4m to be put through the Scheme.)

(b) Helping 40% (max. given): '*Helped with quantification, met HMRC twice to explain. Volunteered some information*'.

(c) Giving 30% (max. given): '*Provided information and documentation when requested and with no delay*'. access to records 30%, total 100%.

(5) *Penalty percentage* after 90% reduction applied to the penalty range of 35% to 70% (equating to 31.5% reduction) to arrive at the 38.5% penalty percentage.

(6) *Special reduction*: HMRC do not consider that there are any special circumstances.

100. The total PLR from tranche 4 is assessed at £2,718,896.55, and the penalty thereon at 38.5% is £1,046,775.17.

Appeal and review

101. On 13 April 2018, Delphi appealed the penalties to HMRC, and the review conclusion on 5 October 2018 upheld the penalties.

102. On 20 October 2018, Delphi appealed the penalties to the Tribunal. The appeal has been assigned to the complex category. On 29 July 2019, the Tribunal granted HMRC's application for the appeal to be heard in private due to the ongoing criminal investigations into Clavis.

Barraclough's evidence

103. The basis for raising the penalty assessments was set out in detail in Barraclough's view of matter letter of 17 January 2018, and followed by the two changes outlined in the cover

email attaching the Penalty Determinations of 23 March 2018. Barraclough's witness statement at para 21 sets out the foundation for there to be errors in the P35 returns submitted as follows:

> 'There is now agreement between the parties that the Scheme did not "work" in producing the expected tax saving and the settlement agreement reached reflects the agreed position that PAYE and NICs are due upon the [tranches of] payments made [to Herald].'

104. The basis for imposing the penalties is therefore that inaccurate returns were submitted as the amounts for PAYE and NICs per the settlement agreement were omitted from the P35 returns for the 2008-09 and 2009-10, and represent the PLR for Sch 24 purposes.

105. For tranches 1, 2 and 3, the inaccuracies were categorised as 'careless' because:

(1) Delphi instructed Tucker to review the Scheme, and Tucker's letter of 7 August 2008 set out his view of the Scheme and its strengths and weaknesses.

(2) Tucker highlighted several weaknesses of the Scheme, including five specific areas of risk, and explained that 'aggressive tax planning will always be open to attack from HMRC'.

(3) Tucker went on to state that not only could he not formally recommend the Scheme but that he recommended the appellant, before entering the Scheme, to seek independent counsel's advice on the Scheme.

(4) HMRC's published guidance on Schedule 24 penalties CC/FS7a sets out what HMRC consider to be 'reasonable care', including if a taxpayer is unsure, he must ask his accountant for advice and then once it is received, to follow that advice.

(5) It would appear that the appellant, by asking its accountant to review the Scheme, was unsure about the use of the Scheme. The appellant's adviser gave it clear advice which Officer Barraclough paraphrased as:

> '… the Scheme is currently and will likely continue to be investigated by [HMRC], that there are a number of other potential weaknesses to the Scheme and that to check the merits of the Scheme, they should seek independent counsel's advice outside those who were to benefit from the appellant's use of the Scheme.'

(6) HMRC rejected the appellant's explanation (as understood by Barraclough), given at the meeting on 16 February 2018 that Tucker's advice 'was merely a professional disclaimer', and that 'no weight could be attached to that advice'.

(7) For the Scheme to work in theory, a genuine independent review of the appellant by a human resource company as the supposed service provider was required. For the first three tranches HMRC accepted that Herald Resource did undertake a review.

(8) Whilst HMRC are unaware of the content of the discussions between Herald and Delphi, there was sufficient information held to suggest that some form of review had taken place, even if the report for the third tranche was word for word (subject to the amount) identical to the report of the second tranche.

(9) HMRC therefore concluded that for the first three tranches, the culpability is attached to the failure to follow the advice provided to the appellant by its accountant, who had highlighted the weaknesses of the Scheme, and was 'careless' within the meaning of Schedule 24.

106. For tranche 4, the inaccuracy has been categorised as 'deliberate' because:

(1) The appellant has provided information to suggest that a meeting took place on 27 October 2009 between Delphi and David Cowen (a director of Clavis) in relation to the appellant's remuneration planning.

(2) The review on 27 October 2009 was the third review by Herald in 13 months. The draft report of the review by Herald Resource included a recommendation of a bonus of £1m gross per director with an invoice amount of £3m. These figures were detailed in the signed reviews of each director on 27 October 2009 by Cowen.

(3) On 31 October 2009, (after Cowen's review), Langran emailed Cowen stating that Delphi would like to put £5.4m through the Scheme, even though Delphi did not have sufficient cash reserves to make the payment. In relation to Langran's email to Cowen, Barraclough stated in evidence that '*the predominant weighting was attached to*' this email as '*the instruction to the avoidance scheme*' in assessing the penalty for tranche 4.

(4) The instruction to Herald did not take place until 3 November 2009.

(5) Delphi agreed with Clavis that they would make one payment of £2.7m on 23 November 2009. After fees, the balance would be loaned back immediately to Delphi's directors to allow reintroduction to Delphi to provide the funds to make the second payment of £2.7m on 3 December 2009.

(6) In directing Herald through Clavis the amount by which the directors wished to be remunerated, the appellant was aware that an independent review of the appellant did not take place. It is HMRC's position that the appellant was simply determining the amount by which the directors wished to be remunerated through the Scheme.

(7) The appellant had already used the Scheme three times and so would have been familiar with how the arrangements should work. For the fourth tranche, the documents show that it was the appellant and not Herald Resource which determined how much was to be paid, but the transactions were still presented as if the appellant had followed the correct steps. The appellant would have known what had happened, and this is why HMRC consider the fourth tranche differently from tranches 1 to 3 when considering the behaviour that led to the loss of tax, and have classified it as 'deliberate'.

107. Barraclough's evidence as respects the tranches is as follows:

(1) In cross-examination regarding whether a 'genuine independent review' took place for tranche 4:

> 'A: … my view is that if a genuine independent review of the company was to take place, the directors, after providing all the information, would not then have to tell the entity how much they wanted to be rewarded.'
>
> 'A: … if you know that 90% is going into an EBT, you can sugarcoat it or cover it with an invoice, however you like, but that it is avoidance, is it not? It is smoke and mirrors. … (2/166/3)

(2) In cross-examination on whether Herald not controlled by Delphi:

> Q: … Delphi did not control Herald, did it?
>
> A: They instructed Herald, but they did not legally control it.
>
> Q: They did not control Clavis?
>
> A: … no, because they are an independent company per se, but they take instructions on avoidance schemes … Delphi would not have put £10 million in if they did not think they were going to get it back.
>
> Q: You might think that the trustees who operated the trusts, they were independent as well. They were not under the control of Delphi, were they?

A: No, but would Delphi have put the money into the trust if they did not think they were going to get it back?

Q: … If you get it back in the form of a loan, then what you have is a loan, is it not?

A: Well, you have money from an EBT and you always knew you were going to get that. The whole point of entering into the tax avoidance scheme is to take money out of the company without paying tax.'

(3) In response to the Tribunal's question on Barraclough's understanding after the judgment of Hose of Lords in *Dextra* [2005] UKHL 47 in assessing tranche 4:

Judge: … you said your understanding is the entry into this scheme at this point in time, 31 October 2009 [i.e. email to Cowen to make £5.4m contribution], is post-Dextra and your understanding of Dextra is 2006. … in what ways was this not the same as Dextra in your understanding? (2/171/8)

A: Yes. My understanding of the judgment of Dextra was that entry into an EBT was classified as a potential emolument at the point in which the moneys were allocated … that the contributions were categorised as a potential emolument that did not give rise to PAYE and NIC whilst no CT deduction was taken. The moment a CT deduction is taken by the corporate, it changes the nature of the contributions, changing them from a potential emolument into an emolument, and therefore subject to PAYE and NIC by the employer at that point.

(4) To the Tribunal's question of Barraclough's understanding of the Clavis Scheme being different from the 'standard' EBT or *Dextra*:

A: So, this scheme involves the payment of an invoice for services to be provided as a way to try and get round the element of not being able to claim a CT deduction and change in the potential emolument to an emolument. Therefore, this scheme takes a CT deduction immediately and does not operate the PAYE and NIC. My understanding of the invoice is that it should be for services rendered to get round the element. However, my view is that if a genuine independent review of the company was to take place, the directors, after providing all the information, would not then have to tell the entity how much they wanted to be rewarded.

(5) To the Tribunal's question as to why the legislative exemption would not apply:

'A: … my view is that the exemption would apply if the entire amount was for a service to be provided to the company. However, this scheme purports for a service to be provided, but it is known all along by all parties that 90% of the money will always be redirected to the directors and that the independent element fee, the 10%, is the only bit that would fall under that category. It is my view that the directors know that before entering into the scheme because they would not enter into a scheme paying millions of pounds in fees if they did not always know that they were going to get their money back at the end.'

(6) In response to Tribunal's question on tranche 4:

'Judge: On the point about no genuine evaluation before the quantum of that invoice [for tranche 4] is set, can you expand on your meaning of "no genuine evaluation"? (2/174/12)

A: ... So, for the first three tranches, although I think there is paperwork to show an evaluation takes place, I think it is questionable to whether one does, as the directors appear to know how much money is going to go into the

scheme and therefore get back. However, on the evidence we have available, we cannot disprove that there was not an evaluation. …

(7) Reply continued to the Tribunal by contrasting tranche 4 with the other tranches:

> 'A: … For the first three tranches, I do not have the evidence available to demonstrate that the reports did not in some way take place. Whether they were worth the paper they were written on, being identical from each other, is a question that could be asked. …. For the final and fourth trance, after the veneer of an independent review taking place and the returns being sent to the reviewers, for the company then to instruct the reviewers how much they wish to be rewarded, when the whole premise of the scheme is that an independent review has to take place, that is why I leant towards deliberate behaviour, because they knew all along that they were going to get their money back and that an independent review was not taking place into the company as they were able to decide how much they wished to be rewarded.'
>
> Judge: So, … in the fourth tranche, … you were placing reliance on this email [of 31 October 2009] where the quantum would appear to have been by instruction of the kind that has come from the directors?
>
> A: Yes.
>
> Judge: Rather than supposedly a review evaluation having taken place?
>
> A: Exactly, madam, yes.

108. In cross-examination, Barraclough was referred to the fact that the enquiries into Delphi's use of the Scheme were conducted under Code of Practice 9 ('**COP9**') for 'investigations where [HMRC] suspect tax fraud' and Delphi directors were served a copy of the COP9 procedure. The letters were issued by Barraclough's predecessor in July 2016 because HMRC had serious concerns as to whether the appellant had been involved in fraud. By reference to HMRC's Fraud Civil Investigation Manual at 202050, a COP 9 letter cannot be issued to a company and hence, Delphi's directors were the recipients of the COP 9 letters. Furthermore, the COP 9 letter applied to both the directors' tax position and that of the appellant as it was Delphi which was the company in which the directors were involved.

109. Aspects of Barraclough's evidence in cross-examination significant to the appellant's case are summarised below.

(1) The enquiries into the CT returns were concerned with the CT deductions:

> Q: And we have already agreed the main objective of these arrangements is, in the case of an EBT contribution, to get a Corporation Tax deduction?
>
> A: Yes.
>
> Q: [Referring to the letter to open the CT enquiry] … So this was the enquiry, and [the letter] makes it plain, does it not, that it is enquiring into the company's tax return?
>
> A: I guess because the expense that was incurred was within the directors' remuneration, then it would be right to open a Corporation Tax into that directors' remuneration expense claimed when there is no equivalent PAYE and NIC operated on that amount.

(2) The case of *Dextra* and the enquiry being on CT deductions:

> Q: So, exactly the same sort of challenge that was successful against the taxpayer in *Dextra*, query the CT deduction?
>
> A: It is querying the entire amount because at that stage, you would only have the return. Therefore, you cannot make a decision, but using this, it is a mechanism to open an enquiry into the expense claim.

(3) That there had been no PAYE enquiry opened:

Q: Was there ever a PAYE inquiry into this company?

A: No, because assessments were issued.

(4) That the first mention of PAYE and NICs being potentially in point was in 2010:

Q: [Referring to the letter from Specialist Investigations in July 2010 being sent] a year after the inquiry has been opened into the CT deduction, and this is the first mention, is it not, of PAYE and NIC?

A: … does it not refer to directors' remuneration, though, as the sole focus of the inquiry?

Q: This is the first reference to PAYE and NIC, is it not?

A: It is, but remuneration is subject to PAYE and NIC.

(5) On aspects of the letter from Tucker to Delphi of 7 August 2008:

(a) Q: … that paragraph opens up with, "Whilst the scheme seems to be most effective" That is quite a strong endorsement, is it not?

A: – you are reading that bit and I am reading the aggressive tax planning bit.

(b) Q: [on risks] it does not say anything about the Income Tax side failing. That is not identified as a risk. The risk that is being identified … is should the Corporation Tax planning fail. He does not go on to say that the Income Tax planning possibly fail …

A: But is that not an acknowledgement that the Income Tax side could fail? He would not highlight if it was not a risk.

(c) Q: … That is telling the client that they are buying an argument. He is saying that he thinks it works, but be warned, if you go in for this, you are likely to have an argument from HMRC. That is what that sentence means, does it not?

A: I read that to be that it is aggressive tax planning.

110. Officer Barraclough was extensively cross-examined on the state of authorities in relation to contributions made to an EBT during the tax year 2008-09, and he accepted or agreed that:

(1) The main objective of the Arrangement was to enable a contribution into an EBT to get a Corporation Tax deduction.

(2) If there was a contribution to an EBT and a loan from the EBT to employees, the state of authorities meant that 'there would be no PAYE and NIC at that time'.

(3) The outcome in *Dextra* where the company sought a tax deduction as well, Barraclough accepted, at least in part, that taxpayers could rely on *Dextra*.

(4) The mischief which the Revenue would be hoping to cure was to work round *Dextra*, and the Scheme was trying to circumvent the effect of the decision of the House of Lords in *Dextra* 'to allow for a CT deduction taken immediately'.

(5) The arrangements in the present case were different to a 'standard EBT', but he could not explain why if in an ordinary standard EBT, it was permissible not to operate PAYE and NIC, that in the present case, PAYE and NIC needed to be operated.

(6) *Sempra* had been decided in 2008 and the view was that with regard to the PAYE element, the Revenue had not succeeded at that point in time in the way it had in *Rangers*.

(7) It was 'not clear that the writing was on the wall for *Rangers*' because the Court of Session judgment was not until November of 2015.

Witness evidence from Tucker and Langran

111. The oral evidence of the appellant's witnesses focussed on various aspects that came to be considered as pivotal by HMRC in assessing the degrees culpability as 'careless' for tranches 1 to 3, and 'deliberate' for tranche 4.

Langran's evidence on instructing Tucker

112. Mr Langran's evidence emphasised the evidence of the network of existing contacts who led Delphi to be acquainted with the Clavis Arrangement, which included:

(1) McNally, who became Kelland's financial adviser from around 1990, and had visited Delphi's premises 'fairly regularly to meet [Kelland] since 2001'.

(2) McNally in turn introduced Mr Forbes of Forbes Accountants, a member of the Probiz Network. In a meeting in early July 2008, Forbes 'described the Scheme to [Langran and Kelland], and Langran thought it was 'inherent' in Forbes' explanation that he recommended the Scheme, but Langran was conscious of getting Forbes' advice checked by 'somebody I know and trust'.

(3) Langran stated in re-examination that he could not recall the exact words of Forbes' advice, but that: 'I am sure he would have said something along the lines of the scheme would offer one a chance to avoid tax in a legal manner'.

(4) Delphi's directors approached Tucker to carry out due diligence, because Tucker (in Langran's words) is 'an extremely cautious man'.

(5) Langran stated in evidence that he thought Delphi would have paid Dickinsons for Tucker's advice.

113. The corroborated evidence on the due diligence carried out by Tucker on Delphi's behalf is summarised as follows:

(1) Tucker visited the trustee's office in Jersey and attended at least two meetings with Clavis in July and August 2008. (It was accepted by Officer Barraclough that Clavis did hold themselves out to be specialist tax advisers.)

(2) On 31 July 2008, Tucker gave his understanding of the Clavis Arrangement to Delphi's directors verbally, and no concerns were expressed during this meeting.

(3) On 4 August 2008, Tucker was given sight of the 6 tax opinions by Andrew Thornhill QC provided to Clavis.

Listing of risks in advice letter

114. The letter of 7 August 2008 was delivered in person to the three directors of Delphi during a meeting which took place on the same day. In relation to the listing of risks in the letter:

(1) Tucker stated in evidence that: 'my recollection is that we did go through the detail of my letter at that meeting'; he also confirmed that the advice he gave orally, such as during the meeting of 7 August 2008, would not have been phrased differently from the advice given in the letter.

(2) Langran confirmed in cross-examination that the directors 'were taken to various parts of the letter, as you would expect'; and Langran understood Tucker's advice as indicating that '[Tucker] believed the scheme worked from a legal and tax perspective'.

(3) When asked about the references to the Scheme being 'most effective' and being 'aggressive tax planning' at the same time, Tucker replied:

> 'My letter was setting out the merits of the scheme and doing, if you like, comparisons to other arrangements and EBTs had been around for a long time

and were not, as far as I was aware at that time, considered as aggressive tax planning.'

(4) As author of the advice, Tucker admitted that obtaining a second counsel's opinion would not alter the risks identified in the advice letter at all.

(5) As to the real risk, Tucker was asked in re-examination:

> Q: Would it be right that the real risk is that Mr Thornhill's advice, Clavis's advice and your understanding were wrong, is that the risk that independent counsel's advice would perhaps help the company with?
>
> A: Yes, it would.

The second opinion caveat

115. In relation to Tucker's statement in the letter of 7 August 2008, Mr Sherry's submissions rely on what is referred to as Tucker's 'second opinion caveat' as underlined below:

> 'My normal and usual advice for any such scheme would be to ask that another Counsel Opinion from a barrister other than the original one is obtained <u>if the Promoters of the arrangements are prepared to permit this</u>', the advice to seek a second opinion was given with a caveat as underlined.'

116. The following aspects of Tucker's evidence are relied on in Mr Sherry's submissions:

(1) In Tucker's witness statement, he stated that disclosure of the full 'bible' of documents to another counsel was unlikely, as evidenced by the Non-Disclosure Agreements ('**NDA**') demanded by both Probiz and Clavis.

(2) When asked during examination in chief about the promoters of the arrangements permitting as a second counsel's opinion on the merits, Tucker confirmed:

> 'At that point, I had not asked Clavis whether they would release the documents for review by another barrister, and in any event before they would allow me to see them I had to sign a confidentiality agreement which restricted the release of these documents to anyone else.'

(3) When asked by the Tribunal the wording used in relation to 'my normal and usual advice', Tucker confirmed: "That would be the firm's sort of policy, and that would have been something which I would be asked to include in such a letter'. When asked about the aim of a second counsel's opinion, Tucker stated:

> 'In terms of asking for another barrister to look at the case, it struck me that with the amounts involved it would give additional defence against any attack that the clients had been negligent in entering into such arrangements.'

(4) When asked by the Tribunal further in relation to his advice to seek a second opinion, Tucker replied:

> 'A: … Although in hindsight and the like, I think it is highly unlikely that any barristers would have come out with an opinion at the time that those arrangements would fail. But my view was that the technical side of the arrangements was fairly robust.'
>
> Q: So, if it is fairly robust, why would you consider it normal good advice to ask your clients to seek second opinion?
>
> A: Broadly because of the amounts involved, just to give them additional comfort.
>
> Q: Additional comfort for what?
>
> A: That the arrangements would work and they would not be subject to challenge or attack.'

(5) Langran stated in evidence that he understood the second opinion caveat to mean:

> 'A: … in [Tucker's] opinion there was no way, having had to sign all the non-disclosure agreements, any other person would be allowed access to the information…. What I am saying is he told us that he did not think Clavis would release the opinion to any other barristers, tax counsel to examine their scheme because of NDA.'

The minutes of meeting supposed to be on 23 June 2008

117. In cross-examination, Langran was asked whether Delphi was 'doing very well' in early to mid 2008 before the financial crisis. He replied that Dephi 'was punching well above its weight in terms of its competition' considering its size. When asked if he could remember the minutes of meeting on 23 June 2008, which recorded Langran and Kelland resolved to set aside £1.5m for provision of rewards for key employees, Langran said he could not remember.

118. In terms of chronology, the minutes of a board meeting (Langran and Kelland present) supposed to have taken place on 23 June 2008 recorded that it was proposed that Delphi 'should make provision within its accounts for the period ending June 2008 for the sum up to £1,500,000 to be set aside to provide rewards to key employees for their working during the period'. This meeting was supposed to have taken place in June 2008, before any of the events involved that led to Delphi being introduced and subsequently entering into the Scheme.

On the resolution to set aside £1.5m

119. Tucker's evidence made reference to a 'Companies Act requirement of having a minute in place' close to the company's year-end to show that it would make provision in accounts to reward employees, and that the Scheme would require the company having to 'establish a remuneration committee' with two directors of the company who could approve any steps taken within the arrangements.

120. The context in which Tucker made this reference of a minute having to be in place before the year-end was 'rather odd' (per HMRC) since Tucker was <u>*not*</u> specifically referred to the minutes of 23 June 2008 but was being cross-examined on the logistics of implementation of the Scheme in relation to the 'bible' of documents.

> 'A: [The bible] set out the split by which the arrangements would work, starting with the initial exchange of letters with Clavis/Herald. There was *obviously a requirement at that time because it was close to the company's year end, for the company to cover its Companies Act requirement of having a minute in place of the company to show* that it would make –
>
> Q: Sorry, I need to pause you here. The company's year end is 30th June, is it not? You said it is close to the company's year end so you were there meeting on 4th August, and I am asking myself, in what sense is it close to the company's year end?
>
> A: I think I need to refresh my memory on the particular document that has been referred to. The actual bible of documents which set out the basis on which the remuneration report would be prepared required a visit by representatives of Herald resources, the HR company, to carry out an evaluation, that subsequently after that report was prepared, it would be sent to the company as part of it. *I might not have these all in the right order. The company had to establish a remuneration committee so that there were two directors of the company who would approve any steps taken within the arrangements.* Subsequent to that, the bible showed that there would be a trust set up in … Jersey, and sub-trusts for the individual directors …(Italics added)

Tranche 4: the basis for change to £5.4m

121. In relation to the communications between Tucker and Langran for tranche 4 and the email from Langran to Cowen of 31 October 2009 to which 'predominant weighting was attached' by Barraclough, Tucker's explanation on being examined in chief was to say:

> 'Mark Langran had phoned me and the discussion related to what the profits of the period were, and the objective of these arrangements, as I understood it, were to enable profits to be extracted and the latest management accounts had profits in excess of that period, and that was the way the discussion went. It was not a recommendation of the amount; it was setting out the level of the profits for the period, which could be sheltered should the directors wish to make a payment in that order of magnitude.'

122. In cross-examination, Tucker's replies to questions included:

> 'Q: … is it not right that the only reason the figure in Clavis's report changes from the one you see in the draft is Mr Langran's email where he communicates a higher profit figure?
>
> A: I would say no, because accounts were also communicated.
>
> Q: Right. So the accounts are sent in on 30th October, and then one day later, we are told, … "Can we do 5.4 million instead?"'
>
> A: … I was not party to how Clavis operated internally, I would not have thought they would have produced a report or varied a recommendation without sight of some accounts to actually support what they were doing.'

123. Tucker's replies in re-examination by Mr Sherry on Langran's email of 31 October 2009 to Cowen that 'we should do £5.4 million' were as follows:

> Q: So, do you want to revisit your answer that it is likely that the figure changed because of the second email [of 31 October 2009]?
>
> A: (Pause for reading) I do not think I do. The evaluation depend[s] on the accounts figure.
>
> Q: … but previously you said you thought it was likely because of Mr Langran's email on the 31st, saying "Can we do 5.4". Are you now saying it is because of the accounts forwarded on the 30th? …
>
> A: Definitely that would have been the basis upon which Mr Cowen would have been amending or updating the recommendation.
>
> Q: Which, the accounts or the email of 31st?
>
> A: The accounts.'

124. When asked by the Tribunal in relation to Langran's email referring specifically to 'Have spoken to Peter tucker and he thinks that we should do £5.4m', Tucker reiterated that:

> 'We would have had a conversation and it would have been based on the fact that the accounts profit was in excess of that amount, and Mr Langran would have asked whether such an amount could go through the arrangements. That would have been the nature of the discussion. I was not setting it, and the accounts of the Company would have disclosed profits certainly of that order of magnitude and considerably more.'

125. When asked by the Tribunal in relation to the timing of tranche 4 being in November and December 2009, and therefore took place after year end date of 30 June 2009, Tucker's explanation was that the £5.4m contributions to Delphi's EBT would have been included in the accounts of June 2009 as accruals, as expenditure that was related to the accounting period 30 June 2009 and met after the year end.

126. Mr Langran's evidence in relation to the email of 31 October 2009 was to refute that the email was an 'instruction' to Clavis/Herald of the amount for tranche 4; rather it was to provide Clavis with Delphi's 'available profits' for the period. In cross-examination, Langran stated:

> A: '… When we first came to discussing this we had, well, we still only had the same amount of money, whatever it was £3 million or £2.7, … as available profits and the word here is "available", we had a lot more money due to us, in around three months' time. Then Clavis, I do not know how they came to hear about this, but whatever, said "okay, if you have available profits being including the further forward cash flow, you can do this loan back mechanism". That is why it changed.'
>
> […]
>
> A: 'The available profits were always £5.4 million, as dictated by 30th June accounts. The amount of money available for us to pay an invoice was significantly lower because of the cash flow issue. We had no idea, … that we could do this loan back arrangement so Clavis, David Cowen, …, he knew that the available profits per se, as per the accounts, having done his review, were £5.4 million but he knew we could not – I guess he knew we could not pay that amount of money. He then came up with the – he told Peter we could then do the loan back thing.'
>
> […]
>
> A: 'I think you are trying to tie me up in knots. The suggestion never came from Mr Cowen "we should do £5.4 million". The amount of money is determined by how much money Delphi Derivates made; Mr Cowen had no idea about that. We had to instruct him.
>
> Q: You instructed him that you got £5.4 million profit?
>
> A: Yes, the accounts showed that and/or we had to tell him, yes.

127. Langran went on to clarify that despite Herald carrying out an evaluation of Delphi's key employees and to provide a recommendation on potential rewards, unless Delphi provided information or accounts on the available profits, the review exercise would be 'pretty hopeless' if the reviewer was kept in the dark as to 'the available pot' that Delphi could afford to pay into Delphi's EBT.

Accounts for the period 30 June 2009

128. The report and accounts Delphi for the year ended 30 June 2009 was exhibited with a manuscript note: 'e-filed 9/6/10'. The profit and loss account showed the following figures between the two years:

	30 June 2009	**30 June 2008**
Turnover	15,290,851	7,512,597
Less: Cost of sales	(1,425,722)	(1,271,147)
Gross Profit	13,865,129	6,241,450
Less: Administrative expenses	**(12,785,918)**	**(6,187,686)**
Add: Operating income	14,500	14,550
Operating profit	1,093,711	68,314

129. The Directors' report on review of the business stated:

> 'Turnover has increased by £7.8m compared to last year as a result of the uncertainty in the market due to the global financial crisis. The directors were

> able to use their expertise to expose [sic exploit] the volatility in the market and generate substantial gains from the future prices they had in place. The gross margin achieved was 90% in comparison to 83% last year, generating a gross profit of £13.9m.

130. The Notes to the accounts show the following relevant to tranche 4:

(1) 'Administrative expenses', of which 'Directors emoluments' was at £11,222,034, (£4,459,025 in 2008) with the emolument to the highest paid director being £3,740,678.

(2) The 'Analysis of net funds' showed an opening net funds of just over £1m and a closing balance of £2.277m, of which £1.6m was cash at bank.

(3) Notes to the Balance Sheet as respects 'Creditors falling due within one year' included Accruals of £5,558,671, of which £5.4m would be for contributions made to Delphi's EBT in November and December 2009 (after year-end).

P35 returns for the relevant years

131. Delphi's P35 returns constituted the 'inaccurate' documents furnished to HMRC on which the Sch 24 penalties are founded. The Tribunal is not provided with a copy of these P35 returns as HMRC have not retained them; nor has the appellant kept a copy for its own records.

132. Mr Tucker's witness statement states at paragraph 51 that he has not retained copies of the P35 returns as such records would only be retained for six years. In cross-examination, Mr Tucker gave his reasons for the basis of preparing the said returns.

> 'Q: … you mentioned … that the PAYE returns were prepared on the basis of the advice received from counsel/Clavis. So, I take it that when preparing those returns you were relying on their advice that no PAYE and NIC liability arises; is that correct?
>
> A:… I did not at the time consider that PAYE applied to such payments, and our tax department produced the P35s based on the regular salary payments and the like which had gone through over the course of the year.'

133. On being further cross-examined on the P35 return preparation, Tucker was asked whether he was 'content to rely on what counsel and Clavis have advised', and replied in the affirmative. As to Langran's evidence, he confirmed that he and his fellow directors 'were relying on Dickinsons to get it right', and that 'they are professional accountants; we are relying on them to do what they are paid for'.

The Loan Charge Review: the Morse Report

134. The appellant lodged the report entitled '*Independent Loan Charge Review: report on the policy and its implementation*' by Sir Amyas Morse published in December 2019 (the '**Morse Report**'). The executive summary states as follows:

> '1.18 HMRC's position at the time was also not supported in the courts. In 2002's *Dextra Accessories v HMRC*, the Special Commissioners found that the employee benefit rust (EBT) scheme under consideration achieved the "outcome promised when they were being marketed". While HMRC was eventually successful in appealing narrower arguments around corporation tax in the House of Lords the question around whether the loans were income was not considered further. It took until 2017 – subsequent to the announcement of the Loan Charge – for *Dextra* to be overruled by the Supreme Court, which concluded that it had been wrongly decided.
>
> 1.19 While loan scheme use was growing in early 2000s, HMRC had not yet received judicial support that loan schemes did not work, and that loans should be taxed as income. Taxpayers did not, therefore, have to accept HMRC's

view. Evidence received by the Review consistently supported the view that such schemes were not seen as being aggressive tax avoidance at the time.'

135. In respect of HMRC's published view, the Morse Report states at para 1.25:

> 'Form 2009 onwards, HMRC also published its view in specialist Spotlight articles, which reach a limited number of agents and tax professionals. Evidence about the readership of relevant Spotlights from the time is not available, but in 2015 (when data is available) the four articles published to that point received an average of just 520 views each. The Review therefore concludes that both individual scheme users, and those using schemes through their employers, would likely have continued to be largely unaware of HMRC's position at this time.'

136. The legal position at the time is summarised in the Report as follows:

> 'The legal position at the time also remained unclear, with the courts not accepting HMRC's view of the tax consequences of loan schemes. The 2008 decision in *Sempra Metals v HMRC* rejected the government's arguments that loans made by an employer's EBT were subject to income tax. The case was not appealed to the higher courts, which may have given scheme users at the time a degree of comfort that the legal position was settled. As had been the case with *Dextra*, it would take until 2017 for the Supreme Court to conclude that *Sempra* had been wrongly decided.'

HMRC's Spotlight 5

137. For the respondents, HMRC's publication entitled *Spotlights* (published on 5 August 2009 and archived 2 November 2009) is lodged to illustrate the views on that tax position for the type of Arrangement entered into by Delphi. Spotlight 5 in this publication states as follows:

> 'Spotlight 5: **Using trusts and similar entities to reward employees –**
> PAYE (Pay As You Earn) and National Insurance contributions (NICs), Corporation Tax and Inheritance Tax
>
> We're aware that companies have been seeking to reward employees without operating PAYE/NICs by making payments through trusts and other intermediaries that favour the employees or their families. The arrangements usually seek to secure a Corporation Tax deduction, as if the amounts were earnings at the time they are allocated, and also defer PAYE/NICs or avoid them altogether. *Our view is that at the time the funds are allocated to the employee or his/her beneficiaries, those funds become earnings on which PAYE and NICs are due and should be accounted for by the employer.*
>
> *In addition our view is that an Inheritance Tax charge may arise on the participators of a close company*. Unless the participators are excluded beneficiaries and have not had funds applied for their benefit, such as the receipt of a loan, a charge to Inheritance Tax arises on participators of close companies at the time the funds are paid to the trustee by the close company. Relief is only available to the extent that a deduction is allowable to the company for the year in which the contribution is made. Later payments of earnings out of the trust that may trigger a deduction to the company would not qualify for relief.
>
> Participators affected by this may need to self-assess a liability to Inheritance Tax. There is further technical advice on Inheritance Tax on Contributions to Employee Benefit Trusts on the HMRC internet site.
>
> We are actively challenging examples of such arrangements and considering legislative options to end further usage of these schemes.' (Emphasis in bold in original replaced by italics here.)

HMRC'S CASE

138. Ms Choudhury's submissions, including those in writing of 26 pages, have addressed the issues arising in this appeal under several headings. The respondents' case is summarised as follows, while the detailed aspects of submissions are considered in the Discussion part below.

(1) Following the Supreme Court's decision in *Rangers*, it is now common ground that the amounts allocated to the directors' respective sub-trusts are earnings for PAYE and NIC purposes.

(2) The appellant's PAYE returns for both years did not include any liability for PAYE or NICs in respect of these amounts into sub-trusts, and were therefore inaccurate.

(3) For the 2008-09 return, HMRC submit that the inaccuracy was 'careless', and for the 2009-10 return, the inaccuracy was caused by 'deliberate' behaviour.

(4) Notwithstanding the different categories of culpability as concerns the two years, Ms Choudhury's submissions on 'careless' behaviour would appear to be generic to both years, and underpin the basis for imposing the penalties, and that the inaccuracy for the year 2009-10 was an escalation from 'careless' to 'deliberate' (due to the behaviour as reflected by the manner in which the fourth tranche was implemented).

(5) The behaviour which caused the inaccuracy falls to be judged by the standard of a prudent and reasonable taxpayer in its position: *Collis*[1].

(6) HMRC submit that the appellant's reliance on (a) the 'prevailing practice' at the time, (b) the advice received from Tucker, and (c) the advice received from others was 'insufficient' for holding that the appellant 'was not careless'.

(7) In relation to the fourth tranche, HMRC submit that 'there is insufficient evidence that an independent review took place' prior to the determination of the amounts to be allocated to the Delphi EBT. In the light of the sequence of events leading to the doubling of contributions from £2.7m to £5.4m, HMRC submit that 'the appellant's directors must therefore have known that the report provided a predetermined outcome', and that 'its only purpose was to provide a smokescreen for the benefit of HMRC'.

APPELLANT'S CASE

139. Mr Sherry submits that the question for the Tribunal is whether HMRC have discharged the burden of showing that the appellant acted carelessly 'in the preparation and submission of the returns' which turned out to be inaccurate.

(1) Tucker was responsible for Delphi's participation in the Scheme from a tax advice and compliance perspective. Dickinsons 'prepared the Corporation Tax returns, ran the payroll of the Company and completed the end of year forms P35, P11Ds as appropriate'.

(2) It is not sufficient for HMRC to demonstrate that the appellant was 'careless' in entering into the Scheme, but this is indeed the carelessness alleged by HMRC.

(3) Even if it could be established that the appellant was 'careless in deciding to enter into the Scheme, that has no bearing, no causal connection with, the completion of the P35 returns'.

(4) Far from the Revenue establishing that the appellant was careless in the submission of the P35 returns, the unchallenged evidence is that the appellant 'took all due care in the completion and submission of the same', including the engagement of Dickinsons, 'a

[1] *David Collis v HMRC* [2011] UKFTT 588 (TC).

perfectly capable and competent firm of Chartered Accountants' to prepare and submit the returns on its behalf.

(5) As to the 'deliberate' penalty in relation to tranche 4, Mr Sherry again emphasises that 'it is not sufficient for the Revenue to demonstrate that the appellant was careless in entering into the Clavis Arrangements', nor is it sufficient for the Revenue to show that the appellant entered into tranche 4 of the Clavis Arrangements knowing that the tranche had not been executed as it should have been.

(6) Even if it could be established that the appellant knew that the Scheme had not been implemented in the manner purported, there is 'no casual connection between that knowledge and the completion of the P35 returns'.

(7) It is the appellant's case that the P35 returns as submitted was in accordance with the 'prevailing practice', and the advice received at the relevant time.

DISCUSSION

Issues for determination

140. Having regard to the factual matrix of the case and the parties' submissions, we determine the appeal by addressing the issues arising in the following order:

(1) Are the penalty notices valid in terms of meeting the relevant time limit?

(2) Were the P35 returns for the years 2008-09 and 2009-10 inaccurate?

(3) Were the inaccuracies 'careless' pursuant to para 3(1)(a) in respect of all tranches?

(4) Was the inaccuracy 'deliberate' pursuant to para 3(1)(b) in respect of tranche 4?

Burden of Proof

141. It is common ground between the parties that HMRC bear the legal burden of proof in relation to a penalty assessment, by reference to the legislative framework under Sch 24. However, the general principle that the party which asserts must prove is not displaced (even in a penalty case) in relation to a fact at issue. A party who fails to discharge the burden of proving the fact at issue on which it seeks to found its case to the required standard will lose on the issue in question. The standard required is proof on the balance of probabilities.

The appellant's reliance on Brady

142. In respect of burden, Mr Sherry has referred the Tribunal to *Brady*[2] wherein the Revenue raised assessments in relation to sums found to have been wrongfully diverted from the taxpayer companies' funds, and notified the taxpayer companies that a number of discovery assessments would be issued 'on the basis that there has been fraud, wilful default or neglect'. The taxpayer companies argued that the burden of proof therefore rested on the Revenue, given that the case against them was fundamentally one of fraud.

143. Mustill LJ in *Brady* observed that the reference to 'fraud' in the notification letter in *Brady* could have been an intimation that the Revenue were proposing to claim lost tax out of time under s 36 of Tax Management Act 1970 (**'TMA')**, by proving fraud, or to use an in-time assessment based on fraud, wilful default or neglect as a springboard for subsequent out-of-time assessment under s 39. Had the Revenue brought the claim to lost tax on the basis of fraud in front of the commissioners, it would have been clear on general principle that the burden would rest on the Revenue. However, before the commissioners, the Revenue made no attempt to advance a case under ss36 and 39, and explained that the reference to 'fraud, wilful default

[2] *Bardy (Inspector of Taxes) v Group Lotus Car Cos plc and another* [1987] 3 All ER 1050, Dillon, Mustill and Balcombe LJJ at the Court of Appeal. This authority, while referred to extensively in the appellant's closing submissions, is not included in the joint bundles of authorities (original or supplemental).

or neglect' was to protect the Revenue's right to interest under s 88. The case was heard on 'an ordinary *Haythornthwaite*[3] basis' for discovery assessments, where 'the only question in issue was whether the taxpayer companies could establish that the assessments were wrong'. Mustill LJ remarked at 1058 of *Brady* that the commissioners 'had no ground for approaching their fact-finding functions on any other basis than that it was for the taxpayer companies to make the running'.

144. Remarking on the fact that the formal burden of proof was not assumed by the Revenue if the contrary has not been asserted by the taxpayer companies, Mustill LJ continued at 1059 in *Brady* as follows, (and is a passage relied upon in Mr Sherry's submissions):

> 'It is commonplace that, if there is a disputed question of fact admitting of only two possible solutions, X and Y, with party A having the burden of proving X in order to establish his case, if A produces credible evidence in favour of X and B produces none in favour of Y, it is very likely that A will win. B must therefore exert himself if he wishes to avoid defeat. But this does not mean that B ever has the burden of proof.
>
> […] This does not mean that, by traversing the taxpayer companies' case, the Revenue have taken on the burden of proving fraud.
>
> Naturally, if they produce no cogent evidence or argument to cast doubt on the taxpayer companies' case, the taxpayer companies will have a greater prospect of success. But this has nothing to do with the burden of proof, which remains on the taxpayer companies because it is they who, on the law as it has stood for many years, are charged with the task of falsifying the assessment.
>
> The contention that, by traversing the taxpayer companies' version, the Revenue are implicitly setting out to prove a loss by fraud, overlooks the fact that, in order to make good their case, the Revenue need only produce a situation where the commissioners are left in doubt. In the world of fact there may be only two possibilities: innocence or fraud. In the world of proof there are three: proof of one or other possibility, and verdict of not proven. The latter will suffice, so far as the Revenue are concerned.' (Sub-paragraphs added)

145. We have regard to the fact that Mustill LJ's comments on burden in *Brady* are to be read in the context of discovery assessments under s 29 TMA**,** where the taxpayer bears the burden of proving the contrary; otherwise the assessment stands good by virtue of the provision under s 50(6) TMA. *Brady* (1987) predates *Burgess & Brimheath*[4] as the authority that the Revenue bear the initial burden on the 'competence' and 'time limit' issues in a case of discovery assessment. Once the initial burden is discharged by HMRC, then the short points on burden we take from *Brady* in the context of discovery assessments are as follows:

(1) The burden of proof to displace the discovery assessment rests on the taxpayer throughout. Even if the Revenue has adduced evidence in response, that does not mean that the Revenue, by traversing the taxpayer's case, has taken on the burden of proof.

(2) In the world of proof, apart from the binary outcome of one or the other possibility, there is the third possibility of 'not proven' – that is to say, when the tribunal as the fact-finding body is left in doubt of the fact at issue.

(3) Further, if the Revenue produces cogent evidence or argument to cast doubt on the taxpayer's case, then the taxpayer will have a greater challenge in discharging the burden required to succeed in their case.

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[3] *Haythornthwaite and Sons Ltd v Kelly* (1927) 11 TC 657.
[4] *Burgess & Brimheath Developments Limited v HRMC* [2015] UKUT 578 (TCC).

146. The appellant's reliance on *Brady* seems to be suggesting that the burden on this appeal rests on HMRC throughout, and that even if the appellant produces evidence or argument to traverse the Revenue's case, that does not mean that the appellant is assuming the burden. Further, we understand that the appellant's reliance on *Brady* is to make the point that if the appellant produced evidence to cast doubt on HMRC's case, then the Tribunal is left in doubt of the fact at issue, and that HMRC would have a greater challenge to prove their case.

147. Notwithstanding our best attempt to discern the application of *Brady* to the appellant's case by transposing the parties in *Brady*, we remain puzzled as to how Mustill LJ's observations in *Brady* is supposed to assist the appellant's appeal. It is not just the need to transpose the parties, but more importantly, Mustill LJ's observations apply to a party having to *prove the contrary*. It is unclear how *Brady* is supposed to apply in the present case when the burden on the Revenue is not about proving the contrary.

148. Furthermore, it seems to us that the burden in a penalty appeal, while residing with the Revenue to establish the statutory conditions for a penalty to be imposable are met, and once the Revenue has discharged the burden, and if the taxpayer wants to avail itself of the defence under para 18(3) of Sch 24, then the onus reverses to the appellant: '*where P satisfies HMRC that P took reasonable care to avoid inaccuracy*'. It seems to us, by virtue of the express wording under para 18(3) of Sch 24, the relevance of Mustill LJ's observations in *Brady* on the issue of burden, if they are to apply in a penalty appeal, are apposite to the burden that is reversed on to the appellant to prove the contrary under para 18(3) of Sch 24.

Statutory wording of para 18(3) Sch 24

149. The documents that contain the inaccuracies are the P35 returns for the relevant years, and it is accepted that these documents had been prepared by Dickinsons as Delphi's agent. Paragraph 18 of Sch 24 entitled 'Agency' is directly relevant, and para 18(1) provides:

> 'P is liable under paragraph 1(1)(a) where a document which contains a careless inaccuracy (within the meaning of paragraph 3) is given to HMRC on P's behalf.'

150. Where a document contains a careless inaccuracy is given to HMRC on P's behalf, P is therefore still held liable to a penalty under para 1, unless sub-para 18(3) applies:

> '… P is not liable to a penalty under paragraph 1 … in respect of anything done or omitted by P's agent where ***P satisfies HMRC*** that P took ***reasonable care to avoid inaccuracy*** (in relation to paragraph 1) …' (Emphasis added)

151. The statutory wording of para 18 therefore directs the burden to be allocated as follows:

(1) Under para 18(1), HMRC have the burden to prove that there is a *prima facie* case that the P35 returns in question contain a careless inaccuracy; and

(2) By virtue of para 18(3), P (i.e. the appellant) has the burden to satisfy HMRC (and on appeal the Tribunal) that it took reasonable care to avoid inaccuracy.

152. In other words, if HMRC have met the burden in relation to para 18(1), then the appellant (without more) will be held liable to the careless penalty. The onus is then reversed onto the appellant to satisfy the Tribunal that it took reasonable care to avoid inaccuracy for the penalty to be discharged. To avail itself of the defence under para 18(3) of Sch 24, the appellant has to satisfy the Tribunal that it '*took reasonable care to avoid inaccuracy'*. The express provision under para 18(3) which places the onus on P is also in line with the general principle that the person who asserts must prove.

The absence of the definite article in para 18(3) Sch 24

153. We note the omission of the definite article in the statutory wording for para 18(3). While the inaccuracy in a particular penalty case is necessarily specific, and indeed para 3(1) for penalty categorisation refers to '*the* inaccuracy' throughout its wording, the definite article is noticeably missing in framing the defence available to P under para 18(3). The exact wording of the defence is: '*P took reasonable care to avoid inaccuracy*'.

154. The omission of the definite article, in our view, is not a slip in legislative drafting, but an intentional omission so that P can avail himself of the defence under para 18(3) without having to prove that he has taken reasonable care to avoid *the* particular inaccuracy in question.

(1) To construe the defence under para 18(3) literally, the omission of the definite article means that the reasonable care to avoid inaccuracy is to be exercised in a generic manner, and is not intended to be specific to the inaccuracy in question that has given rise to a potential penalty assessment.

(2) On a purposive construction, if reasonable care is to be exercised to avoid *the* inaccuracy, that would have presupposed knowledge on P's part of the inaccuracy in the first place. If P had the knowledge of *the* inaccuracy (which gives rise to the penalty in question), P should have taken care to remove the inaccuracy altogether. The formulation of taking 'reasonable care to avoid *the* inaccuracy' as a defence would not have made any sense. To stand as a defence against a penalty, the reasonable care to avoid inaccuracy cannot presuppose foreknowledge of what the inaccuracy in question is going to be.

155. In our judgment, if HMRC have met the burden under para 1 Sch 24 that the penalties are imposable, then for para 18(3) Sch 24 purposes, it is not sufficient for the appellant to traverse HMRC's case, but that the appellant has to meet the burden of availing itself of the defence by making a positive case that it '*took reasonable care to avoid inaccuracy*'.

The statutory condition under para 3(1) Sch 24

156. The penalties are pursuant to para 1 Sch 24, and para 3(1)(a) defines an inaccuracy as 'careless' '*if the inaccuracy is due to failure by P [i.e. the taxpayer] to take reasonable care*'. In view of the parties' submissions, the interpretation of 'careless' in the context of para 3(1)(a) requires the construction of its two constituents: '*due to*' and '*failure to take reasonable care*'.

Case law meaning on 'failure to take reasonable care'

157. Schedule 24 FA 2007 was enacted to repeal the old penalty regime under s 95 TMA. The concept of taking 'reasonable care' in giving a document to HMRC has drawn on case law concerned with discovery assessments under s 29 TMA, and the old penalty regime under s 95 TMA. It is opportune to set out the statutory wording of the respective provisions under sub-sections 29(4) and 95(1) TMA which have in some way influenced the development of the meaning of taking 'reasonable care' in the context of Sch 24 provisions.

(1) The statutory wording for the first condition to be met in raising a discovery assessment under sub-s 29(4) before and after 1 April 2010[5] is as follows:

(a) Prior to 1 April 2010: 'The first condition is that the situation mentioned in subsection (1) above [*is attributable to fraudulent or negligent conduct on the part of*] the taxpayer or a person acting on his behalf'.

[5] Words substituted by Finance Act 2008 c 9 Sch 39 para 3 with effect from 1 April 2010, except where SI 2009/403 art. 10 applies; 1 April 2012 otherwise.

(b) From 1 April 2010: 'The first condition is that the situation mentioned in subsection (1) above [*was brought about carelessly or deliberately by*] the taxpayer or a person acting on his behalf'.

(2) The repealed sub- 95(1) stated as follows:

'(1) Where a person fraudulently or negligently –

(a) delivers any incorrect return of a kind mentioned in … this Act …'

158. The authorities which have contributed to developing the meaning of 'reasonable care' for Sch 24 purposes include:

(1) In *Anderson (deceased)*(2009)[6], which was an appeal against a discovery assessment, Judge Berner considered the test to be applied in relation to 'negligent conduct' under the now superseded version of s 29(4) TMA to be an 'objective' test by reference to the 'reasonable taxpayer':

> '[22] … The test to be applied, … is to consider what a reasonable taxpayer, exercising reasonable diligence in the completion and submission of the return, would have done.'

(2) In *Hanson* (2012)[7] Judge Cannan considered 'carelessness' for Sch 24 purposes with reference to 'negligent conduct' and adopted the objective test of the 'reasonable taxpayer' in *Anderson (deceased)*, and stated that:

> '[19] … In my view carelessness can be equated with "negligent conduct" in the context of discovery assessments under section 29 Taxes Management Act 1970. In that context, negligent conduct is to be judged by reference to the reasonable taxpayer.'

(3) Noting that *Anderson (deceased)* was concerned with s 29(4) TMA, Judge Cannan in *Hanson* went on to conclude that there is a subjective element in the test of 'reasonable care' apposite to Sch 24 provisions:

> '[21] … What is reasonable care in any particular case will depend on all the circumstances. In my view this will include the nature of the matters being dealt with in the return, the identity and experience of the agent, the experience of the taxpayer and the nature of the professional relationship between the taxpayer and the agent.'

(4) In *Catherine Grainne Martin*[8] (2014), Judge Redston compared the error penalty regime under Sch 24 with the predecessor provisions under s 95 of TMA, and similarly concluded that the concept of taking reasonable care in the context of Sch 24 penalty regime incorporates a subjective element, and stated that it is 'similar to the approach taken on "reasonable excuse"', and so 'differs from the strictly objective meaning of negligence' (at [127]). Judge Redston remarked on the absence of 'reasonable excuse' provisions in Sch 24, and hence the subjective element should be accorded in the test of 'reasonable care' to counter the absence of 'reasonable excuse' provisions in Sch 24.

> '[130] If failure to take reasonable care were to be an objective test, Sch 24 would be much harsher than the TMA penalty provisions, because the objective test of negligence at TMA s 95 can be mitigated by the reasonable excuse provisions…'

[6] *Anderson (deceased) v Revenue and Customs Comrs* [2009] UKFTT 258 (TC).
[7] *Hanson v HMRC* [2012] UKFTT 314 (TC).
[8] *Catherine Grainne Martin v HMRC* [2014] UKFTT 1021 (TC).

(5) *Collis* (2011) concerned an appeal against a 'careless' penalty under Sch 24, Judge Berner aptly summarised the test as being objective and referable to the 'reasonable taxpayer' but taking into account the subjective attributes of the taxpayer in question:

> '[29] … That penalty applies if the inaccuracy in the relevant document is due to a failure on the part of the taxpayer (or other person giving the document) to take reasonable care. We consider that the standard by which this falls to be judged is that of a prudent and reasonable taxpayer in the position of the taxpayer in question.'

Is 'careless' under Sch 24 the same as 'negligent' under s 95 TMA?

159. The appellant's submissions have relied on case law from the old error penalty regime under s 95 TMA, where the definition of negligence was derived from the nineteenth century authority of *Blyth v Birmingham Waterworks Co*[9](1856):

> 'Negligence is the omission to do something which a reasonable man, guided upon those considerations which ordinarily regulate the conduct of human affairs, would do, or doing something which a prudent and reasonable man would not do.'

160. On the interpretation of 'carelessness', the appellant draws on *Bayliss*[10] which was an appeal against a penalty under the now repealed s 95 TMA, and where the concept of 'negligence' was considered in accordance with to *Blyth* (with the concomitant requirement to prove causation). The appellant's case is that HMRC have failed to establish causation in the present appeal in line with the tribunal's conclusion in *Bayliss* – in that HMRC have failed to establish the causal link between the appellant's failure to obtain a second opinion and the the inaccuracies in the P35s.

161. Before we can address the substantive submissions on causation, it is pertinent to establish the extent that case law on the penalty regime under the superseded s 95 TMA should instruct the Tribunal in construing provisions under Sch 24 FA 2007 of the new penalty regime. In our judgment, 'failure to take reasonable care' under para 3 Sch 24 FA 2007 is a different test to 'negligence' under s 95 TMA for the following reasons.

(1) The test of 'negligence' in the *Blyth* sense is referable to a hypothetical person – the prudent and reasonable man – and is therefore primarily an objective test.

(2) The objective test of negligence at s 95 TMA could be mitigated by the 'reasonable excuse' provisions at s 118(2) TMA whereby the subjective element was introduced into the former penalty regime.

(3) In the context of the penalty provisions under Sch 24 FA 2008, however, the objective and subjective elements of the test are combined, and the relevant test has been held by case law on Sch 24 FA 2007 to require consideration of the conduct which could be expected of a prudent and reasonable taxpayer (the objective aspect) in the position of the taxpayer in question (the subjective aspect).

162. In this respect, we agree with Judge Morgan in *Alan Anderson*[11](2016) where the tribunal was referred to explanatory notes published with the draft legislation of Sch 24 in 2007, and the consultation document published before the draft legislation which suggested that the term 'failure to take reasonable care' would 'incorporate the terms "negligent conduct" and "negligence"'. Nevertheless, Judge Morgan's conclusion at [120] is that:

[9] *Blyth v Birmingham Waterworks Co* [1856] 11 Ex 781.
[10] *Anthony Bayliss v HMRC* [2016] UKFTT 500(TC).
[11] *Alan Anderson v HMRC* [2016] UKFTT 335, [2017] SFTD 100.

> '… even if it is permissible to look to such materials for guidance as to the intent of Parliament in interpreting legislation, the statements in the materials are not sufficient to conclude that the two terms are simply interchangeable. Although there are indications that the change in terminology was not intended to give materially different results (at any rate as regards penalties), Parliament has chosen to use different words and it is those words which must be interpreted. The starting point must be that the term "careless" as further defined as a "failure to take reasonable care" has to be interpreted according to the usual principles of statutory interpretation.'

163. We are of the view that the authorities on s 95 TMA are of limited relevance to the penalty code under Sch 24. Since the concept of 'causation' is central to the appellant's case, and is a concept derived primarily from case law ruling on s 95 TMA, we address the extent of relevance that the concept of causation derived from s 95 TMA may have in the construction of the relevant provisions under Sch 24 as follows.

The construction of 'due to' in para 3(1)

164. The question we direct ourselves to address is whether there is any basis for construing the statutory condition under para 3(1) Sch 24 as requiring a proof of causation. The statutory phrase 'due to' arguably may have given rise to the notion of causation. The relevant dictionary meaning to be given to 'due to' in para 3(1) is '*attributable to, ascribable to'* (as an adjectival phrase) or '*because of, on account of, owing to*' (as a prepositional phrase).

165. The change in the statutory wording referred to earlier in relation to sub-s 29(4) TMA, where the wording '*attributable to fraudulent or negligent conduct*' became '*brought about carelessly or deliberately by*', was part of a number of changes stated in explanatory notes issued in 2008 with the draft amendments to s 29 TMA. The explanatory notes referred to the amendments of s 29 TMA as being made to align with the terms used in the new penalty regime under Sch 24 FA 2007, 'as part of introducing a more uniform penalty regime across different taxes': *Alan Anderson* at [118]. In the discovery assessment context of sub-s 29(4), the wording of 'attributable to' and 'brought about' between the insufficiency of tax discovered and the behaviour of the taxpayer similarly connotates with 'due to' in para 3(1) of Sch 24.

166. We are of the view that the nexus required to be established at para 3(1) is one of *attribution* – in the sense that the inaccuracy can be accounted for by a mode of behaviour which is characterised as 'failure to take reasonable care'. Attribution in the sense of *because of*, *on account of*, or *owing to* connotes the sense that the inaccuracy in question being accountable by, or explained by a failure to take reasonable care. In our judgment, 'due to' in para 3(1) of Sch 24 does not equate to the kind of nexus of causation apposite to tort liability.

167. *Blyth* was a case on tort liability. To establish liability in tort, it is necessary to prove the chain of causation whereby a duty of care existed between the parties, there was a breach of that duty (by omission or commission of a certain action), and that breach of duty is the proximate cause of the damage or injury sustained. The most important element of proof is the casual link between the breach and the injury, and causation in tort is often cast in terms of 'but for' the defendant's actions/omissions, the plaintiff's injury would not have occurred.

168. The 'but for' type of causation in tort requires *specificity* in order to establish the breach of a particular duty of care is the cause of injury. Specificity for each element of proof requires the pinpointing of an action or omission to establish the breach, and that it is a specific breach that is the immediate cause of the injury. Each element of proof in tort is primarily objective, and the causal link required to be established for each element needs to be tight to prove proximity whereby the breach in question is the *immediate* cause of the injury in question.

169. Unlike the proof of breach in tort, which is an objective test, the characterisation of the mode of behaviour under the description of 'failure to take reasonable care' is an objective test, and at the same time, takes into account the subjective attributes of the taxpayer in question. Unlike the pinpointing of an action or omission to establish a breach in tort, the characterisation of a mode of behaviour for para 3(1) purposes is a broader consideration than the mere focus on a specific action or a particular omission.

170. The taxpayer's defence under para 18(3) is in a generic sense of: 'took reasonable care to *avoid inaccuracy*'. The absence of the definite article in 'avoid inaccuracy' is conspicuous, and connotates the generality of a mode of behaviour, rather than the specificity of a particular action or omission. The absence of the definite article in para 18(3) defence points to the construction that the nexus between inaccuracy and behaviour applicable to Sch 24 FA 2007 is not one of causation in the 'but for' sense, which requires the pinpointing of an action or omission to be *particularised* in order to establish the 'but for' causation.

171. For these reasons, we do not find it appropriate to import the concept of causation apposite to the law of tort to construe the statutory wording 'due to' at para 3(1). We reject the notion that 'due to' in para 3(1) which introduces the nexus between the inaccuracy in question and the taxpayer's behaviour connotates causation in the 'but for' sense required in tort.

172. Having set out the case law relevant to our consideration, and have addressed certain points of statutory construction relevant to considering the parties' submissions, we now address the issues for determination in this appeal in turn.

Issue 1: Are the penalty assessments in time?

173. The present case is concerned with assessment to a penalty where there was no assessment to the tax concerned (but by way of a settlement agreement), so the time limit provision under para 13(3)(b) applies: '*if there is no assessment to the tax concerned within paragraph (a), the date on which the inaccuracy is corrected*'.

174. At the end of the first diet of the hearing, the Tribunal raised the point as regards the validity of the penalty notices in relation to para 13(1)(a) and (b) of Sch 24 for HMRC to 'assess the penalty' and 'notify the person', as well as the time-limit provision under para 13(3)(b) whereby an assessment of a penalty under para 1 must be made before the end of the period of 12 months beginning with the date on which the inaccuracy is corrected, if there is no assessment to the tax concerned.

175. The Tribunal is satisfied that the penalty notices are valid on the facts of the case:

(1) The date on which the inaccuracy was corrected (where there was no assessment to the tax concerned) was the date of the settlement agreement between Delphi and HMRC; namely: 29 March 2017.

(2) The period for assessing the penalty began to run from 29 March 2017.

(3) The notices of penalty assessments are dated 23 March 2018, and confirmed by Officer Barraclough's evidence.

(4) On 23 March 2018, Tucker with Langran were sent by email the relevant letter and schedules (also sent by post) to notify Delphi of the Penalty Determinations.

(5) Tucker's witness statement confirms that the Penalty Determinations were received by post on 3 April 2018.

176. The date of the assessment and notification of the penalties as required under para 13(1) therefore took place on 23 March 2018, and within 12 months of the date of the settlement agreement on 29 March 2017. The appellant does not dispute that on the facts of the case, both

the 'making' and 'notification' of the penalty assessments took place within the twelve months of the date of the settlement agreement.

177. For completeness, we note that para 13(3) specifies the 12-month time limit applies to 'An *assessment* of a penalty under paragraph 1', as distinct from the 'notification' of a penalty; see *Honig v Sarsfield* [1986] STC 246 where the Court of Appeal distinguished the stages of 'assessment' from 'notification'. Therefore, even if notification had been made more than 12 months after 29 March 2017, the penalty notices would still have been valid if the date of the penalty assessments was within the 12-month period from 29 March 2017.

Issue 2: Were the P35 returns inaccurate?

178. Issue 2 is factual in nature, and requires the Tribunal to decide if one of the pre-conditions for an error penalty is met by reference to para 1(2)(a) Sch 24, which states:

> (2) Condition 1 is that the document contains an inaccuracy which amounts to, or leads to –
>
> (a) an understatement of a liability to tax, …

179. HMRC's case is that the P35 returns filed for 2008-09 and 2009-10 were inaccurate because the returns did not include the amounts allocated to the sub-trusts of Delphi's directors. These amounts fell to be assessed for PAYE and NICs following the Supreme Court's judgment on the *Rangers* case, and therefore should have been included in the P35 returns.

180. There is a prima facie case that the P35 returns in question had led to an understatement of a liability to income tax and NICs by omission in accounting for the EBT contributions that were allocated to the directors' sub-trusts. On the face of it, Condition 1 under para 1(2) Sch 24 is met in respect of both tax years.

The non-production of the P35 returns

181. As a matter of fact, HMRC have not produced a copy of the P35 returns for 2008-09 and 2009-10 as exhibits of the documents said to have contained the inaccuracies. Ms Choudhury's submissions do not draw on the evidence of Officer Barraclough, who was unable to confirm if the P35s contained the inaccuracies. Instead, Ms Choudhury refers to Mr Tucker's statement and oral evidence, for confirmation that the sums allocated to the sub-trusts were not included for PAYE and NICs purposes.

182. For the appellant, Mr Sherry submits that HMRC have failed to provide any evidence of an inaccuracy in any of the P35 returns; that HMRC have relied on peripheral evidence provided by Mr Tucker, and such reliance is 'misplaced' as it is 'not sufficiently strong to prove' HMRC's case. Mr Sherry referred us to *Rogers and Shaw*[12], which concerns late filing penalties for Self-Assessment returns, and the Upper Tribunal found that:

> '[50] … if HMRC fail to provide <u>any evidence at all</u> to the effect that a s8 notice was served, they will have failed to demonstrate a crucial fact on which their entitlement to a penalty hinges and the FTT will necessarily set aside the penalties charged for alleged failure to comply with that notice.
>
> [51] Where HMRC have given <u>some</u> evidence that a s8 notice was served, it will then be a matter for the FTT to determine whether that evidence is sufficiently strong to discharge HMRC's burden of proof. The FTT's assessment of the evidence should take into account the extent to which the taxpayer is disputing receiving a s8 notice. …' (Emphasis original)

183. The crucial fact in *Rogers and Shaw* concerned whether there was evidence that HMRC had served a notice under section 8 of the Tax Management Act 1970 to notify the taxpayers

[12] *Revenue and Customs Comrs v Nigel Rogers and Craig Shaw* [2019] UKUT 0406 (TCC).

of their obligation to file a Self-Assessment return. Despite both cases being concerned with penalties, we do not consider the facts in *Rogers and Shaw* to be on all fours with the present case. Whilst HMRC's entitlement to impose a late filing penalty under Schedule 55 of the Finance Act 2009 ('**Sch 55**') hinges on a s 8 TMA notice having been served, there is no equivalent of a prerequisite notice having to be served by HMRC for a Sch 24 penalty to be imposable. The nexus for imposing a Sch 24 penalty is an alleged error in a document 'P' (such as a taxpayer) gives to HMRC – the P35 returns in issue here were documents emanating from the appellant as the taxpayer, and furnished to HMRC.

184. Mr Tucker's explanation that Dickinsons did not retain a copy of the P35s after the statutory period of six years for record retention, which would be 5 April 2015 (for 2008-09) and 5 April 2016 (for 2009-10). With reference to the expiry dates of the 6-year record retention periods, we note the following dates in the chronology of enquiries.

(1) HMRC had opened an enquiry into 2008-09 CT return on 15 September 2009, which was before the expiry date for the 6-year retention period on 5 April 2015.

(2) HMRC had opened an enquiry into 2009-10 CT return on 12 January 2011, which was before the expiry date for the 6-year retention period on 5 April 2016.

(3) The EBT Settlement Opportunity letter sent to Delphi in December 2014 was to intimate that PAYE and NICs were at issue for users of the Clavis Arrangement, and the letter was followed up by another letter dated 27 February 2015.

185. The EBTSO letters therefore pre-dated the 6-year expiry dates of 5 April 2015 and 2016, and could have, arguably, alerted the appellant to the fact that the taxes at issue were PAYE and NICs and not corporation tax.

186. Similarly, whilst HMRC had opened the enquiries into Delphi's CT returns, the issue of PAYE and NICs being the 'lost revenue' was alive at least from the time of the EBTSO letter in December 2014, but HMRC did not retain a copy of the P35 returns either. The P35 returns emanated from Delphi, and it is not surprising that Barraclough was unable to speak to whether the sums allocated to sub-trusts in the relevant years were in fact omitted on the P35s if he had not had sight of the actual P35 returns.

187. In any event, Delphi does not dispute that the amounts allocated to the sub-trusts in relation to Delphi's directors had not been included in the P35 returns for 2008-09 as respects tranches 1, 2 and 3, and for 2009-10 as respects tranche 4. We have regard that the inaccuracy in each return was by way of omission of the relevant tax liabilities in their entirety, and not by way of some certain figures having been stated on the returns which turned out to be understatements. The substantive sums of the omitted PAYE and NICs were, in fact, determined by the settlement agreement and became the quantum of the Potential Lost Revenue ('**PLR**') for Sch 24 purposes.

188. In these circumstances, we consider that the evidence from Tucker, and the fact that the PLR had been agreed between the parties by dint of the settlement agreement, are sufficient for us to make the necessary findings of fact; namely Delphi gave HMRC a document (the P35 for each relevant tax year) pursuant to para 1(1)(a), and the document contains an inaccuracy which leads to 'an understatement of a liability to tax' pursuant to para 1(2)(a).

189. Notwithstanding the non-production of the P35s in question as the relevant documents, we find that Delphi 'gave' HMRC the P35s in terms of para (1)(a), and Condition 1 in terms of para 1(2)(a) is met that both P35s contained an inaccuracy by way of omission.

Issue 3: Were the inaccuracies 'careless' in respect of all tranches?

190. We understand Ms Choudhury's submissions on 'careless' behaviour to be relevant to both tax years, and underpin the overall basis for imposing the penalties. Whilst the assessment to penalty has categorised the inaccuracy in relation to tranches 1 to 3 as 'careless', and tranche 4 as 'deliberate', we consider that the facts for assessing tranches 1 to 3 to be equally relevant to tranche 4. HMRC's case is that tranche 4 had circumstantial factors that escalate the degree of culpability to 'deliberate', and in addressing Issue 3, we make no distinction between tranches 1 to 3 and tranche 4. In this regard, our findings and conclusion in relation to Issue 3 apply equally to tranches 1 to 3 as to tranche 4.

191. The parties have made extensive written submissions on Issue 3, and there are three key strands in the arguments put forward as concerns the 'careless' penalty. It is opportune to summarise these strands by reference to Ms Choudhury's submissions for HMRC on Issue 3:

> (1) For the avoidance of doubt, the penalties have *not* been imposed on the basis that the appellant and/or its advisers took a different view of the law from HMRC at the relevant time.
>
> (2) Rather, the basis for imposing the penalties is that Delphi failed to follow the advice of its own accountant and/or to obtain further advice from independent counsel. In failing to do either, the appellant acted carelessly.
>
> (3) It is HMRC's case that 'a second opinion would have highlighted [certain] points not properly considered in [Tucker's] letter'. The failure to take a second opinion was the carelessness which led to the inaccuracies in the PAYE returns.

192. In response, Mr Sherry submits that the appellant could not be held as 'careless' for the inaccuracies in the P35 returns by reference to: (a) the 'prevailing practice' at the time; (b) the advice received from Tucker and others; and (c) that there was no causal link between the possibility of a second opinion and the inaccuracies in the P35 returns.

Issue 3(a): Whether a 'prevailing practice'

193. The appellant contends that the tax treatment of contributions made to the EBT was in accordance with prevailing practice and 'a widely held view' that such arrangements would not be subject to income tax and/or NICs. In this respect, the appellant relies on the *Morse Report*, and that: (a) taxpayers were entitled to follow what the courts had decided and not to accept HMRC's published view at the time; (b) the *Morse Report* endorses Tucker's advice and evidence that loan schemes 'were not seen as being aggressive tax avoidance at the time'.

194. On this basis, Mr Sherry invites the Tribunal to find that if the appellant had sought a second opinion at the time, in the light of *Dextra* and *Sempra*[13], such an opinion 'was highly unlikely to have differed as to the PAYE position' because 'there would have been no authority to base a contrary view on'.

195. As to the admissibility of the *Morse Report* the appellant urges on the Tribunal to exercise its discretionary power under Rule 15(2)(a), whereby the Tribunal 'may admit evidence whether or not the evidence would be admissible in a civil trial in the United Kingdom', citing *Avonside Roofing*[14], which has made reference to the *Morse Report*.

196. The only authorities ruling directly on the use of EBTs at that time were two first-instance decisions of the Special Commissioners in *Dextra* (2002) and *Sempra* (2008). Ms Choudhury submits that the so-called 'prevailing practice' in the appellant's submissions is 'an allusion to the fact that at the time the Scheme was entered into, the courts had not agreed that payments

[13] *Dextra Accessories Ltd v Macdonald* STC (SC) 413; *Sempra Metals Ltd v HMRC* [2008] STC)(SC) 413.
[14] *Avonside Roofing Ltd v HMRC* [2021] UKFTT 158 (TC).

to an EBT constituted earnings (or emoluments)' given the substance of the decisions in *Dextra* and *Sempra*. Ms Choudhury submits that:

(1) In *Dextra*, the Special Commissioners had not accepted the Revenue's argument that the payments to the EBT in that case were earnings, and this argument was not pursued on appeal.

(2) Despite losing the argument in relation to income tax in *Dextra*, HMRC relied on it again in *Sempra* where the Special Commissioners dismissed an appeal against assessments to corporation tax in respect of payments to an EBT, but again did not accept HMRC's argument that payments into the EBTs constituted earnings.

(3) HMRC were unable to pursue this argument further in *Sempra* because the parties settled before the High Court hearing of HMRC's appeal.

(4) The Supreme Court in *Rangers* (2017) held that both *Dextra* and *Sempra* had been wrongly decided.

(5) Further, the appellant ignores the fact that in both *Dextra* and *Sempra*, it was found that the taxpayer company was ***not*** entitled to a deduction for corporation tax for the contribution made to an EBT – even if the taxpayer company did not have to account for PAYE in relation thereto.

(6) The appellant's witnesses, however, accepted that the Scheme was designed with the aim of bringing about ***both*** a corporation tax deduction ***and*** monies being paid to employees without deduction of income tax and NICs.

(7) As provided by the legislation at the time, the corporation tax deduction could have been secured by accounting for income tax and NICs on the benefits provided out of the contributions to an EBT.

(8) It is therefore incorrect to say that the Scheme was in accordance with 'prevailing practice', or (if different) the decided cases at the time, because the appellant was seeking a CT deduction ***and*** avoiding the obligation to account for income tax and NICs under PAYE by means of an arrangement that involved more than simply setting up an EBT.

(9) The Scheme therefore could not have succeeded in its purpose of securing a corporation tax deduction without accounting for income tax and NICs, on the basis of: (i) the wording of the legislation, and (ii) HMRC's published views.

(10) In the context of the appellant's contention on 'prevailing practice', it is worth noting that both PAYE determinations and NIC decisions (December 2012 for 2008-09, and November 2013 for 2009-10) were issued to the appellant in respect of the Scheme long before *Rangers* was decided.

197. In terms of case law meaning for 'prevailing practice', Ms Choudhury cites *Hoey*[15] where the Upper Tribunal considered the statutory term of '*the practice generally prevailing at the time*' in the context of discovery assessments pursuant to s 29(2) TMA. *Hoey* concerned discovery assessments raised in relation to payments made to the taxpayer as a beneficiary of an EBT of the type that was determined in *Rangers*. The UT in *Hoey* referred to *Household Estate Agents*[16] where Henderson J said at [161]:

> '… it seems to me that a practice may be so described only if it is relatively long-established, readily ascertainable by interested parties, and accepted by HMRC and taxpayers' advisers alike: compare the decision of the Special

[15] *Stephen Hoey v HMRC* [2021] UKUT 82 (TCC).
[16] *HMRC v Household Estate Agents Ltd* (2007] EWHC 1684 (Ch) on 'prevailing practice' in discovery cases.

> Commissioners (Dr A N Brice and Mr John Walters QC) in *Rafferty v HMRC* [2005] STC(SD) 484 at paragraph 114'. [i.e. "a practice generally prevailing had to be a practice, or agreement, or acceptance over a long period whereby the Revenue agreed or accepted a certain treatment of sums in particular circumstances" per *Rafferty*.] '

198. In reply, Mr Sherry submits that the appellant does not rely on the statutory defence of 'prevailing practice' pursuant to s 29(2) TMA. Rather, the appellant refers to 'prevailing practice' in the sense of 'a widespread practice', of what was 'commonly adopted by a majority of taxpayers and their advisers at the times the appellant submitted its P35 returns'. In particular, the appellant does not argue that the decided case law was accepted by HMRC (as required in discovery cases).

199. In other words, Mr Sherry seeks to distinguish the concept of 'prevailing practice' relied upon by the appellant for Sch 24 purposes from the concept of 'general practice prevailing at the time' that can be relied upon by a taxpayer to resist the allegations of carelessness 'for s29(2) TMA purposes. Mr Sherry further submits that the relevant test for carelessness for Sch 24 purposes is what a prudent reasonable taxpayer in his situation would have done, not what HMRC or their officers would have done for s 29 TMA purposes in the discovery context.

200. It is further submitted for the appellant that whether or not HMRC's view remained consistent despite defeats at first instance is irrelevant. In this respect, Mr Sherry refers us to:

(1) *R(oao Cartref & Ors)*[17] wherein claims for judicial review were made against HMRC's enforcement of the relevant legislation as enacted to tackle 'Disguised Remuneration', by notifying the claimants' liability to a tax charge from 5 April 2019, unless a settlement was agreed in advance of that date. The overarching issue for the judicial review claim was 'whether an incompatibility declaration on human rights grounds is available in respect of the Loan Charge' introduced by Finance (No 2) Act 2017, Schedule 11'. Mr Sherry highlights that the High Court in *Cartref* made no comment about the interaction between the decided cases in *Sempra* and *Dextra* and HMRC's contrary views.

(2) *Morse Report* where it is reported that the Spotlights reached a 'limited number of agents and tax professionals', and that scheme users 'would likely to have continued to be largely unaware of HMRC's position at this time' (i.e. from 2009 onwards).

Issue 3(a) Conclusion on 'prevailing practice'

201. Having considered the parties' submissions, we conclude that the appellant's reliance on what it described as 'prevailing practice' does not assist its case for the following reasons.

(1) We reject the notion that there should be a different interpretation of the term 'prevailing practice' for present purposes to what has been established in case law in the context of s 29(2) TMA. On the contrary, the fact that a Sch 24 penalty is often imposed in tandem with a discovery assessment supports the interpretation that any reliance on 'prevailing practice' as a defence against a Sch 24 penalty is referable to the same standard and proof in line with the defence of '*the practice [being] generally prevailing at the time*' under s 29(2) TMA against a discovery assessment.

(2) Parliament's intention that there should be consistency in construing s 29 TMA and Sch 24 FA 2007 is evident by the harmonisation of the statutory wording in s 29(4)TMA to that of Sch 24 FA 2007 as discussed earlier, which resulted in the amended wording

[17] *R(oao Cartef) v HMRC* [2019] EWHC 3382 (Admin).

from 1 April 2010 to '[*was brought about carelessly or deliberately by*]' that is the current version of s 29(4) TMA.

(3) We have not heard any convincing legal submissions for the appellant by reference to established case law that the notion of 'prevailing practice' for Sch 24 purposes should be differently established from than that for s 29(2) TMA purposes. Insofar as the appellant seeks to rely on the notion of 'prevailing practice', that notion is to be in harmony with s 29(2) TMA.

(4) The appellant's assertion that *Sempra* and *Dextra* had established a settled view of the law has no factual basis. The taxpayer in *Hoey* similarly argued that the state of the law at the time (based on *Sempra* and *Dextra*) meant that it was a fair assumption that HMRC would abide by the court's decisions, even if the decisions had found against HMRC. The UT found that the taxpayer's argument fell at the first hurdle regarding the state of law, after noting that:

> '[169] … HMRC highlight that *Sempra* was settled before HMRC could appeal (as recorded in Judge Poon's dissenting judgment in the FTT's decision in *Rangers* at [210]). In any case HMRC say no authority is advanced for the proposition that, because a case goes against a party and the party does not appeal, the party is content with the outcome such that it forms part of the generally prevailing practice. HMRC litigated *Sempra* after *Dextra.* The position HMRC adopted in *Rangers* showed that at no point had HMRC accepted *Sempra* and *Dextra*.'

(5) The appellant's reliance on *Sempra* and *Dextra* as the authorities underpinning the purported 'prevailing practice' that PAYE/NICs were not payable on EBT contributions is misguided, as concluded by the UT in *Hoey* at [170]: both *Sempra* and *Dextra* were first instance decisions which did not create a precedent, and while the decisions would have been of 'persuasive value', 'there could not be said to be a settled view of the law'.

(6) Further, *Sempra* and *Dextra* (wrongly) held that no CT deduction was available (and no PAYE/NICs payable) on contributions to EBTs. Even taking *Sempra* and *Dextra* at their face value, the appellant has failed to establish that these two authorities could be construed as giving rise to a prevailing practice that EBT contributions could avoid PAYE/NICs *and at the same time* obtain a CT deduction as claimed by the Scheme: see Cockerill J's judgment in *R(oao Cartref)*[18] which highlighted that HMRC had been consistent in their view that EBTs were ineffective in avoiding PAYE/NICs.

(7) The *Morse Report*, even if admitted as evidence, does not assist the appellant. The paragraphs relied upon by the appellant, as recorded earlier in the decision, are to be read in the context of the whole report. To the extent that it sheds any light on the state of the law on the tax treatment of EBTs, the *Morse Report* highlights is that there was no settled view of the law. For present purposes, we find the UT's observation in *Hoey* at [167] apt:

> 'In our view, all this [excerpts from the *Morse Report*] confirms is that there is a dispute, … around the position that was being maintained by HMRC. It does not tell us what the position was at the relevant time. For the appellant's purposes, it does not provide the necessary evidence for them to meet their burden. Insofar as the support is relevant, it lends support to the idea that

[18] Cockerill J's judgment in *R(oao Cartref Care Home Ltd & Ors) v HMRC* gives a full summary under the heading '*The background noise: Spotlights, mailings and Rangers*' at [75] to [86] of HMRC's view being consistent throughout that schemes used to reward employees without accounting for PAYE and NICs were ineffective, which eventually led to the introduction of the Loan Charge legislation in 2017.

> HMRC had a view which was different to that set out by the court decisions [i.e. *Sempra* and *Dextra*] referred to.'

202. The appellant has asserted a prevailing practice in terms of no PAYE/NICs being regarded as payable on EBT contributions. We do not consider this to be an adequate characterisation of the practice that the appellant is required to establish. The relevant 'prevailing practice' for present purposes, at its fundamental level, has to be characterised as one with two co-existing strands of practice: namely (i) *no PAYE/NICs were payable* on the EBT contributions, and (ii) a CT deduction relief being available *at the same time*.

203. Further, and insofar as the appellant seeks to rely on there existed a prevailing practice in its defence, it is for the appellant to establish the fact it so relies on. Notwithstanding the appellant's reliance on *Brady* as respects the burden of proof, we consider that the onus is on the appellant to establish that there was a prevailing practice extant in 2008-09 and 2009-10 as characterised by both aspects of the tax treatment as regards CT deduction relief and no PAYE/NICs arising. We adopt Henderson J's definition in *Household Estate Agents* – a practice can be said to the 'prevailing' if it is '*relatively long-established, readily ascertainable by interested parties, and accepted by HMRC and taxpayers' advisers alike*'.

204. We conclude that the appellant has failed to prove that such a practice was in any way prevailing or extant at the relevant time of 2008-2009 and 2009-10, for Delphi to take a CT deduction while at the same time avoid paying PAYE/NICs.

205. For completeness, we should note HMRC's objection to the *Morse Report* as admissible evidence to support the appellant's submissions that the *Report* confirmed that taxpayers were entitled to rely on the law as interpreted by the courts at that time (i.e. not as interpreted by HMRC). HMRC's position is that the *Morse Report* is not authority as to the law, and it is doubtful whether it even constitutes admissible expert/opinion evidence, and poses a similar question as arose in relation to a report prepared by an All-Party Parliamentary Group in *Cartref* (see [172]-[173]).

206. The Tribunal has adopted the *de bene esse* approach in hearing the appellant's submissions in reliance on the *Morse Report*. We are of the view that the *Morse Report* is of no assistance to the appellant's case, not only for all the reasons as noted by the UT in *Hoey*, but that the EBTs being considered in the *Morse Report* were the 'standard' EBTs which did not seek to invoke the exemption under para 8(a) Sch 24 to FA 2003, that being the key feature in the design of the Clavis Arrangement.

207. The Clavis Arrangement, by seeking to invoke the 'goods and services' exemption, is to be differentiated from the standard EBTs covered by the *Morse Report*. For this reason alone, the reliance placed by the appellant on the *Morse Report* to assert that there was a settled view of the law is plainly unsupportable, if not distortional or misleading, since the *Morse Report* says nothing about whether taxpayers were entitled to take the view that a CT deduction could be claimed on the contributions to sub-trusts in an EBT, while loans out of the sub-trusts of the EBT were not taxable as earnings (as in the Clavis Arrangement). The excerpts from the Report relied on by the appellant are highly selective, and we have regard that the Report is to be read in conjunction with the pertinent remark contained in the executive summary:

> 'This does not imply approval of artificial tax schemes, or of tax avoidance. If the Loan Charge controversy shows anything, it shows what a bad idea participating in such schemes was in the past and will be in the future.'

208. In any event, HMRC are emphatic that their case is not based on there being a difference between the appellant and/or its advisers took a different view of the law from HMRC at the relevant time. In this respect, even if the appellant had proved that such a prevailing practice was extant at the time of the tranches being implemented, it would not have been enough to

traverse HMRC's case, so to say. We need to go on to consider whether the basis for imposing a careless penalty is valid in terms of para 3(1) of Sch 24.

Issue 3(b): Whether failure to take reasonable care

HMRC's submissions on the basis of careless penalty

209. Ms Choudry's submissions in this respect are summarised as follows:

(1) HMRC are not contending that the Trust or sub-trusts which formed part of the Scheme were not correctly established and/or were a sham, or that any of the payments in question were not actually made by the appellant.

(2) HMRC's case is that the appellant did not meet the standard of a reasonable and prudent taxpayer because it did not follow the advice it had been given to obtain advice from independent counsel before entering into the Scheme.

(3) HMRC accept that the appellant did not have any tax expertise of its own. Langran's witness statement referred to several individuals involved in the Scheme: McNelly, Forbes, Clavis, etc. However, it is clear from Langran's evidence that the only person who was instructed to give Delphi advice and actually gave advice was Tucker.

(4) Tucker's advice was primarily set out in his letter dated 7 August 2008. HMRC invite the Tribunal to read the letter for itself and form its own view.

(5) At two separate places, the letter of 7 August 2008 recommended that the appellant obtain advice from independent tax counsel.

(6) HMRC's case is that the appellant did not follow Tucker's recommendation as clearly set out in his letter, which puts the appellant in a different position from the taxpayer in *Hicks*[19] (where the taxpayer did follow the advice it had been given). The present case can also be distinguished from *Herefordshire Property Company*[20] wherein the taxpayer had used a previous scheme marketed by the same promoter and had no reason to seek further advice.

(7) As a final but important point, HMRC submit that it is reasonably clear that the directors were simply concerned with ensuring that they were not entering into any illegal or criminal activity. They were not concerned with whether they were entering into genuine commercial transactions or whether HMRC considered the required tax savings could be obtained. Both Tucker and Langran referred to how HMRC's view was not the law. Langran said that he would have phrased the question (i.e. instructions) to Tucker as '… *please examine the scheme to see if it is a legitimate tax avoidance*'. Given the context, HMRC submit that it is unsurprising that the appellant chose to ignore the clear recommendation from Tucker to obtain independent advice.

Evaluation of appellant's witness evidence

210. The key aspects of evidence in this appeal concern the advice given by Tucker to Delphi in respect of the Clavis Arrangement, and the evidence came to be focused on the letter of 7 August 2008 authored by Tucker. The meanings of the content of the letter were subjected to extensive cross-examination and then re-examination, with nuances of various possible and plausible interpretations of the material content being given by Tucker of his advice letter, or being put forward by the appellant's counsel in re-examination for assent. Our overall assessment of Tucker's evidence in this respect is that it represents a reconstruction of possible and plausible interpretations of the advice letter with the hindsight of the legal issues that are

[19] *Hicks v HMRC* [2020] UKUT 12 (TCC); [2020] STC 254.
[20] *Herefordshire Property Company v HMRC* [2015] UKFTT 79 (TC).

alive in this appeal. This assessment of Tucker's evidence given in cross-examination and re-examination is not allayed by Tribunal's follow-up questions of some length to try to get closer to the meanings of the advice letter at the time it was written, as an attempt to ascertain the exact nature of the advice (i.e. untampered by the legal issues at hand) that was given by Tucker back in August 2008.

211. For the avoidance of doubt, we have no issue with the credibility of Mr Tucker and Mr Langran, in the sense that we do not find either witness to have set out to mislead the Tribunal. However, we find that the passage of more than 14 years between the time of the given advice as encapsulated in the letter of 7 August 2008 and the witnesses being called for evidence in October 2022 has rendered much of the appellant's witness evidence in this respect of little assistance in ascertaining the exact advice that was given by Tucker in the letter of 7 August 2008. We are faced as the fact-finding tribunal with the obvious difficulty posed by any reliance of witnesses' recollection of events from the distant past for the same reason as articulated by Leggatt J in *Gestmin*[21] at [17]:

> 'In fact, psychological research has demonstrated that memories are fluid and malleable, being constantly rewritten whenever they are retrieved.'

212. By way of illustration, we highlight some unsatisfactory aspects of the appellant's witness evidence which undermine its overall reliability.

(1) In cross-examination, and in relation to the meaning of the phrase '*aggressive tax planning*' in the advice letter, Tucker stated variously:

(a) That he did not consider the Scheme to be '*aggressive tax planning*' because EBTs had been around for a long time.

(b) Later on, Tucker said he considered aggressive tax planning was 'close to sham transactions', and that such transactions would not only be ineffective for tax purposes, but would also be illegal and potentially give rise to criminal liability.

(c) Tucker then sought to revise his view and said that the Scheme could almost certainly be considered aggressive because there was such a large take-up of these arrangements.

(2) Tucker was clear that any advice he gave orally would not have been phrased differently from the advice given in the letter. There is a conflict with Langran's evidence on this point because Langran stated that while Tucker's advice in the letter was to obtain further advice, he had not said this at the meeting: '*in the meeting no, on the letter, yes*'.

(3) Tucker stated that the risk he had referred to in the last paragraph to be 'a commercial risk' (which is understood as intending to counter-balance the list of tax risks itemised in the letter that led to the suggestion that the appellant should obtain independent counsel's opinion) – but there is no reference to the risk being a commercial risk in the final paragraph, only a reference to the possibility of Delphi's directors wishing 'to proceed having taken a commercial view'.

(4) In re-examination, Tucker agreed to the proposition put forward in question by Mr Sherry that the real risk with which independent counsel's advice would help was that Thornhill's advice, Clavis's advice, and Tucker's understanding of the tax consequences of the Scheme were wrong, (which is understood as a suggested interpretation led by the appellant's counsel of what the 'real risk' possibly could have meant in Tucker's letter)

[21] *Gestmin SCPS SA v Credit Suisse (UK) Ltd and another* [2013] EWHC 3560 (Comm).

– and this proposed interpretation was put forward for Tucker's assent to link the 'real risk' as put forward with the advice to seek independent counsel's opinion.

(5) In relation to the minutes of meeting of 23 June 2008, Langran could not recall having had the meeting, while Tucker's evidence seemed to be concerned with the Companies Act requirement of having such a minute in place. It is not necessary for us to determine the appeal by making a finding of fact in relation to whether the purported meeting did take place in June 2008 as recorded (which would have to had taken place before Delphi was in fact introduced to the Clavis Arrangement in July 2008). Nor do we seek to make any finding that the minutes were retrospectively put in place in order to meet Companies Act requirement (in view of Tucker's evidence and the possibility that the meeting did not take place in June 2008 as recorded). The unsatisfactory state of the witness evidence not only cast doubt on the reliability of the witnesses' recall in this instance, but possibly also on the contemporaneity of the minutes.

213. We accept that the inherent unreliability of human memories, and we make no criticism of the unsatisfactory aspects of evidence highlighted above. We have regard to the observation that the process of recall inevitably involves reconstruction, and questions asking witnesses to distinguish between 'a genuine recollection' and 'a reconstruction of events' are misguided as highlighted in *Gestmin*:

> '[21] … Such questions are misguided in at least two ways. First, they erroneously presuppose that there is a clear distinction between recollection and reconstruction, when all remembering of distant events involves reconstructive processes. Second, such questions disregard the fact that such processes are largely unconscious and that the strength, vividness and apparent authenticity of memories is not a reliable measure of their truth.'

214. It is not only the fallibility of human memories, but also its malleability that leads us to conclude that leads us to conclude that the witness evidence on the content of Tucker's advice letter of 7 August 2008 represents a reconstruction of possible and plausible interpretations of the advice letter with the hindsight of the legal issues that are alive in this appeal. As observed in *Gestmin*, the process of civil litigation subjects the memories of witnesses to 'powerful biases' and 'considerable interference' in the following manner:

> '[19] The process of civil litigation itself subjects the memories of witnesses to powerful biases. The nature of litigation is such that witnesses often have a stake in a particular version of events. This is obvious where the witness is a party or has a tie of loyalty (such as an employment relationship) to a party to the proceedings. Other, more subtle influences include allegiances created by the process of preparing a witness statement and of coming to court to give evidence for one side in the dispute. A desire to assist, or at least not to prejudice, the party who has called the witness or that party's lawyers, as well as a natural desire to give a good impression in a public forum, can be significant motivating forces.
>
> [20] Considerable interference with memory is also introduced in civil litigation by the procedure of preparing for trial. A witness is asked to make a statement, often (as in the present case) when a long time has already elapsed since the relevant events. The statement is usually drafted for the witness by a lawyer who is inevitably conscious of the significance for the issues in the case of what the witness does nor does not say. The statement is made after the witness's memory has been "refreshed" by reading documents. The documents considered often include statements of case and other argumentative material as well as documents which the witness did not see at the time or which came into existence after the events which he or she is being

> asked to recall. The statement may go through several iterations before it is finalised. Then, usually months later, the witness will be asked to re-read his or her statement and review documents again before giving evidence in court. The effect of this process is to establish in the mind of the witness the matters recorded in his or her own statement and other written material, whether they be true or false, and to cause the witness's memory of events to be based increasingly on this material and later interpretations of it rather than on the original experience of the events.'

215. In this respect, we accept Ms Choudhury's submission that Tucker, and to a much greater extent, Langran, sought to minimise the importance of the advice given in the letter. Tucker's evidence that the last paragraph of the letter was the disclaimer whose purpose was to protect Dickinsons, while Langran referred to the entire letter a disclaimer in both his witness statement and oral evidence.

216. When we conclude that the appellant's witness evidence represents a reconstruction of possible and plausible interpretations of the advice letter with the hindsight of the legal issues that are alive in this appeal, we mean that the evidence of Mr Tucker and Mr Langran was coloured by their knowledge of the desired legal outcome that could flow from their testimonies. Consequently, in making our findings of fact, we have given more weight to the documentary evidence as the contemporaneous records before corroborating with witness evidence as the 'best approach' according to *Gestmin*:

> '[22] In the light of these considerations, the best approach for a judge to adopt in the trial of a commercial case is, in my view, to place little if any reliance at all on witnesses' recollections of what was said in meetings and conversations, and to base factual findings on inferences drawn from the documentary evidence and known or probable facts. This does not mean that oral testimony serves no useful purpose – though its utility is often disproportionate to its length. But its value lies largely, as I see it, in the opportunity which cross-examination affords to subject the documentary record to critical scrutiny and to gauge the personality, motivations and working practices of a witness, rather than in testimony of what the witness recalls of particular conversations and events. Above all, it is important to avoid the fallacy of supposing that, because a witness has confidence in his or her recollection and is honest, evidence based on that recollection provides any reliable guide to the truth.'

Findings of fact as regards Tucker's advice

217. The precise terms of the instructions from Langran to Tucker in relation to carrying out a review that resulted in the advice letter of 7 August 2008 are not on record. From obtainable evidence, we find:

(1) The first instruction given by Langran by email dated 17 July 2008 to Tucker was to call Forbes to discuss the Scheme, but the email itself has not been produced.

(2) Langran, on behalf of Delphi, gave instructions to Tucker to review the Scheme, but there is no written record of the instructions given by Langran, who stated in evidence that he had probably asked Tucker by telephone to review the Scheme.

(3) The transcript of the phone call between Tucker and Cowen, Tucker described his role as reviewing the way they [i.e. Clavis] had put the Scheme together and Tucker accepted this was accurate in evidence.

218. The only documentary evidence extant is Tucker's letter of 7 August 2008. We accept the appellant's witness evidence that the letter was delivered by hand when Tucker met with the directors of Delphi on 7 August 2008, and that Tucker's verbal advice during the meeting

would not have been differently phrased from his written letter. There is no written record of the substance of the meeting with the directors on that day.

219. There is the transcript of the phone call Tucker made to Cowen on 7 August 2008 while Tucker was still on Delphi's business premises. The phone call to Cowen would appear to be made during the day's meeting with the directors to resolve some issues that emerged during the discussion. In our view, the best commentary to interpreting Tucker's letter is the transcript of the telephone conversation Tucker had with Cowen on the same day.

220. We consider the advice letter of 7 August 2008 is to be read for its ordinary meaning, and by reference to any supportive information from the transcript of the phone call to Cowen. On this basis, and by reference to the transcript, we make the following findings of fact.

(1) Tucker informed Cowen that '[his] *role in all of this is really to review the way [Clavis/Herald] put the scheme together*', and this was stated by Tucker to interject Cowen who was in the flow to impress Tucker of the legal significance of *Sempra*.

(2) From Tucker's own statement of his role in this review, and his nonchalance to the significance of *Sempra* as lending support to the efficacy of the Clavis Arrangement as a tax avoidance scheme, and Tucker's evidence that he understood his instruction to be to review the '*technical aspects of a tax arrangement*' (emphasis added) a reasonable inference is that the instructions to Tucker did not include a review of the efficacy of the Scheme from a tax perspective.

(3) That Tucker's instructions were centred on the review of the documents and legal instruments to implement the scheme is consistent with the concerns Tucker put forward for Cowen to allay: *'a certain artificiality'*; '*the very narrow gaps when something was forced through … on the bridle*'; '*these reports are too much of a standard*'. Tucker's review involved him looking through the bible of documents, including '*a full blown Jersey discretionary trust for all nine yards of it*' which made his heart drop.

(4) That Tucker saw his role in carrying out the review was for the purpose of ensuring that Dickinsons could assist Delphi to get the documentary trail in the right place and at the right time is consistent with what Tucker said to Cowen: '*if I am getting involved with it … we want to make sure that we've not spoilt the ship*'.

(5) Tucker admitted to Cowen of the fee earning prospect for his firm whereby Dickinsons would assist Delphi with the documentation if Delphi entered the Scheme: '*we will be charging our client because we will be getting involved in making sure all the documentation is done at the time and not all pre-signed and the like*.'

(6) Tucker's review would appear to cover the economics of entering the scheme: the costs and benefits analysis whereby he reached the conclusion that '*the costs will kill it*' and there would be no point going in for just £1m given the overheads, but a minimum of £2m or £2.5m; of insurance cover. It is a reasonable inference that in this cost-benefit analysis, Tucker would have taken into account the tax savings the Scheme was supposed to procure in obtaining a CT deduction and no PAYE/NICs payable.

(7) The economics of the Scheme must have included the tax savings having to more than cover the 10% that Clavis/Herald were to deduct from each invoice total. Tucker referred the below 50% possibility of retrospective legislation stopping the CT deduction as '*a downside*', and remarked on '*not an employment point*'.

(8) The phone call started with the question which Tucker said he could not 'bottom out', and the question was concerned with what was going to happen to the monies allocated to sub-trusts at the point of exit.

(9) The concern was allayed by the proposition of a 'fallow year' (allegedly from counsel) for a sub-trust after the cessation of employment. The call that started this question finished with Tucker's summary of his understanding: '*leave a fallow year and then the loan can be written off without being benefit*'.

(10) A reasonable inference from this question that started and finished the phone call and was the dominant chord running through the conversation is that Tucker's review was focused with the logistics in implementing the Scheme, and the concern behind this question was how the Scheme would work in reality, so that the trust monies would find their way home, so to say, without incurring a tax charge.

221. Based on our findings on the transcript, we now turn to the advice letter of 7 August 2008 that has been subjected to intense scrutiny to make our findings of fact.

(1) The letter was dated 7 August 2008, and was taken in person by Tucker to attend his meeting with Delphi's directors on the same day, during which the content of the letter was related and discussed with the directors. The meeting went on for an hour and a half, and Tucker then made the phone call to Cowen to help him 'bottom out' the issue as how the trust monies were to make a final exit without a tax charge.

(2) The letter started with the *caveat* that Tucker had not yet taken up any external references on the scheme with other accountants.

(3) The advice remarked on 'the merit of simplicity' of the Scheme by using 'an exemption within anti-avoidance rules' by way of sub-contracted services to 'circumvent' the rules applicable to 'the direct use of an EBT' to obtain a CT deduction, as per Thornhill's Opinion. That the Scheme was trying to utilise an exemption within the anti-avoidance rules applicable to EBTs was clear from the outset to Tucker.

(4) The dispensation from DOTAS reporting, the off-shore features in the Arrangement to bypass tax on loan interest payable by the sub-trusts, the cost-benefit analysis to set the entry level for costs to be outweighed by the anticipated tax deductions – all point towards the purpose of the Scheme as for tax avoidance.

(5) That the purpose of the Scheme was about avoiding tax was clear to Tucker as the adviser and Delphi's directors as the recipients of the advice. Tucker accepted in cross-examination that the Scheme was intended to save both corporation tax and income tax, as it would not be '*sensible*' otherwise. Langran confirmed in cross-examination that he had been aware that the Scheme sought to provide a corporation tax deduction without giving rise to an income tax liability: '*the purpose of the scheme was to try and avoid both taxes*'; and agreed that there would be no point in doing it otherwise. We find that it is in view of the avoidance of *both taxes* that Tucker considered the Scheme as a form of '*aggressive tax planning*'. We reject the interpretation that '*any* aggressive tax planning' at paragraph 11 is a reference to some notional scheme and not the Clavis Arrangement. We find that the very context of paragraph 11 means that the description of 'aggressive tax planning' was intended to apply to the Clavis Arrangement.

(6) With the tax avoidance purpose being inherent in entering such a Scheme, the letter then outlined the possible areas of risk at paragraph 9, and correctly identified the likely implications for Inheritance Tax, Income Tax and Corporation Tax.

(7) Crucially, the interaction between Corporation Tax and Income Tax is identified at paragraph 9(4) of the letter, although the risk was in anticipating CT planning failing (rather than 'the "income tax" side' failing as it turned out to be).

(8) The tax savings anticipated to be delivered by the Scheme was firmly in the cost-benefit matrix, and the listing of *tax* risks (not commercial risks) in paragraph 10 follows on logically to advise the appellant to obtain '*another Counsel Opinion from a barrister other than the original one*' – to address the tax risks (not commercial risks). In the context of Thornhill having been referred to in no uncertain terms at paragraph 4 of the advice letter: 'the opinion of Andrew Thornhill a well respected QC at Pump Court Tax Chambers', we find that Tucker was very clear and unequivocal that Thornhill's opinions should not be taken as the last word as regards the exposure to tax risks on proceeding with the Scheme.

(9) While the advice contained in paragraph 10 is bracketed by 'My normal and usual advice for any such scheme' and 'if the Promoters of the arrangements are prepared to permit this', that does not detract from the fact that the recommendation that the appellant should seek independent counsel's opinion is unequivocal due to the prospect of litigation. We find that Tucker assessed that the prospect of litigation was close to certain and is contained in the sentence in paragraph 11: '*any aggressive tax planning will always be open to attack from HMRC and their current policy is to litigate everything*' (emphasis added). We find that the adoption of the wording 'will always' and 'litigate everything' was not intended to be read as hyperbole, but was chosen after deliberation by Tucker and partners in Dicksons who had input into the letter, and that the wording was intended to communicate a close-to-certain prospect of litigation for participating in the Scheme.

(10) We find therefore that Tucker's advice for seeking independent counsel's opinion stated in paragraph 10 and reiterated in paragraph 13, was firmly set within the context of the close-to-certain prospect of litigation in paragraph 11. There follows more costs analysis by relating the promoters' undertaking to fund the first stage of litigation, but any onward litigation would be '*very expensive*' (paragraph 12). We find that both paragraphs 11 and 12 are substantive in detail, and are not included in the letter merely for window dressing purposes to back up a supposed disclaimer. These paragraphs are included to give substance to the kernel of the advice in paragraph 10, and as reiterated in paragraph 13: '*I would recommend that the matter be put before independent counsel*'.

(11) We find that the written advice to seek independent counsel's opinion was given with the close-to-certain prospect of litigation in mind, and this finding is consistent with Tucker's oral evidence: '*In terms of asking for another barrister to look at the case, it struck me that with the amounts involved it would give additional defence against any attack that the clients had been negligent in entering into any such arrangements*.'

(12) The concluding paragraph where Tucker seemed to be equivocal in his position is to be read in the light of the foregoing paragraphs 10 to 13. On that basis, we find:

(a) Given the close-to-certain prospect of litigation, Tucker was unable to recommend the Scheme (in the sense of giving his professional endorsement);

(b) However, if the directors of Delphi decided to go ahead '*having taken a commercial view*' (i.e. as a commercial decision based on weighing up the costs for entering into the Scheme against the double tax savings in terms of both PAYE/NICs and corporation tax, factoring in the risks associated with the close-to-certain litigation);

(c) Then Tucker would assist Delphi to implement the Scheme properly as made clear to Cowen in the phone call on the same day: '*if I am getting involved with it ... we want to make sure that we've not spoilt the ship*', and Dickinsons could derive the benefit from earning additional fees if Delphi chose to proceed.

Issue 3(b) Conclusion on basis for 'careless penalty'

222. We find that the appellant in appointing Tucker to review the Scheme did not fall short of the standard of being a prudent and reasonable taxpayer, since Tucker's qualification and experience is commensurate with the task he was entrusted to do.

223. It was suggested by Mr Sherry that the appellant would seem to have been penalised for appointing an adviser who was extra cautious, with the corollary of the suggestion being that it would have been better for the appellant to appoint a less cautious adviser who would not give such a recommendation. We are of the view that a taxpayer who resorts to obtain the advice of an unsuitably qualified adviser can be found to be not acting with due care, as illustrated by the facts in *Hicks*[22], and Mr Sherry is right not to pursue this argument further.

224. In *Hicks*, the Upper Tribunal, in the context of 'carelessness' for s 29 TMA discovery assessment purposes, held that it was 'careless' of Mr Bevis (Mr Hick's adviser) to take on the role of giving tax advice in relation to the deductibility of the expenditure as wholly and exclusively for the purposes of Hick's pre-existing trade, which was 'clearly wrong' as found by the FTT in *Hicks*. Based on the FTT's fact-findings, the UT remade the FTT's decision and allowed HMRC's appeal. The UT in *Hicks* concluded at [140]:

> 'By taking the role of a tax adviser to Mr Hicks in this respect, Mr Bevis has to be judged by the standard of a reasonably competent tax adviser giving advice to a taxpayer on this matter. The advice which Mr Bevis gave was not advice that could have been given by a tax adviser of reasonable competence.'

225. Contrary to Mr Bevis in *Hicks*, we find Mr Tucker to be of reasonable competence in giving the advice as he did. Tucker confirmed in evidence that the letter of 7 August 2008 was not a generic letter but was a bespoke piece of advice, and had been reviewed by two other partners in Dickinsons who assisted in editing the letter. We find the advice letter to be thorough in its scope, professional in its recommendations, clear and concise in naming the risks, sagacious in delineating the extent of endorsement, and befitting as a letter of this nature for which Delphi would have been charged a fee to obtain the advice.

226. The kernel of Tucker's advice is encapsulated in his overall evaluation of the Clavis Arrangement– '*Whilst the scheme seems to be most effective any aggressive tax planning will always be open to attack from HMRC*'. There are two aspects to this evaluation:

(1) First, Tucker was prepared to say that the Scheme '*seems most effective*', but was careful in not staking his opinion on the ultimate effectiveness of the Scheme. Tucker was fully aware that the Scheme relied on the novel feature of the service and goods exemption, and in that respect departed from the standard EBTs. Tucker was circumscribed his endorsement of the Scheme with the verb '*seems*' to qualify 'most effective'. Plainly, why Tucker considered that the Scheme only *seems* to be most effective was because of the 'possible areas of risk' as identified at paragraph 9.

(2) Secondly, Tucker's assessment of the close-to-certain prospect of a challenge from HMRC was grounded on the factual statement in paragraph 11: '*Enquiries have been raised into … companies which have utilised these arrangements*.' At the relevant time, Tucker was also a serving member of the Council of ICAEW, and of the Tax Committees of the Tax Faculty of ICAEW. We infer that Tucker would have been aware of the Institute's representations to HMRC on a range of tax issues, including those on the tax treatment of contributions made to EBTs. Tucker's professional involvement at the Institute level as a council member and a committee member of the Tax Faculty of ICAEW lent extra weight to his evaluation that '*any aggressive tax planning will always*

[22] *HMRC v John Hicks* [2020] UKUT 0012 (TCC).

be open to attack from HMRC'. We accord due weight to Tucker's advice that HMRC's 'current policy' was to 'litigate everything' as coming from a professional not only with years of practice experience as a tax specialist and a STEP qualified practitioner, but with additional expertise and considerable institutional knowledge gleaned from years of involvement at the Council and Faculty levels of the ICAEW.

227. We find Tucker to be a conscientious professional, and would have kept abreast with tax law development relevant to any advice he would undertake to give to his clients. Tucker's advice was grounded in the understanding that the Clavis Arrangement was not the same as the 'standard' EBTs litigated in *Dextra* and *Sempra*, (and possibly why it was irrelevant for Tucker to hear out Cowen when the latter sought to impress Tucker of the taxpayer's win in *Sempra* over the phone). Tucker was aware of 'the possible areas of risk' raised by the Clavis Arrangement that would be open to challenge by HMRC, and quite properly itemised areas of risk in the advice letter for the directors' attention. Unlike Mr Bevis in *Hicks*, Tucker did not stray beyond his competence by an attempt to pronounce on the efficacy of the Scheme from the legal point of view in respect of the areas of risk he had raised, and hence, recommended that the appellant should obtain independent counsel's opinion to address the list of tax issues.

228. The appellant, having instructed Tucker as a suitable adviser to carry out a review of the Scheme, was given the kernel of advice that (i) the Scheme 'seems most effective' (but not outright effective because there are these areas of risk identified), and that (ii) HMRC 'will always' challenge 'any aggressive tax planning' (such as the Clavis Arrangement). The conclusion that Tucker '*can not formally recommend such a scheme to [Delphi] as there is certainly a risk in entering such arrangements*', in our view, fell far short of a full endorsement for the Scheme. On the contrary, the conclusion conveyed the certainty of a risk in entering into the Scheme.

229. It is apt for us to ask what is the risk being referred to in Tucker's conclusion viz. *there is certainly a risk in entering such arrangements*. Ultimately, it is plain for all concerned, Clavis/Herald, Tucker and Delphi's directors, that the purpose of the Scheme was to avoid both PAYE/NICs and Corporation Tax. It is plain that the attraction of the Scheme to Delphi's directors was the prospect of extracting profits out of Delphi while paying as little to no tax as possible. Tucker was basically advising the directors that *there is certainly a risk* that the Scheme fails to deliver the tax savings as promised, with the corollary that Delphi would be found as having underdeclared its tax liabilities.

230. The question for the Tribunal is what a prudent and reasonable taxpayer – intent on fulfilling its obligations to render accurate returns to account for all its tax liabilities – would have done when faced with such advice as given by Tucker by letter dated 7 August 2008 which concluded with an unambiguous lack of endorsement of the Scheme due to the certainty of a risk in being found to have underdeclared its tax liabilities.

231. The substance of Tucker's advice and his conclusion demands a response from a prudent and reasonable taxpayer intent on meeting its obligations to render correct returns to account for its tax liabilities – but the appellant did nothing in response whatsoever. It is in this regard that we conclude that the appellant fell short of the standard of being a prudent and reasonable taxpayer by taking no action to address the possible areas of risk raised in Tucker's letter in order to enable itself to meet the obligations in rendering accurate and complete returns to account for all its tax liabilities.

232. Whilst one obvious action to take by a prudent and reasonable taxpayer on receiving Tucker's advice would be to obtain independent counsel's opinion as recommended, that was by no means the only response open to Delphi on receiving Tucker's advice. For the avoidance of doubt, we conclude that the appellant had failed to take reasonable care to avoid inaccuracy

not because it did not obtain independent counsel's opinion per se, but because it took no action whatsoever to address the certainty of a risk (namely the Scheme failing and tax liabilities owing) that was cogently explained and plainly stated in the advice letter of 7 August 2008.

233. On one interpretation, and by reference to Tucker's understanding of his instruction in terms as stated to Cowen in the phone call, that was '*to review the way [Clavis/Herald] put the scheme together*', Tucker's remit might have been more focused on the logistics of how monies were supposed to flow through the Scheme to find their way home to the directors eventually, and on the legality of each implementing steps of the Scheme (including exit on cessation of employment) than on the critical concern in this appeal – that is to say, whether Delphi would be meeting its taxpayer's obligations in rendering complete and accurate returns to account for its tax liabilities by entering into the Scheme.

234. The interpretation that the critical concern in this appeal was not uppermost in the directors' minds when instructing Tucker is consistent with the fact that there was no action taken in response to the substantive advice on the areas of risk that would have direct bearing on Delphi's obligations as a taxpayer to render accurate and complete returns. This interpretation is also consistent with the part of Tucker's conclusion in the advice letter where he referred to the alternative of the directors wishing to proceed '*having taken a commercial view*'. Taking a commercial view as the premise for proceeding has the implication of setting aside the critical concern that was inherent in '*there is certainly a risk*' in the immediately preceding sentence. Taking a commercial view in terms of the supposed cost-benefit analysis from avoiding taxes over and above the critical concern as a taxpayer to render complete and accurate returns is a failure to take reasonable care to avoid inaccuracy for Sch 24 purposes.

235. The penalties are pursuant to para 1 Sch 24, and para 3(1)(a) defines an inaccuracy as 'careless' '*if the inaccuracy is due to failure by P [i.e. the taxpayer]*[23] *to take reasonable care*'. The causative link, as we understand it, is derived from the statutory wording of 'due to', which means (per Oxford English Dictionary): '*attributable to, ascribable to'* (as an adjectival phrase) or '*because of, on account of, owing to*' (as a prepositional phrase).

236. We conclude that there was a failure to take reasonable care on the part of the appellant for Sch 24 purposes, and that the inaccuracies in the P35 returns were attributable to the appellant's failure to take reasonable care in terms as discussed above. We conclude therefore that HMRC have met the burden of proof that there was a failure on the appellant's part to take reasonable care under the terms of para 3(1)(a) of Sch 24 for a careless penalty to be imposable on all tranches.

Issue 3(c): the chain of causation and para 18(3) defence

237. We consider Mr Sherry's submissions for the appellant as having two aspects.

(1) First, that the appellant had taken reasonable care to avoid inaccuracy and we consider this aspect under the terms of para 18(3) defence.

(2) Secondly, that HMRC have not established the causal link that failure to obtain a second opinion was the carelessness which led to the inaccuracies in the PAYE returns.

Submissions for the appellant on having taken reasonable care

238. The conclusion we reach for Issue 3(b) should be sufficient to determine the appeal, unless the appellant satisfies us that it had taken reasonable care to avoid inaccuracy under the terms of para 18(3) Sch 24. The appellant has referred to *Bayliss v HMRC* [2016] UKFTT 500(TC), *GC Field & Sons Ltd v HMRC* [2021] UKFTT 297 (TC), and *Avonside Roofing v*

[23] 'P' is defined under para 1(1)(a) of Sch 24 as the person who '*gives HMRC a document of a kind listed in the Table below*', and for present purposes, P being the taxpayer shall suffice.

HMRC [2021] UKFTT 158 (TC) for its submissions on carelessness. Mr Sherry's submissions for the appellant are summarised as follows.

(1) It is not accepted that the appellant instructed or received advice from Tucker only. Clavis held themselves out to be experts in the field and provided advice on the Arrangement, shared the advice in the six Counsel Opinions, and gave assurances and 'comfort' on multiple occasions that the Arrangement was 'legitimate' and 'worked'.

(2) Through discussion with Tucker, the appellant also relied heavily on the six opinions produced by Andrew Thornhill KC who was 'the respected QC' and 'the representative in *Sempra* and to [Langran's] knowledge he had beaten, won a victory against HMRC'.

(3) There is nothing in case law authorities that suggests that in order to take reasonable care, a taxpayer has to specifically instruct a professional in writing or otherwise. Mr Sherry said that *Bayliss* at [15] makes it clear that unsolicited advice and assurances given by one's advisers and the promoters of a scheme may be relied upon.

> '… [the accountant] explained that there was a "tax loophole" under which a loss could be created to offset the gains. We accept the appellant's evidence that he understood this to mean a fallow in the tax rules that allowed less tax to be paid, and that he was assured that the arrangement was legal.'

(4) Tucker's letter of 7 August 2008 should be interpreted by reference to what the author and the recipient knew or understood about tax avoidance arrangements and in particular EBTs at the time. (The Tribunal is asked to refer to 'the findings of the Morse Report in this respect'.) Mr Sherry also said the letter should not be read with the benefit of hindsight or with knowledge of what transpired in the case law many years later.

(5) Referring to *Hicks* at [287] (which is an impossible paragraph reference[24]), Mr Sherry submits that 'entering into a scheme is not in and of itself careless or deliberate'.

(6) The suggestion of a second opinion is Tucker's August 2008 letter 'is not as clear cut as HMRC have interpreted it'; that 'there is ambiguity in the letter in that it refers to "my normal and usual advice would be" and then a recommendation qualified by "considering he amount you may wish to place in these arrangements' (Mr Sherry's emphasis). It is submitted that the advice given by Tucker 'was directed to the question of whether or not the appellant should enter into the Arrangements in the context of a commercially driven decision in light of the amounts potentially involved'.

(7) 'One key point' emphasised by Mr Sherry is that the appellant 'did obtain independent advice in the form of [Tucker's] verbal and written advice'; that Delphi did not just rely on the advice from the Scheme promoters.

(8) Further, that Tucker provided a 'recommendation' to obtain a second counsel's opinion was understood to be simply a '*suggestion*' which '*did not tell [Delphi's directors] that they had to do it*'. It is submitted that it does not 'automatically raise the objective standards by which the appellant has to be judged'.

(9) Mr Sherry submits that Tucker as the author of the letter of advice stated in evidence that, in his view, a second counsel's opinion '*would give additional defence*

[24] The FTT decision of *Hicks v HMRC* [2018] UKFTT 0022 (TC) has 217 paragraphs in total, and the UT decision of *HMRC v Hicks* [2020] UKUT 0012 (TCC) has 206 paragraphs in total. The citation reference of '*Hicks* at [287]' at paragraph 65 of the appellant's written submissions is therefore incorrect, since neither the FTT nor the UT decision would have a paragraph number 287, and we have not sought to trace what the correct reference might have been intended by Mr Sherry.

against any attack that the clients had been negligent in entering into any such arrangements'. Mr Sherry argues that the 'recommendation' was therefore reflective of Tucker's 'very cautious mindset and represented a "belt and braces" approach'.

(10) Mr Sherry invites the Tribunal to consider: would a reasonable and prudent taxpayer in these circumstances (and one who understood the recommendation to be a disclaimer) have taken *additional* Counsel's advice on the proposal? And submits that the answer is clearly, no.

Findings of fact in relation to submissions for the appellant

239. We consider the submissions made for the appellant by making the relevant findings of fact as follows in the order of the numbering of Mr Sherry's submissions.

(1) *Advice from Clavis* – We accept that the appellant drew 'comfort' from Clavis' advice that the Arrangement was 'legitimate'. We find that to ascertain the legality of the Scheme was of '*paramount importance*' to Delphi, as testified by Langran, who spoke of the directors' concern not to do anything which would jeopardise their Financial Conduct Authority ('**FCA**') registration because the FCA registration was '*vital*'; hence '*If there was any hint that [the Scheme] was illegal, criminal, bad, naughty, etc. we would not have touched it with a barge pole*'. The emphasis of taking advice from Clavis was to ensure the Scheme was '*legal*', '*above board*', '*legitimate tax avoidance*' – as stated by Langran, but that paramount concern for legality did not equate with taking reasonable care to ensure that Delphi did not under-declare its tax liabilities.

(2) *Reliance on Thornhill's opinions* – In relation to Thornhill's Opinion (or his six opinions) being '*the cornerstone*' as Langran put it for Delphi's belief that the Scheme was legally and technically sound, we find that this assurance and comfort to be of the same nature as Clavis' advice.

(a) In other words, Delphi was careful to make sure that it would not jeopardise its FCA registration in entering the Scheme, but that in our view, did not automatically commute to taking reasonable care to avoid Delphi understating its tax liabilities.

(b) Further, the significance of *Sempra* or Thornhill's opinions was over-rated, and this was not just in hindsight. It was evidently clear from the transcript that Tucker was not as enamoured by the taxpayer's win in *Sempra* as Cowen, or was Tucker going to take Thornhill's opinions as the last word on the matter. Tucker's advice, whilst clearly stating Thornhill's credentials, was categorical in pitching the recommendation to be '*independent*' and from '*a barrister other than the original one*' should be obtained.

(c) It is a reasonable inference that Tucker's advice was given in the full knowledge that Clavis would of course only show counsel opinions endorsing the Scheme, and Tucker showed sagacious scepticism by *not* taking Thornhill's opinions as the last word given the Clavis-Thornhill alliance.

(d) *McClean v Thornhill*[25] was concerned with a claim of professional negligence against Mr Thornhill and was brought by participants in a tax avoidance scheme investing in LLPs taking part in film distribution. Thornhill had provided opinions to the LLPs regarding the arrangements, and Zacaroli J held that the participants could not reasonably rely on those opinions (by Thornhill) and ought to have obtained their own independent advice, which was precisely what Delphi was advised to do by Tucker.

[25] *McClean & Ors v Thornhill* [2022] EWHC 457 (Ch).

(3) *Legitimate tax avoidance scheme* – We accept that the directors of Delphi, like the taxpayer in *Bayliss* were assured that the Scheme was a legitimate tax avoidance scheme, on reliance of Clavis' assurance. This does not assist the appellant, however, since the Scheme being 'legal' (in the sense that the transactions involved were not a sham) has no bearing on the correct tax treatment for the transactions in question. It is accepted that the appellant took reasonable care to ensure the legality of the Scheme – but that was no proof that the appellant had taken due care to avoid understating its tax liabilities. The central flaw in the submissions for the appellant is to conflate (if not to confuse) taking due care to ensure the legality of the Scheme with taking due care to avoid inaccuracy in stating Delphi's tax liabilities.

(4) *Advice letter read in the light of the Morse Report* – We reject the proposition that the reception of Tucker's advice letter by its recipient should be interpreted with the *Morse Report* in mind. This proposition is utterly flawed for the following reasons.

(a) We have found that the Morse Report does not support what the appellant is asserting in reliance thereon. We follow the Upper Tribunal in *Hoey* that the Morse Report shows that there was no settled view of the law at the relevant time to support the appellant's unsubstantiated claim that there was any prevailing practice that the contributions into Clavis kind of EBT could obtain a CT deduction while <u>at the same time</u> allowing no PAYE/NICs to be payable on loans made to the directors via the sub-trusts.

(b) Quite apart from the irrelevance of the Morse Report, this submission is devoid of evidential or legal basis that the fact-finding tribunal should make a finding of fact of the interpretation of the advice letter by its immediate recipients by reference to the Morse Report published a decade later.

(c) In our view, so far as the interpretation of the advice letter is concerned, Tucker's state of knowledge at the time when he was giving his advice was the only relevant reference point (not what the Morse Report said a decade later). It was clear that the close-to-certain prospect of a challenge from HMRC of the Clavis Arrangement was a central concern for Tucker, as stated in paragraphs 11 and 12 of the letter. Insofar as the Morse Report has any relevance to interpreting the content of the advice letter, the Report would seem to lend support to Tucker's concern that there was not settled view of law for Delphi to rely on.

(d) We also have regard to the caveat stated by Tucker that he had 'not taken up external references on the scheme with other accountants', which would suggest that Tucker had not canvassed widely other accountants' views to inform him of the advice he would be giving. The reference to the Morse Report might arguably have some relevance if Tucker had canvassed the wider view of the accountancy profession at the time, so what the Morse Report reported a decade later of practitioners' views could not have any relevance to the state of knowledge Tucker had at the time of giving his advice.

(5) *Entering into a scheme is not in itself careless* – We accept Mr Sherry's written submission at paragraph 65 on this point, even though we are unable to trace his citation reference to *Hicks* at [287]. We accept that Delphi took reasonable care to ascertain the legality of the Clavis Arrangement before entering into the Scheme, but that in itself does not prove that the appellant took reasonable care to avoid inaccuracy in terms as required under para 18(3) Sch 24.

(6) *That Tucker's 'normal and usual advice <u>would be</u>'* – The emphasis of Tucker's ambiguity in casting his 'normal and usual advice would be' makes no difference to our

findings of fact as detailed in addressing Issue 3(b). The important finding of fact as regards Tucker's advice letter is that there was no outright, unqualified professional endorsement for entering the Scheme from Tucker in the context of his view of HMRC's policy to challenge '*any aggressive tax planning*'. The lengthy submissions for the appellant to circumscribe Tucker's advice in paragraph 10 of the letter are to suggest Delphi's case as: (a) somehow qualifying the normal and usual advice by *exception*, or (b) being contingent upon Clavis' permission[26]. These submissions might have been relevant for submissions on 'reasonable excuse' for failure to follow advice. However, the relevant defence here is not whether the appellant had a reasonable excuse for failing to follow advice, and Sch 24 has no provision for 'reasonable excuse'.

(7) *That Delphi did not just rely on Clavis' advice* – we accept that Delphi took due care in instructing Tucker who was suitably qualified to advise them to the extent that was documented in the advice letter. The critical point is that after receiving Tucker's advice as discussed for Issue 3(b), Delphi took no action in response to the advice.

(8) *That recommendation was a 'suggestion'* – Tucker was the adviser, and the ultimate responsibility of taking reasonable care to avoid inaccuracy rests with Delphi, not its adviser. To downplay the recommendation as a mere suggestion is again a submission that the appellant had a reasonable excuse not to follow the advice.

(9) *That recommendation was reflective of Tucker's very cautious mindset* – we have made relevant findings of fact as to Tucker's competence as an adviser. We are unable to make contrary finding that Tucker's advice was somehow over-cautious as Mr Sherry submits. We have regard to the fact that Tucker's advice to obtain independent counsel opinion in paragraphs 10 and 13 was sandwiched by details in paragraphs 11 and 12, and his overall evaluation of the Scheme was well founded, properly reasoned, and factually substantiated as set out under Issue 3(b).

(10) *Would a reasonable and prudent taxpayer take additional counsel's advice?* – The question cast by Mr Sherry, while intended to be rhetorical, is addressed here as a factual question. In this respect, we have regard to the long-standing professional relationship between Tucker. We find the directors of Delphi to be sophisticated taxpayers, and had formerly considered other tax avoidance schemes. We find that Tucker's letter did not give unqualified endorsement of the Clavis Scheme and that it was Tucker's view that '*any aggressive tax planning will <u>always</u> be open to attack from HMRC*' – the adverb 'always' conveyed certainty of HMRC's challenge on the Scheme that a prudent and reasonable taxpayer would have taken further action to ascertain the tax savings purported to be delivered by the Scheme would be supported by another counsel's opinion. Further, the certainty of HMRC's challenge was grounded in the fact that enquiries had already been opened into scheme users as related by Tucker's letter. We conclude that a prudent and reasonable taxpayer, with the sophistication as the appellant's directors, and having due regard for its obligation as a taxpayer to deliver documents that were accurate in stating its overall tax liabilities, would have obtained additional counsel's advice given the certainty of the prospect of challenge from HMRC.

240. In summary, we reject Mr Sherry's submissions as flawed for two main reasons:

(1) The submissions, at most, establish that the appellant had taken reasonable care to establish the legality of the Scheme before entering into it, but that does not prove that the appellant had taken reasonable care to avoid inaccuracy in its taxpayers' returns. The

[26] For completeness, we note Officer Barraclough's evidence that while he did not know if Clavis would have permitted the appellant to obtain further advice, he said other users had done so.

flaw in this aspect of submissions is to conflate or to confound the care taken to establish the legality of the Scheme with the reasonable care required to avoid inaccuracy in general for para 18(3) purposes.

(2) The submissions amount to making a defence that the appellant had a reasonable excuse for failing to follow the advice stated in Tucker's letter. The flaw in this respect is that the statutory defence for Sch 24 purposes is not whether the taxpayer had a reasonable excuse for the inaccuracy that led to a loss of tax, but whether the taxpayer had taken reasonable care to avoid inaccuracy (in general).

241. We conclude that the appellant has not proved, on the balance of probabilities, that it took reasonable care to avoid inaccuracy (in the sense of being intent that the returns it rendered to HMRC to account for its tax liabilities would be complete and accurate) to avail itself of the defence under para 18(3) Sch 24.

Whether 'causal link' between alleged failure and loss of tax

242. Mr Sherry submits that HMRC have failed to establish that there is a causal link between the alleged failure and the loss of tax, as stated at paragraph 53 of his skeleton argument:

> 'Applying the test laid by the case of *Bayliss*, the real question is whether the Company carelessly filed an incorrect return. The focus is therefore on the alleged error in the return and whether the Company was careless in making that error. In this case, as the Company fully relied on the expertise of Clavis (and their Queen's Counsel Opinions) as promoter of the Arrangements, on its accountants and its auditors, there can be no suggestion that it failed to take care when implementing and carrying out the first three tranches of Arrangements. In light of assurances that the Arrangements were above board as well as delivering remuneration in a CT tax efficient manner, the fact that the Supreme Court decided nine years later that there was a PAYE/NICs liability attached does not demonstrate carelessness in submitting a P35 on the reasonable assumption that income tax was not deductible. … In any event, if the Company had sought a second Opinion, they may have been advised that a Corporation Tax deduction was not available (although this is highly unlikely in light of the prevailing practice and thinking about EBTs at the time) but this would not have informed the Company on how to fill and submit its P35 return. Had the Company sought a second Opinion at the time, the FTT is invited to hold that, in the light of the authorities [i.e. *Sempra* and *Dextra*] (which were the extant authorities at the time), such an Opinion was highly unlikely to have differed as to the PAYE position (there would have been no authority to base a contrary view on).'

243. The crux of the appellant's argument is that its failure to obtain a second opinion did not cause the inaccuracies in the P35 returns. It is submitted for the appellant that it is highly unlikely that any such opinion would have been that the amounts allocated to an EBT were subject to PAYE/NICs so that such amounts ought to be included in the appellant's P35 returns.

244. In making the appellant's submissions on causation, Mr Sherry refers to *Bella Figura*[27] where the UT considered the test of 'carelessness' for the time-limit issue under s 36 TMA:

(1) The UT did not hold that a reasonable taxpayer would have obtained *additional* advice; rather, it upheld the FTT's finding that carelessness was established because the taxpayer company Bella Figura Limited ('**BFL**') obtained *no* advice.

(2) The UT found at [61] that the FTT erred in ignoring two relevant considerations:

[27] *Bella Figure Limited v HMRC* [2020] UKUT 120 (TCC).

(a) That the taxpayer had taken steps to select an appropriate practitioner to prepare documentation in the knowledge that the documents would need to meet specific requirements. The UT then observed:

> 'The FTT should have gone on to consider whether even in the absence of specific advice, BFL obtained implicit reassurance that the loan would qualify which was enough to amount to the taking of reasonable care' (emphasis original).

(b) That the FTT did not take into account the fact that s36 of TMA is concerned with the question of whether a failure to take reasonable care causes a loss of tax.

(3) In the appellant's case, HMRC have failed to show the causal link between what they perceive to be misconduct by the appellant and the fact that PAYE should have been deducted from the payments made to the sub-trusts. In other words, HMRC cannot show that the alleged failure to seek a second counsel's opinion (in light of reliance on advice by Clavis, Thornhill's opinions, accountants/auditors that the Arrangement would deliver the tax consequences sought) caused the alleged loss of tax.

HMRC's submissions in reply

245. Ms Choudhury's reply to the 'causal link' submission is as follows:

(1) As confirmed by Tucker's evidence, the P35 returns were completed by Dickinsons on the appellant's instructions in accordance with the views of Clavis and counsel's opinions. HMRC had initially opened enquiries into the appellant's company tax returns, which is 'unsurprising', since 'the accounts showed an amount being paid by way of directors' remuneration and the enquiry enabled HMRC to determine what the payment was for'. In turn, a check was not carried out of the appellant's PAYE returns because HMRC issued determinations based on the information obtained during the enquiries into the appellant's CT returns.

(2) The appellant's submission is 'wrong' that a second opinion would not have been different from Thornhill's because:

(a) First, there was no 'settled view' at the time.

(b) Secondly, the appellant relies on the expertise of Clavis and on Thornhill's opinions which 'it was not entitled to do so', and 'ought to have obtained its own advice' as recommended by Tucker.

(c) Thirdly, the fact that Tucker had recommended the appellant to obtain a second opinion from independent counsel suggests that he considered there was a possibility that there would be a difference of opinion, and this would protect the appellant from being considered negligent.

(3) HMRC submit that a second opinion would have highlighted the following points, none of which were properly considered in Tucker's letter:

(a) The Scheme was seeking to secure a CT deduction without the payment of income tax/NICs and there was no judicial endorsement of that tax treatment;

(b) HMRC did not accept that income tax/NICs were not payable in respect of amounts received from an EBT and were continuing to challenge this point in litigation; and

(c) A transaction may not be illegal but nevertheless constitutes tax avoidance.

(d) Further, it is submitted that if the appellant had obtained a second opinion and it had endorsed the Scheme (despite HMRC's views at the time), HMRC acknowledge that they would have considerable difficulty in establishing that it had

failed to take reasonable care. As confirmed by Tucker in evidence, that was also the reasons Tucker had made the suggestion in the first place.

(e) The fact is that the appellant did not follow Tucker's advice, but instead it claims to have relied on Tucker's advice which itself was based on what had been said by Clavis and Thornhill and which concluded with Tucker recommending the appellant to obtain further advice.

(f) The advice relied upon by the appellant was therefore inadequate. It led to Delphi failing to account for PAYE/NICs in respect of the sums allocated to the directors by the sub-trusts so there was an inaccuracy in the returns for the two years in question which led to an understatement of tax.

Discussion on submissions on 'causal link'

246. The 'test laid by the case of *Bayliss*' in relation to Mr Sherry's submissions on causation is understood to be a reference to [68] of *Bayliss* where Judge Falk (as she was then) observed:

> 'In the absence of subsequent reassurances, completion of a tax return on the assumption that the scheme worked might well have amounted to a negligent behaviour. However, in order for s 95 [TMA] to be engaged HMRC would also have needed to show that there was a causal link between the negligence and the errors in the return.'
>
> Given that HMRC has accepted that the transaction was not a sham this would not be a straightforward point: HMRC would probably need to pursue a line of argument that the errors should have been of sufficient concern to prompt the appellant to seek advice from another tax specialist before completing the return, which should (if the adviser had sufficient expertise) have led to the appellant being advised that the scheme did not work either due to the application of s 16A TCGA or for other reasons. However, HMRC put forward no such argument and it is not obvious to us that such argument would have succeeded.'

247. In terms of the construction of 'due to' as the nexus relevant to Sch 24 provisions, we have considered the relevance of the concept of 'causation' under s 95 TMA and tort liability in some detail. We reject the submissions from the appellant that seek to establish a causal link in the 'but for' sense between the inaccuracies in the P35 returns on the one hand and the failure to obtain independent counsel's opinion on the other. The relevant statute to determine this appeal is Sch 24 FA 2007, and we reject the appellant's submissions on 'causation' as derived from the concept of 'negligence' under the superseded s 95 TMA apposite to tort liability.

248. In terms of fact-findings, Mr Sherry has invited the Tribunal to make a finding of fact in support of the appellant's causation argument that a second opinion from counsel would not have differed from Thornhill's. This is a finding of fact that we categorically cannot make. Not only was there no settled law on the tax treatment of EBTs at the time, but the Clavis Arrangement departed from the standard EBTs by trying to invoke the goods and services exemption. To make a finding of fact that a second opinion would necessarily concur with Thornhill's would be pure speculation.

249. Mr Sherry also submits that causation cannot be made out when the sub-trust allocations were made by independent trustees in the amounts set out in the settlement agreement and on which Delphi paid all the tax due. It is argued that Delphi'a alleged actions or omissions cannot be said to have caused any potential loss of revenue because Delphi did not control the trustees, so the action of the independent trustees could not give rise to the causal link for Delphi's failure to return PAYE/NICs. We understand the gist of Mr Sherry's submission here is to say that the *payer* of the sub-trust allocations to the directors was different from Delphi as the *taxpayer* of the PAYE/NICs liabilities, and the specificity proof required for the 'but for' kind

of causation is not made out. We have concluded that the kind of causal link required for tort liability is the wrong model to construe 'due to' in para 3(1) Sch 24. In any event, the factual basis of this argument is unclear to us, given that the PLR has been determined by the settlement agreement which also fixed the identity of 'P' as Delphi for Sch 24 purposes, regardless of the role played by the trustees in the Scheme.

250. For the reasons that we reject the appellant's submissions that 'due to' for Sch 24 purposes is to be construed as connotating the kind of causation as propounded by *Bayliss* for s 95 TMA penalty regime, and the impossibility to make the required finding of fact as invited by the appellant to make its case on causation, we dismiss this ground of appeal in its entirety.

Issue 4: Was the inaccuracy 'deliberate' in respect of tranche 4?

The basis for assessing tranche 4 as 'deliberate'

251. Ms Choudhury's submission is that the particular facts in relation to tranche 4 suggest that the allegation of deliberate conduct is justified because:

(1) The Clavis Scheme was founded on the basis that Herald would undertake an independent review of the appellant. HMRC accept that Herald carried out a review for the first 3 tranches (even when the report produced for tranche 3 was identical to tranche 2, save for the amount).

(2) There is insufficient evidence that an independent review took place for tranche 4:

(a) Cowen of Clavis and Herald prepared a draft report dated 27 October 2009 following his attendance at Delphi's premises on the same date, which recommended rewards of £1m for each of the directors.

(b) On 30 October 2009, the appellant sent Cowen a copy of its accounts for the year ended 30 June 2009.

(c) On 31 October 2009, Langran emailed Cowen to say he had just spoken to Tucker who thought they should 'do' £5.4 million and to check if that was ok.

(d) Cowen's response was not provided but a further draft report was prepared which used the £5.4m figure referred to in Langran's email, as did the final report.

(e) The report was being prepared in October so the profits for the year ended 30 June 2009 would have been known.

(f) The appellant entered into 'the circular loan back arrangement in order to increase the tax savings'.

(3) Tucker initially stated that he did not consider the evaluation had changed as a result of the accounts being sent to Cowen but changed his answer on being re-examined.

(4) HMRC submit that the accounts were for the period 30 June 2009 and there is no suggestion that the figures had changed in the period between Mr Cowen attending the appellant's premises on 27 October and the date the draft accounts were sent to him.

(5) HMRC submit that the appellant, through Langran, gave a direction to Herald as to the amount it wanted to be put through the Scheme. The directors would have been aware that no review was carried out in respect of tranche 4, and the only review carried out had resulted in a different figure of £1m for each director as the proposed remuneration, as seen in the draft report prepared before Langran's email of 31 October 2009.

(6) Further, or in the alternative, Herald did not give the appellant's directors any genuine advice about the level of remuneration to be given to them: it merely recommended a sum equal to the figure Delphi had provided to Herald of £5.4 m.

(7) If the review was independent, the appellant should not have needed to tell Herald the sums in which it wanted the directors to be rewarded. The directors would therefore have been aware that Herald did not carry out a genuine remuneration exercise as to what was required to reward and incentivise them.

252. Based on the foregoing, Ms Choudhury submitted that the inaccuracy in relation to tranche 4 was caused by deliberate behaviour since (a) the appellant's directors 'must have known that the report provided a predetermined outcome'; (b) that 'its only purpose was to provide a smokescreen for the benefit of HMRC'; and (c) the 'veneer' of the independent review was not in place. The directors therefore could not claim that they did not know that the sums in question would be returned to them; they therefore knowingly took actions that resulted in the P35 return for 2009-10 being incorrect in terms of both *Auxilium* and *Clynes*.

The appellant's submissions on tranche 4

253. Mr Sherry's submissions focus on HMRC not discharging the burden of proof in respect of 'deliberate' behaviour for tranche 4, in that:

(1) HMRC rely on 'insufficient evidence' that an independent review had been carried out by Herald to prove their case. 'An insufficiency of evidence cannot assist in proving HMRC's serious allegation of deliberate conduct'.

(2) Whilst Mr Cowen's response to Langran's email of 31 October 2009 was noted by HMRC as not being provided, HMRC are prepared to invite the Tribunal to make the 'same assumption' that Cowen 'blindly and mindlessly complied with [Langran's] presumed request'.

(3) A decision to follow the suggestion or wishes of the appellant as to the amounts to be contributed to individuals does not automatically mean that Herald did not carry out an independent review, or was not acting independently of the appellant, or not providing the services agreed under the Outsourcing Agreement: *Portview* at [35(4)(i)-(vii)].

(4) Even if Herald were encouraged or persuaded by the appellant's wishes, 'in the absence of any evidence of collusion or sham, Herald had complete freedom to produce/amend its report as it saw fit' as per the terms of the parties' agreement and in accordance with Thornhill's Opinion.

(5) At the time of tranche 4, the most recent extant decision of the courts on the relevance of the circularity of funding and whether it alerted the analysis of expenditure and receipts was the Court of Appeal's decision given in October 2008 in *Tower Cashback v HMRC*. (The decision was reversed on this point – after tranche 4 had been implemented – by the Supreme Court on 11 May 2011.) But the circularity argument does not turn the loans from the trust into earnings if they were otherwise not thought to be so in the light of the extant authorities of *Dextra* (at first instance) and *Sempra*.

(6) The argument is 'fatally flawed' in light of Barraclough's acceptance that the appellant did not legally control Herald, Clavis or the Trustees who operated the trusts. A change in the draft report does not mean that the appellant or its directors *knew* of or could in any way control Herald's actions or omissions.

(7) These allegations do not explain how the alleged lack of an independent review caused an inaccuracy in the P35 return for 2009-10. It is submitted that even if there was no independent review, this would have only affected the CT position: the PAYE/NIC deductibility would have remained the same at the time the P35 was submitted per the applicable case law.

254. In summary, Mr Sherry submits that HMRC have failed to establish that 'by providing financial information or instructing Herald (post-interviews) as to the amount of contributions (or the profits available for contributions)' –

(1) The appellant knew or was reckless that by so doing, it would prevent the CT exemption (i.e. 'anything given as consideration for services provided in the course of a trade') from applying to tranche 4, or that

(2) The appellant knew or was reckless that in doing so, it would alter the PAYE position later.

Case law on 'deliberate' action

255. In considering whether the inaccuracy in respect of tranche 4 was 'deliberate', we find what Judge Morgan said in *Clynes*[28] to be particularly relevant, where she took as the starting point the dictionary definition of the term 'deliberate' (as regards action) being: '*Well weighed or considered; carefully thought out; formed, carried out, etc. with careful consideration and full intention; done of set purpose; studied; not hasty or rash*'(at [81]). Applying the dictionary meaning to 'deliberate' in the context of Schedule 24 penalty regime, Judge Morgan said:

> [82] … for there to be a deliberate inaccuracy on a person's part, the person must to some extent have acted consciously, with full intention or set purpose or in a considered way',

256. We also have regard to the timing and the manner of tranche 4 being implemented as having direct bearing on the evaluation whether the inaccuracy can be categorised as 'deliberate' in the light of *Clynes*:

> '[86] … depending on the precise circumstances, an inaccuracy may also be held to be deliberate where it is found that the person consciously or intentionally chose not to find out the correct position, in particular, where the circumstances are such that the person knew that he should do so….'

257. In *Auxilium*[29] the Tribunal (Judge Greenbank and Michael Bell) interpreted 'deliberate inaccuracy' for Sch 24 purposes in terms as follows:

> '[63] In our view, a deliberate inaccuracy occurs when a taxpayer knowingly provides HMRC with a document that contains an error with the intention that HMRC should rely upon it as an accurate document. This is a subjective test. The question is not whether a reasonable taxpayer might have made the same error or even whether this taxpayer failed to take all reasonable steps to ensure that the return was accurate. It is a question of the knowledge and intention of the particular taxpayer at the time.'

Findings of fact regarding tranche 4

258. With the case law definition for deliberate action in mind, we have regard to the sequence of events and the evidence of Tucker and Langran in relation to tranche 4.

(1) The enquiry into the CT return for the accounting period ended 30 June 2008 was opened on 15 September 2009, and was a fact firmly in the background at the time when the appellant embarked on implementing tranche 4.

(2) In fact, the conjunction of events meant that Clavis Solutions (as 'tax advisers to Herald Resource) was responding to Officer Walker's request in connection with the enquiry into Delphi by way of Sally Fuller's telephone call to Walker, while at the same time preparing for tranche 4 to be implemented – Fuller's call to Walker on 21 October

[28] *Anthony Clynes v HMRC* [2016] UKFTT 369 (TC)
[29] *Auxilium Project Management Ltd v HMRC* [2016] UKFTT 249 (TC) =.

2009 was followed the next day by her email instruction for the sign up pack for SPT4 to be produced.

(3) Dickisnons as Delphi's advisers, would appear to have been updated by Fuller, as inferred from the opening paragraphs in their letter of 21 October 2009, and Dickinsons by making direct reference to Officer Jones of SI Liverpool co-ordinating the enquiries into other users of the Clavis Arrangement, was fully aware of the scale of investigation.

(4) Around the time of tranche 4 being discussed, HMRC's Spotlight 5 would have been in circulation since 5 August 2005, and its archived date was 2 November 2009.

(5) Cowen of Herald/Clavis supposedly had prepared an evaluation report dated 27 October 2009 following his attendance at Delphi's premises on the same date, which recommended rewards of £1m for each of the directors. However, Sally Fuller's email of 22 October 2009 (which pre-dated Cowen's visit of 27 October 2009) was to instruct her colleagues to produce 'new sign up pack for SPT4' where she clearly stated to her colleagues: '*They're doing £3m and will relate to their year ended 30 June 2009*'.

(6) The reasonable inference, from Sally Fuller's instruction email of 22 October 2009, that the figure of £3m was already determined ***before*** Cowen's visit of 27 October 2009 purportedly to carry out an independent review.

(7) Furthermore, the figure per Sally Fuller's email of 22 October 2009 would appear to be referable to Delphi's cash position at the time of tranche 4, being £3m (or £2.7m), according to Langran's evidence.

(8) When Sally Fuller told her colleague '*They're doing £3m*' (before Cowen's visit), the most probable inference of the identity of 'they' would be '*the directors of Delphi*'.

(9) Tucker's evidence was that the tranche 4 payment was made post-year-end, and included in the final set of accounts by way of an accrual.

(10) The reasonable inference is that the management accounts provided to Cowen by email on 30 October 2009 would not have included the £5.4m.

(11) Between the management accounts on 30 October 2009 and the set of accounts filed on 9 June 2010, an accrual of £5.4m augmented the figure for Directors' emoluments to £11m, (inclusive of the £5.4m invoice paid to Herald), which represents 86% of the 'Administrative expense' total of £12.78m for period ended 30 June 2009.

(12) Tucker's evidence originally stated that the management accounts would not have changed Herald's recommendation, then changed to state that Herald would not have changed the figure without supporting documents, such as the management accounts.

(13) Langran's evidence concurred with Tucker's amended evidence, in that the change of recommendation in Herald's report from £3m to £5.4m was due to the set of accounts sent on 30 October 2009.

(14) Langran's statement in cross-examination was that the email of 31 October 2009 was 'to instruct' Cowen of the 'available profits' from accounting period ended 30 June 2009 because Cowen had 'no idea about [the company's profits]'.

(15) Between the email of 31 October 2009 and Herald Employment (Cheshire) informing Herald Resource (Jersey) on 16 November 2009 of the increased amount of remuneration budget, the reasonable inference is that the loan-back arrangements had been agreed to take place for the recommended sum to change from £3m to £5.4m.

(16) Langran's email to Cowen of 23 November 2009 was to signal to Cowen to arrange for the first instalment payment of tranche 4 to be loaned back to the directors to meet the second instalment payment of the tranche 4 invoice.

259. We make the following findings of fact for determining the behaviour for tranche 4.

(1) We find that the original recommendation of £3m was by reference to Delphi's cash position at the time, and the figure of £3m was in correspondence to instruct Herald/Clavis for the purpose of producing the 'sign up pack for SPT4' as related in Sally Fuller's email instruction to her colleagues of 22 October 2009.

(2) We find that the figure of £3m had emanated from the directors of Delphi and was determined *before* Cowen's supposed review carried out on 27 October 2009.

(3) Herald revised the recommended figure to £5.4m on being 'instructed' by Delphi (via Langran's email of 31 October 2009) of its 'available profit'.

(4) We accept Langran's evidence that Cowen had 'no idea' of Delphi's 'available profits' without being so instructed.

(5) Langran, in turn, was advised by Tucker, who would have known from the draft set of accounts that Delphi's taxable profits stood at around £6.5m without any EBT payment invoice.

(6) The circular loan back arrangements were devised to get round the net funds position at year end 2009, standing at just over £2m (cash plus investments), which was very far short of the £5.4m required to reduce operating profit to £1m.

(7) The original recommendation of £3m referable to Delphi's cash position would have taken into account of what Langran referred to as cash inflow after June 2009.

(8) Without the loan back arrangements, Delphi would only have the cash to make £2.7m (or £3m) and would have to pay Corporation Tax on circa £3.5m instead of £1m.

(9) We find that Langran's evidence (a) that '[t]he suggestion never came from Mr Cowen "we should do £5.4 million", because 'Cowen had no idea about that', and (b) 'We had to instruct him' – to be a truthful representation of what actually happened. To that extent, we find that the final EBT payment £5.4m was attributable to a deliberate action of the appellant.

(10) We also find that the contrivance of the loan-back arrangements of the first instalment of £2.7m for the sole purpose of providing funds for the appellant to pay the second instalment of tranche 4, in order to double the overall CT deduction to £5.4m to be a deliberate action.

Conclusion on tranche 4

260. We find that the inaccuracy in relation to tranche 4 was attributable to deliberate action. We have regard to the fact that the test for 'deliberate' inaccuracy is a subjective one, and that we are concerned here with the knowledge and intention of the appellant specifically.

261. We find that the original sum of £3m for the purpose of producing the sign up pack to be an instruction emanating from the directors of Delphi and given to Herald/Clavis by 22 October 2009, at least about a week *before* the remuneration evaluation meeting of 27 October 2009. We conclude that the remuneration evaluation meeting was to give the 'veneer' of an independent review having been carried out, when the figures of remuneration budget were by instruction of Delphi's directors all along, whether it was the original £3m or the revised £5.4m.

262. Depending on the precise circumstances, an inaccuracy may also be held to be deliberate where it is found that the person consciously or intentionally chose not to find out the correct position, in particular, where the circumstances are such that the person knew that he should do so. We have special regard to the fact that Dickinsons, as advisers to Delphi, was in correspondence with HMRC in late October while at the same time, advising Delphi of the sum of £5.4m to enhance the CT deduction for the year to 30 June 2009.

263. We also have regard to the CT return enquiry into the appellant for the year 30 June 2008 having been opened in September 2009, and Spotlight 5 having been in the background at the time of tranche 4 being implemented. With the ongoing enquiry into Delphi, and the large-scale enquiry into other Clavis Scheme users that Delphi (via Dickinsons as its adviser) would have been aware of, the appellant had not taken any steps at that juncture to re-evaluate the Scheme prior to embarking on tranche 4.

264. To the extent that the Scheme purported to obtain a CT deduction through the provision of service in the form of an independent review of Delphi to make the remuneration recommendation so as to qualify for the disapplication of s 1290 CTA 2009 under sub-s (4)(a), we are satisfied that HMRC have met the burden in establishing that on the balance of probabilities, Herald did not carry out an independent review for the exemption to apply in relation to the final figure for tranche 4, and that the appellant knowingly instructed Herald to amend the recommended amount to £5.4m with the intention that it could double the CT deduction for the year 2009 in order to reduce its corporation tax liability.

265. We conclude that the inaccuracy in the P35 return for the tax year 2009-10 in relation to tranche 4 was due to the deliberate action on the part of the appellant for the deliberate penalty to be imposable.

DISPOSITION

266. The appeal is determined as being brought under para 15(1) of Schedule 24 against the penalties being payable by the appellant. No appeal is being brought under para 15(2) of Schedule 24 as to contend the quantum of the penalties.

267. Paragraph 17 of Schedule 24 provides that the Tribunal may affirm or cancel HMRC's decision on an appeal under para 15(1).

268. For the reasons set out in this Decision, the Tribunal affirms HMRC's decision to impose the penalties of £525,484.99 for the year 2008-09, and £1,046,775.17 for the year 2009-10.

269. The appeal is accordingly dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

270. 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 HEIDI POON
TRIBUNAL JUDGE

Release Date: 18 August 2023