



Case number: FTC/72/2013

Income Tax- ITTOIA 2005- effect of partial surrenders of insurance policies by individual- did claimant make a mistake for which rectification is available? Yes. Should s. 539 of ITTOIA or s. 50 of TMA 1970 be read so as to remove restrictions on deficiency relief or to reduce the tax payable? No. Can the FTT entertain the public law issues? No.

UPPER TRIBUNAL

TAX AND CHANCERY CHAMBER

BETWEEN:

JOOST LOBLER

Appellant

and

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

Respondents

TRIBUNAL: MRS JUSTICE PROUDMAN DBE

**Sitting in public at The Rolls Building, Fetter Lane, London EC4A 1NL on 19, 20 and 21
January 2015**

Michael Firth, instructed by Smith Pearman, Chartered Accountants, for the appellant

**Jonathan Davey, instructed by the Solicitor and General Counsel to HM Revenue and
Customs, for the respondents**

**Hui Ling McCarthy (who made written submissions pursuant to the direction of Judge
Greg Sinfield of 13 November 2014 under r.5 (3)(d) of the Upper Tribunal Rules 2008
(as amended) and who made oral submissions pursuant to the direction dated 19
January 2015 of Mrs Justice Proudman), for the Chartered Institute of Taxation**

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DECISION

1. This is an appeal by the taxpayer Joost Lobler from the decision of Judge Charles Hellier and Kamal Hossain FCA FCIB sitting in the First-tier Tribunal of the Tax Chamber (“the FTT”). The FTT decided that it was unable to interfere with the amendment made by HMRC to the Appellant’s tax return under legislation (Chapter 9 Part 4 of the Income Tax (Trading and Other Income) Act 2005 (“ITTOIA”)) which treats prescribed sums arising in relation to policies of life assurance as being liable to income tax.

2. The FTT dismissed the appeal with “heavy hearts” [28], and observed in [1], [3] and [4] that:

“In this appeal a remarkably unfair result arises as a result of a combination of prescriptive legislation and Mr Lobler’s ill-advised actions...

He made no profit or gain as that term is commonly or commercially understood and yet he becomes liable to pay tax which exhausts his life savings and may bankrupt him. That is an outrageously unfair result.

...The appeal takes place at a time when there is great media and political comment about a fair tax system. That interest focuses on the avoidance of tax by those who have substantial income, but to our minds it is more repugnant to common fairness to extract tax in Mr Lobler’s circumstances than to permit other taxpayers to avoid tax on undoubted income.”

3. The legislation has also attracted serious judicial criticism in four other cases in the FTT.

4. In this appeal Mr Firth appears for Mr Lobler and Mr Davey for the Commissioners for Her Majesty’s Revenue and Customs (“HMRC”). Pursuant to a direction of Judge Sinfield in the Upper Tribunal (“the UT”) under r.5(3)(d) of the Upper Tribunal Rules 2008 (as amended) (“the Rules”) the Chartered Institute Of Taxation (“the CIOT”) was permitted to make written submissions.

5. Observing on the first day of the hearing that the CIOT was present in the person of (possibly among others) Ms McCarthy, its Counsel who had made those written submissions, and believing that I should have the benefit of hearing her submissions in detail and that both parties should have the opportunity to respond to them fully, I gave a direction that she be permitted also to address this Tribunal orally. The CIOT’s interest is that further appeals, claims for judicial review and other disputes with HMRC, where taxpayers face similar consequences to those affecting Mr Lobler, have been stayed pending the outcome of this appeal. In its application under r.5 (3)(d) of the Rules the CIOT gave details of some of those other cases. The CIOT is in the process of gathering information from other

interested parties and professional bodies in order to make a formal submission to HMRC and the Treasury with a view to obtaining a change in the law.

6. Both Judge Sinfield and I made (unopposed) orders under r.10 (4) of the Rules that each party to the appeal on the one hand and the CIOT on the other
5 should bear their own costs in relation to the application and their respective submissions, written and oral.

Background

7. ITTOIA deems a person making a partial surrender of each insurance policy
10 which he holds as having realised taxable income in the relevant years, notwithstanding that he may have made no actual profit or gain on the policy.

8. The facts of Mr Lobler's case are set out in detail in [6]-[13] of the decision and the legislation is set out at [14]-[17].

9. In brief, Mr Lobler is a Dutch national. In early 2004 he came to England for
15 work purposes with his wife and two young children. In 2005 he sold the family home in the Netherlands for the rough equivalent of £350,000. This sum represented Mr Lobler's entire life savings and he decided to invest all of it in life insurance policies with Zurich Life ("Zurich"), an insurance company in the Isle of Man.

10. He then took out an interest-bearing loan from HSBC of another \$700,000
20 and invested this sum in further life insurance policies with Zurich. Mr Lobler's total investment with Zurich amounted to approximately \$1,406,000 invested on 1 March 2006 in 100 life insurance policies. It does not appear that tax avoidance was a purpose influencing the choice of financial product in which Mr Lobler
25 invested.

11. In 2006 Mr Lobler bought a house in England for use as his family home. On
30 28 February 2007 he withdrew \$746,485 from the policy to repay the HSBC loan of \$700,000 including the accrued interest. On 29 February 2008 he withdrew a further \$690,171 which he used to pay for the house and various renovation works. In short, he withdrew from the policies by way of partial surrender of each policy a total of 97.5% of the amount he had originally put in.

12. The effect of the legislation is as follows. When Mr Lobler made partial
35 surrenders, the value surrendered for the purposes of s. 507 ITTOIA was the amount received. For each year the s. 507 calculation produced a deemed gain equal to the amount received less 5% of the premium originally paid. A chargeable event arose and because there was a chargeable event there was for the purposes of s. 462 "a gain from a policy", and by s. 463 tax was to be charged on "the amount of the gains arising in the tax year".

13. Thus ITTOIA treats Mr Lobler as having realised taxable income of some \$1.3m and he is liable to pay some \$560,000 in tax, which exhausts his life savings and may bankrupt him, although he made no substantial profit or gain. Mr Lobler now recognises the prescriptive effect of the legislation which, as a matter of interpretation of the words used, he accepts.

14. In *Mayes v HMRC* [2011] STC 1269 I pointed out that the rules (the precursor of those in ITTOIA but the same for present purposes) showed a lack of interest in (a) attributing gains to the person who made them, (b) not attributing them to a person who did not make them or (c) timing the taxation of the gain fairly. I said at [44] and [47],

“This is legislation which does not seek to tax real or commercial gains. Thus it makes no sense to say that the legislation must be construed to apply to transactions by reference to their commercial substance...

Chapter II of the Taxes Act adopts a formulaic and prescriptive approach. No overriding principle can be extracted from the legislation, or from the authorities, that some types of transaction should be ignored in the application of the Chapter.”

The Court of Appeal (and I) accepted the taxpayer’s analysis, in relation to a blatant tax avoidance scheme, from the viewpoint of the purposive construction of the relevant provisions. HMRC’s new GAAR [General Anti-Abuse Rules] Guidance (effective 15 April 2013) provides (at [D15.4.2]):

“Although the courts [in *Mayes*] saw that actual overall gains should be taxed eventually if there was a UK taxpayer bondholder throughout, and identified a legislative policy of discouraging early partial surrenders in excess of the allowable amounts, they also identified arbitrary or unfair results in a variety of circumstances... Since the legislation did not seek to tax real or commercial gains the view was taken that it made no sense to say that the legislation should be construed to apply to transactions by reference to commercial substance, and an underlying or overriding purpose could not be extracted that would lead to parts of the scheme being ignored.”

15. In July 2008 Mr Lobler terminated the policies and received some US\$35,000. By the time of the termination of the policies an excess of only some US\$65,656 was generated over that which was invested some two years previously. On the surrender of all rights under a policy, s. 484(1)(a)(i) provides for a chargeable event.

16. S. 539 of ITTOIA provides for “relief for deficiencies” to be (pursuant to s. 541 and s. 491), “the total previous gains”, less the excess (if any) by which, “the total benefit value” exceeds the “total allowable deductions”. Those phrases are defined but suffice it to say that Mr Lobler had a deficiency of some US\$1,230,000 which could be set against other taxable income in that tax year.

He could not carry the deficiency forward or back and he did not have any other income anywhere near that figure so that the deficiency relief was of no use to him.

5 17. In making his partial surrenders, Mr Lobler filled out Zurich forms without the benefit of any legal or other advice. I understand the form with which I have been supplied to relate to the first surrender, although the figures are confusing. I am told that Mr Lobler withdrew \$746,485 in February 2007 but the form (dated 29 November 2006) refers to a withdrawal of \$700,000. At all events the form provided four options, A, B, C, or D, and he made the same choice on both
10 occasions.

15 18. A was a full surrender, B was a partial surrender across all policies and funds, C, the box checked by Mr Lobler, was a partial surrender to raise US\$700,000 across all policies from specific funds (which on the form I have Mr Lobler named as follows: HSBC Chinese Equity fund, 100% of Fund value, Merrill Lynch IFF Latin American Fund, 100% of Fund value and HSBC Indian Equity Fund, “remainder to US\$700,000”) and D was full surrender of individual policies, naming the amount required from surrender of individual policies or specifying the number of individual policies to be surrendered. Mr Lobler did not tick the box for Option A as he did not aim to withdraw all of his funds at the
20 same time. There was nothing to choose between C and D for Mr Lobler, save that if he had opted for D, the tax charge would have been significantly lower.

25 19. Mr Lobler received the funds in the requested amounts. He did not refer to these amounts on his self-assessment tax returns in 2007 and 2008, assuming that no gain arose on the withdrawals since they were withdrawals of capital. He did not think of this again until he received a letter from Zurich informing him of a chargeable event gain of \$676,184 in relation to the 2007 withdrawal and of \$619,871 in relation to the 2008 withdrawal. Zurich also informed HMRC, as it was obliged to do.

30 20. HMRC opened enquiries in relation to Mr Lobler’s 2007 and 2008 tax returns and decided to amend Mr Lobler’s self-assessments to reflect the tax liability incurred by making the two withdrawals. Under the legislation Mr Lobler incurred a deemed gain of roughly \$1.3m and was assessed to tax accordingly. This represents an effective tax rate of 779 per cent on actual income generated by the policy.

35 21. This large tax liability is the direct result of Mr Lobler selecting Option C on the claim form provided by Zurich rather than a different option under which the deemed chargeable gain and therefore the tax charge on Mr Lobler would have been significantly lower.

40 22. On discovering the effect of Mr Lobler’s selection, Zurich offered by letter to HMRC dated 27 June 2011 to recalculate the Chargeable Event Certificates, “based on what would be the more appropriate method of making withdrawals from the investment.” However, the offer was subject to HMRC’s consent.

HMRC maintained that the tax charge on Mr Lobler was rightfully incurred and on 12 July 2011 rejected Zurich's offer to recalculate.

23. Mr Firth submits that the tax rate payable is arbitrary, since if Mr Lobler had withdrawn 100% of his policies he would have paid tax on his deemed taxable income at 40%, whereas the effect of his withdrawing 97.5% was that he was taxed at some 779%.

Preliminary

24. Two preliminary matters arise. First, it is said by HMRC that the FTT did not find as a fact that Mr Lobler made a mistake in making the partial surrender in the way he did. This is on the basis that at [13] the FTT said (my emphasis),

“Mr Lobler says that he made a mistake in the way in which he withdrew funds from the policies. He did not realise that the effect of making a partial surrender was that almost all the amount he withdrew would be treated as taxable income.”

25. I agree with Mr Davey that the second sentence of this paragraph follows from the first and is not (*pace* Mr Firth) an independent finding. In other words, it is again what Mr Lobler says.

26. However, it is in my view plain almost beyond argument that there was a finding that Mr Lobler made the postulated mistake, for four reasons. First, because of the previous finding in [11] which is not hedged about with any such words as are found in [13],

“Mr Lobler assumed that because he had withdrawn no more than he had paid for the policies no taxable gain would arise.”

It follows therefore that there was a finding that he must have made a mistake in the way in which he withdrew funds from the policies.

27. Secondly, because the decision states in round terms the unfairness of the legislation to Mr Lobler, which it would not have done if he had not made a mistake. The FTT considered (at [24]) that the legislation placed such an excessive burden on Mr Lobler that it may have crossed the line between taxation and (I assume) confiscation of property by the state. Thirdly, because the decision dealt with rectification at [22] and [23] in a manner showing that he made a mistake in which Zurich was not concerned.

28. Fourthly, it does not appear that Mr Lobler's evidence was challenged in this regard, so that it was necessary for the FTT to accept it.

29. The second preliminary matter is the issue of carelessness. Mr Davey pointed out that in [1] of the decision the FTT described Mr Lobler's actions as "ill-advised",

5 "In this appeal a remarkably unfair result arises as a result of a combination of prescriptive legislation and Mr Lobler's ill-advised actions."

30. Thus, he argued, Mr Lobler was careless, not taking advice as he should have done as to the tax consequences of his choice. That was, he said, the meaning of "ill-advised". However since Mr Lobler did not take any advice at all the FTT plainly used "ill-advised" in the sense of not sensible, prudent or wise, meaning simply wrong. The FTT's overall assessment of the outcome of the appeal was that it was unjust, which again leads me to the conclusion that the FTT did find that Mr Lobler had made a mistake which was misguided (in the sense of wrong) rather than careless.

15 31. In any event carelessness is relevant to the exercise of the court's discretion, that is to say, certain remedies, but not generally to the analysis of mistake, let alone the issue of human rights: see *Daventry District Council v Daventry & District Housing Limited* [2011] EWCA Civ 1153 at [83]. I note that in *Kelly v. Solari* 9 M&W 54, cited in *Norwich Union Fire Insurance Society v. Wm H Price Limited* [1934] AC 455 at 462, Baron Parke stated the law in the context of money paid under a mistake of fact, as follows,

25 "If it (the money) is paid under the impression of the truth of a fact which is untrue, it may, generally speaking, be recovered back, however careless the party paying may have been in omitting to use due diligence to inquire into the fact... The "fact" which Baron Parke is referring to is one "which would entitle the other to the money" if true. The reference to intention is crucial."

32. Again, in *Pitt v. Holt* at [114], Lord Walker said (describing it as an "uncontroversial point" and referring to *Deutsche Morgan Grenfell Group plc v. IRC* [2007] AC 558 at [24]-[30]),

35 "It does not matter if the mistake is due to carelessness on the part of the person making the voluntary disposition, unless the circumstances are such as to show that he deliberately ran the risk, or must be taken to have run the risk, of being wrong."

Three grounds of appeal

33. Mr Firth contends that Mr Lobler is entitled to the exercise of various remedies and that the FTT erred in not applying them.

34. There were three principal grounds of appeal:

- (i) *Private law grounds*
 - (a) The doctrine of mistake at common law,
 - (b) The doctrine of mistake in equity,
 - (c) The remedy of rectification,
 - 5 (d) Human Rights and private law.
- (ii) *Human Rights grounds in private law*
 - (a) Breach of Article 1 Protocol 1 ECHR,
 - (b) Breach of Article 14 ECHR.
- (iii) *Public Law grounds*
 - 10 (a) Jurisdiction of the FTT,
 - (b) Alleged *ultra vires* acts by HMRC.

Mistake at common law and in equity

15 35. At common law, mistake operates to nullify consent so that the contract can be rescinded: see *Bell v. Lever Brothers* [1932] AC 161 at 217. However the mistake has to be (see *per* Lord Wright in *Norwich Union Fire Insurance Society Limited v. Price* [1934] AC 455 at 463),

20 “of such a nature that it can properly be described as a mistake in respect of the underlying assumption of the contract or transaction or as being fundamental or basic.”

36. Lord Thankerton (who was in the minority, but not as to what the law was) in *Bell v Lever Brothers* at p.208 said as follows:

25 “The real question, therefore, is whether the erroneous assumption on the part of both parties to the agreements...was of such a fundamental character as to constitute an underlying assumption without which the parties would not have made the contract they in fact made, or whether it was only a common error as to a material element, but one not going to the root of the matter and not affecting the substance of the consideration.”

30 37. Equity however intervenes in a mistake on the basis of unconscionability and injustice.

38. Mr Davey submitted, first, that all the cases of common law mistake related to the formation of a contract so that there was no agreement necessary for a

binding contract. He referred to the examination of the authorities about mistake and frustration in *Great Peace Shipping Limited v. Tsavlis (International) Limited* [2002] EWCA Civ 1407 in which Lord Phillips MR, giving the judgment of the Supreme Court, said at [73],

5 “The avoidance of a contract on the ground of common mistake results from a rule of law under which, if it transpires that one or both of the parties have agreed to do something which it is impossible to perform, no obligation arises out of that agreement.”

10 39. Again, at [76] of *Great Peace* the elements of the doctrine are laid out as follows,

15 “...the following elements must be present if common mistake is to avoid a contract: (i) there must be a common assumption as to the existence of a state of affairs; (ii) there must be no warranty by either party that that state of affairs exists; (iii) the non-existence of the state of affairs must not be attributable to the fault of either party; (iv) the non-existence of the state of affairs must render performance of the contract impossible; (v) the state of affairs may be the existence, or a vital attribute, of the consideration to be provided or circumstances which must subsist if performance of the contractual adventure is to be possible.”

20 40. Further, in *Great Peace* the Court of Appeal disapproved *Solle v. Butcher* [1950] 1 KB 671, holding that relief cannot be given for common mistake in circumstances wider than that stipulated for in *Bell v. Lever Brothers*. There is no equitable jurisdiction to grant rescission of a contract on the ground of common mistake where that contract is valid and enforceable on ordinary principles of contract law.

30 41. There are basically two types of mistake (ignoring for this purpose unilateral mistake as to the terms of the contract of which the other party was or ought to have been aware), (a) where the parties agree on the terms of the contract but have entered into it under a shared fundamental misapprehension and (b) where there is some mistake between the parties which means that there is no agreement at all on the terms apparently stated.

35 42. Both these concepts relate to a bilateral contract. The remedy sought with common law mistake is that the contract is void. However, I do not agree with Mr Davey that this is necessarily the case with the result that rescinding or rectifying just one part of a transaction is not possible: see the decision of Scott J in *Re Cleveland plc* [1991] BLC 424 and Lord Wright’s statement referring to “contract or transaction” above. It seems to me that the doctrine of mistake is not limited to the formation of the contract and a withdrawal from a life insurance policy can in principle give rise to it.

43. Secondly, Mr Davey submits that the mistake could not be sufficiently fundamental or serious because the subject-matter of the mistake was not essentially different from that which was expected. He used the example of quantum, asking rhetorically at what point was the tax rate so high that the mistake became fundamental? When did a partial surrender mistake become sufficiently serious? When 6% was surrendered, or 60%? However Mr Firth relied on *HMRC v. Procter & Gamble UK* [2009] EWCA Civ 407; [2009] STC. 1990 (at [30]-[33]) for the proposition with which I respectfully agree that, as Jacob LJ said at [32],

10 “you do not have to know where the precise line is to decide whether something is one side or the other”.

44. Avoidance or rescission of the withdrawal transaction is not to my mind the right solution because the party receiving the benefit of the mistake is not Zurich but a third party to the policy contract, HMRC. Mr Lobler did intend to surrender his policies, Zurich intended to provide him with a payment calculated in accordance with his contract and he did indeed receive it.

Rectification

45. Rectification for mistake is a different matter. The remedy has its own rules. With a bilateral contract, those rules (as summarised by Peter Gibson LJ in *Swainland Builders Limited v. Freehold Properties Limited* [2001] 2 EGLR 71 at [33]) are: (i) that the parties had a common continuing intention, whether or not amounting in law to an agreement, in respect of the particular matter in the instrument to be rectified; (ii) there was an outward expression of accord; (iii) the intention continued at the time of execution of the instrument sought to be rectified; and (iv) by mistake, the instrument did not reflect that common intention.

46. The FTT, doubtless trying to help Mr Lobler, itself I believe raised the question in [22]-[23] of whether rectification might be available,

30 “If a court would order rectification of the forms on which Mr Lobler made his application for funds so that they would take effect as the full surrender of some of the subsidiary policies, then relying on the maxim that equity treats what should have been done as done, we might treat the applications as total surrenders.”

47. Thus although the FTT did not itself have power to order rectification, it could determine that if rectification would be granted by a court who does have jurisdiction to grant it, Mr Lobler’s tax position would follow as if such rectification had been granted.

48. It has never been suggested that before the effect of the availability of specific performance can be taken into account by the FTT, the appellant must go to court

and actually obtain the remedy of specific performance. On the contrary, the cases show that this is not the case: see *Oughtred v. IRC* [1960] AC 206, *Jerome v. Kelly* [2004] UKHL 25, *BMBF (No 24) Limited v. IRC* [2002] STC 1450 and *HSP Financial Planning Limited v. HMRC* [2011] UKFTT 106 (TC). A tribunal
5 such as the FTT must however take into account all the factors that the Court would in deciding whether specific performance would be available, such as whether damages would be inadequate, whether specific performance would require constant supervision, whether the appellant is ready, willing and able to perform, hardship and so on.

10 49. I am told that the cases in this context are all specific performance cases; equity treats a specifically enforceable contract to do a thing as if it were already done: see *Walsh v. Lonsdale* (1882) 21 Ch D 9 at 14, *Oughtred* at 227, *Neville v. Wilson* [1997] Ch 144 at 157.

15 50. One issue is therefore whether the same principle applies to rectification as it does to specific performance, although the FTT made no direct reference to specific performance. Mr Davey said that it does not, but without to my mind giving any convincing or principled reason as to why not. As specific performance is also a discretionary remedy I agree with Mr Firth that there is no relevant distinction between specific performance and rectification for present
20 purposes.

51. In the event, the FTT decided that rectification was not available because (notwithstanding the fact that Zurich was keen - if HMRC consented - to recalculate the tax certificates) there was a lack of common intention (at [23]):

25 “There was nothing before us to suggest that Zurich had any intention at all in relation to the withdrawals sought by Mr Lobler.”

52. On an application to rectify a bilateral contract, classically formation of the contract, there is indeed a requirement of common intention within *Chartbrook Limited v. Persimmon Homes Limited* [2009] AC 1101. In the bilateral case, convincing proof, with the burden on the party seeking rectification, is required to
30 contradict the inherent probability that the written instrument represents the parties’ intention. Where however a transaction is unilateral, unilateral mistake suffices for rectification. It is common sense that the test for unilateral mistake in a voluntary transaction should be if anything even more rigorous.

53. It was fundamental to Mr Firth’s analysis of mistake that the mistake made by
35 Mr Lobler was a unilateral mistake, so that it was the intention of Mr Lobler alone that was in issue, and not, as found by the FTT, a common mistake, involving the intention of Zurich as well as Mr Lobler. Accordingly, says Mr Firth, the FTT was guilty of an error of law and the UT can and should intervene to correct it.

54. Mr Firth submitted that the power in the present case was akin to a trustee
40 power. He relied on *IBM United Kingdom Pensions Trust Limited v. IBM United Kingdom Holdings Limited* [2012] EWHC 2766 (Ch) at [21]-[24]. In that case Warren J was concerned to identify the parties who had to have the objective

common intention (the pension trustees and the employer) so it was not a true unilateral transaction:

5 “...the search in the present case is not for a consensus between IBM
and the Trust Company about what it was that the 1983 Trust Deed
and Rules or any of the later versions of the Trust Deed and Rules
should provide. Rather, the search has a different emphasis: it is to
10 establish two matters: first, what, objectively, the Trust Company, as
the person in which the power of amendment was vested, intended
each of the versions of the Trust Deed and Rules should provide; and
secondly, what, objectively, Holdings [the principal employer]
intended to consent to when executing those Deeds and Rules.”

55. However, Warren J went on to say (at [23]-[24]),

15 “There is thus a significant difference of approach in the contractual
cases and a case such as the present. In the contractual case, it is
necessary to establish a continuing common intention objectively
manifested...

In the case of a power of amendment by a trustee of a pension scheme
and the giving of consent to the amendment by an employer the
position is different...

20 The objective evidence, such as board minutes, will be very important
in establishing precisely what it was that the relevant decision makers
and approvers intended. This evidence may not be evidence of an
expression of intention communicated to any third party since the
minutes or other evidence may remain entirely internal to the trustee
25 or the employer and not be communicated to each other or indeed to
anyone else. But that is not a requirement when it comes to the trustee
seeking to prove that the amending document did not in fact reflect the
intention of the employer or, indeed, its own intention.”

30 56. Mr Firth’s analysis is as follows. Exercising a power under a contract is not a
bargain in any sense of the word, but a unilateral act. Mr Lobler was equally
entitled to execute a full surrender of some or all of his policies as he was partially
to surrender them. The power exercised by Mr Lobler was partially to surrender
the policies, a power dependent only on the intention of the person exercising the
power. In that respect, says Mr Firth, the power is like an option, about which
35 Hoffmann J said in *Spiro v. Glencrown Properties Limited* [1991] Ch 537 at 541,

“But only the grant of the option depends upon consent. The exercise
of the option is a unilateral act. It would destroy the very purpose of
the option if the vendor had to obtain the vendor’s countersignature to
the notice by which it was executed.”

40 57. I asked to see the contract between Mr Lobler and Zurich, as it was not in the
UT appeal bundle. It was eventually produced on the second day of the hearing:

“*International Wealth Account Capital Redemption Plan terms and conditions (UK version)*”. I note from the second page that, “Each contract consists of this Plan, the Application [which I have not seen] and any other submissions made by the Planholder.” The contract is governed by the laws of the Isle of Man. I have
5 assumed in the absence of any evidence to the contrary that this law is the same as that of England and Wales for present purposes.

58. Mr Firth referred me to Clauses 1.8, 1.9 and 6.4 of the contract in support of his contention that Mr Lobler had an absolute right to surrender or cancel his policies. Mr Davey disputes this analysis. He too referred to clause 6.4 but said it
10 had to be read together with Guidance Note 16 on the Claim (withdrawal) Form,

“All policy owners/trustees should sign the form. If this has not been done, we will be unable to accept the instruction and your payment will be delayed. The residence information must also be completed.”

59. However I do not see that this provision is any different from the provisions that would apply to an option.

60. Again, Mr Lobler’s right to withdraw is subject to Zurich’s ability to defer cancellation, namely, where the Fund Manager had deferred cancellation, to the next dealing date or for a month or for six months, depending on the
20 circumstances. However I do not consider that it matters for the purposes of the analysis that in certain circumstances Zurich could defer payment. The issue is whether Mr Lobler had the right without recourse to Zurich to call for his money. He did. The right to deferral follows the right to withdraw and deferral does not affect the nature of the prior right.

61. Indeed the finding by the FTT that Zurich did not have any intention in relation to the relevant matter supports the conclusion that Mr Lobler’s actions were unilateral. Zurich’s intention was simply to accept the instructions and act accordingly. Zurich then transferred Mr Lobler’s funds without having suffered the consequences of any kind of reliance on Mr Lobler’s mistake. In other words,
30 Zurich would have accepted the transaction regardless of which option Mr Lobler chose. It was unaffected by the mistake and it would remain unaffected by rectification of the mistake.

62. It therefore seems to me that Mr Firth is correct in his analogy with the exercise of an option and that it is Mr Lobler’s unilateral intention that falls to be
35 examined, rather than any bilateral intention.

63. However not only is the burden on Mr Lobler to prove that intention but it must be proved that his mistake was a serious one. The unilateral mistake required for rectification of a voluntary disposition should be of similar seriousness to that required for rescission under the test in *Ogilvie v. Littleboy* (1897) 13 TLR 399.
40 Thus the test will normally only be satisfied where there was a mistake as to some matter of fact or law fundamental to the transaction: see the judgment of Lloyd LJ

in the Court of Appeal in *Pitt v. Holt* [2011] EWCA 197, approved by the Supreme Court at [2013] UKSC 26; [2013] 2 AC 108.

64. HMRC say that as Mr Lobler filled in the documentation in the way that he did his intention can only have been to part surrender the Zurich policies.
5 However, in *AMP (UK) Plc v. Barker* (2000) WL 1918516 Lawrence Collins J said (at [70]),

10 “...rectification may be available if the document contains the very wording that it was intended to contain, but it has in law or as a matter of construction an effect or meaning different from that which was intended: *Whiteside v. Whiteside* [1950] Ch 65, 74; *Grand Metropolitan plc v. William Hill Group Limited* [1997] 1 BCLC 390, 394.”

65. In *Pitt v. Holt* the test for mistake was restated as one of seriousness and unconscionability. As Lord Walker said at [126],

15 “The gravity of the mistake must be assessed by a close examination of the facts, whether or not they are tested by cross-examination, including the circumstances of the mistake and its consequences for the person who made the vitiated disposition....

20 The injustice (or unfairness or unconscionableness) of leaving a mistaken disposition uncorrected must be evaluated objectively, but with an intense focus...on the facts of the particular case.”

66. Again, he said at [128],

25 “More generally, the apparent suggestion that the court ought not to form a view about the merits of a claim seems to me to go wide of the mark...

30 ...The court cannot decide the issue of what is unconscionable by an elaborate set of rules. It must consider in the round the existence of a distinct mistake (as compared with total ignorance or disappointed expectations), its degree of centrality to the transaction in question and the seriousness of its consequences, and make an evaluative judgment whether it would be unconscionable, or unjust, to leave the mistake uncorrected. The court may and must form a judgment about the justice of the case.”

35 67. In *Pitt v. Holt* the Supreme Court disapproved the distinction between the effect (in the sense of legal effect, the legal character or nature: see [119]) and the consequences of a transaction, replacing it (see [122]) with the test of causative mistake of sufficient gravity. The Court also considered whether there was a distinction between on the one hand mere causative ignorance and on the other a mistaken conscious belief or a mistaken tacit assumption. Lord Walker said at
40 [108],

“I would hold that mere ignorance, even if causative, is insufficient, but that the court, in carrying out its task of finding the facts, should not shrink from drawing the inference of conscious belief or tacit assumption when there is evidence to support such an inference.”

5 68. It is clear from *Pitt v. Holt* at [129]-[132] that a mistake as to the tax consequences of a transaction may, in an appropriate case, be sufficiently serious to warrant rescission and thus rectification. There is no justification for a different approach to mistakes about tax and other types of mistake.

10 69. There is no doubt that Mr Lobler would not have instructed Zurich in terms of a partial withdrawal had he known about the devastating tax consequences of his choice of withdrawal method. It is common sense that nobody would willingly contract to pay an amount of tax that would effectively lead to his own bankruptcy if there were a choice not to do so and achieve the same goal. It is therefore clear to me that the mistake made by Mr Lobler is of a sufficiently serious nature within
15 the *Pitt v. Holt* test.

70. However the question remains as to whether (as *per* Lloyd LJ in the Court of Appeal in *Pitt v. Holt*) the fundamental or root element of the transaction was affected by the error on Mr Lobler’s part. On one argument the root of the transaction was the withdrawal of the funds and Mr Lobler has indeed been
20 successful in withdrawing the funds, error or not. On another, the withdrawal was so affected by the tax consequences that the effect of the withdrawal was entirely different from that which Mr Lobler believed it to be. It is not in my judgment realistic to say the former was the case, as it is akin to saying that the issue arises out of an unforeseen result of the transaction, rather than the root of it. This
25 brings in by the back door the old distinction, disapproved in *Pitt v. Holt*, between the effect and the consequences of a transaction.

71. As to what Mr Lobler would have done if he had not made a mistake, it seems to me that he would have chosen Option D on the form (although I note that in a letter to HMRC dated 23 February 2011 he says he should have chosen Option B)
30 bearing in mind that he did not intend to withdraw all his funds at the same time so that Option A was inappropriate. Option D seems to me to be obvious. I note that on the 2006 form I have in relation to the first two funds he elected in any event to withdraw “100% of Fund value”.

72. Moreover, I do not shrink (*per* Lord Walker in the passage quoted above from
35 *Pitt v. Holt* at [108]) from drawing the inference of conscious belief or tacit assumption by Mr Lobler that tax would not be payable on the withdrawals.

73. As to the discretionary nature of the remedy, I have decided that the FTT did not find that Mr Lobler was careless when he filled in the form. Even if this is wrong, the level of carelessness in not taking advice when he filled in the form
40 was not to my mind such as would deprive him of the remedy of rectification. Mr Davey pressed on me that Mr Lobler could and should have taken advice as to the best means of withdrawals from the policies; the true analysis of the matter is only that Mr Lobler now wishes that he had not done what he did. I do not agree. One

does not seek advice on everything, the legislation is not at all intuitive and no reasonable man would have expected the outcome.

74. I therefore find that Mr Lobler would be entitled to rectification and that his tax position is to be determined as if that remedy had been granted.

5

Human Rights

75. The CIOT has been calling for a change to what it claims is complex, disproportionate and opaque tax legislation on a partial surrender of life insurance policies. A number of cases directly related to part surrenders under ITTOIA are currently stayed awaiting the outcome of Mr Lobler’s case. Rectification may not be open to all the persons affected and therefore the analysis of Mr Lobler’s human rights is of significant public interest.

76. Consideration of the human rights ground is strictly only necessary if I were to find against Mr Lobler in private law and I have found in his favour on the ground of rectification. However, owing to the interest in this particular aspect of the case I should briefly address the points arising out of the human rights ground in any event.

77. In short, the human rights argument in private law runs as follows. By s. 3 (1) of the Human Rights Act 1998 (“HRA”) primary legislation of whatever kind (see *Ghaidan v. Godin-Mendoza* [2004] UKHL 30, *Sheldrake v. DPP* [2005] 1 AC 264) must be read and given effect to in a manner compatible with human rights, if that is possible.

78. Thus if the application of ITTOIA breached Mr Lobler’s human rights (specifically his right under Article 1 Protocol 1 (“A1P1”) of the European Convention on Human Rights (“ECHR”)), then in line with HRA that part of ITTOIA has to be construed in accordance with the ECHR rights “as far as it is possible to do so”. Although the human right engaged in this dispute is A1P1, Mr Firth has also put forward a case for breach of Article 14 ECHR.

30

Was there a breach of Mr Lobler’s human rights?

79. A1P1 is headed “Protection of Property” and reads as follows:

“Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.”

35

The preceding provision shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties.”

5 80. I bear in mind the observations of Lord Wilson in *R (oao T and Anor) v. Secretary of State for the Home Department* [2014] UKSC 35 at [51], citing Lady Hale in *R (oao Chester) v. Secretary of State for Justice* [2013] UKSC 63; [2014] AC 271 at [100] that the court (and therefore the parties) should indicate in precisely what way it is alleged that the appellant’s rights have been violated. I
10 mention this because (although this may be unfair: see [6] of Ms McCarthy’s written submissions) Mr Firth’s submissions seemed to me to be made on the basis that Mr Lobler’s position is so extreme that it speaks for itself with the effect that the burden is on HMRC to justify its conduct.

15 81. In cases concerning the payment of taxes, the European Court of Human Rights (“ECtHR”) recognises the “wide margin of appreciation” enjoyed by the tax legislation of Member States, see for instance *Gasus Dossier and Fordertechnik GmbH v Netherlands* (1995) 20 EHRR 403 at [60]:

20 “In passing such laws the legislature must be allowed a wide margin of appreciation especially with regard to the question whether –and if so, to what extent– the tax authorities should be put in a better position to enforce tax debts than ordinary creditors are in to enforce commercial debts. The Court will respect the legislature’s assessment in such matters unless it is devoid of reasonable foundation.”

25 82. Tax legislation in itself can be a legitimate aim in the public interest because the collection of taxes is of clear public benefit and is therefore granted “additional deference and latitude”: see *NKM v. Hungary* [2013] STC 1104 at [50]. At [56]-[57], the ECtHR said,

30 “The court further reiterates that the levying of taxes constitutes in principle an interference with the right guaranteed by [A1P1] and that such interference may be justified under the second paragraph of that article, which expressly provides for an exception in respect of the payment of taxes or other contributions. However, this issue is nonetheless within the court’s control...

35 ...it is naturally in the first place for the national authorities to decide what kind of taxes or contributions are to be collected. The decisions in this area will commonly involve the appreciation of political, economic and social questions which the Convention leaves within the competence of the states parties, the domestic authorities being better placed than the court in this connection.”

40 83. Given this wide margin of appreciation in relation to tax legislation, in order for ITTOIA to amount to a breach of an ECHR right, the interference with that right must be “devoid of reasonable foundation”: see *Gasus and National and*

Provincial Building Society and Others v United Kingdom (1998) 25 EHRR 127; [1997] 69 TC 540 esp at [80].

84. The interference could be justified if it satisfied the following three tests (apparently articulated to define “manifestly devoid of reasonable basis”) in *NKM* (at [48], [59] and [60]): (i) the legislation must be sufficiently accessible, precise and foreseeable in its application, (ii) the legislation must pursue a legitimate aim in the public interest and (iii) the interference with the right to peaceful enjoyment must be proportionate in the sense that it strikes a fair balance between the demands of the general interest of the community and the requirements of the protection of the individual’s fundamental rights.

85. Complex as it may be, the legislation is (under (i)) accessible and precise in its application. It is true that, considering “foreseeability”, the legislation’s application is somewhat unintuitive, unexpected and surprising for those not familiar with this aspect of tax law, which would I assume include most policyholders. However, *NKM* also states at [48] that “a rule is “foreseeable” when it affords a measure of protection against arbitrary interferences by the public authorities”. ITTOIA does not allow for arbitrary interferences as the legislation is prescriptive as to when tax is charged and when it is not.

86. As to (ii), Mr Firth argued that the primary aim of the legislation in its current form is administrative convenience and that administrative convenience in itself is not a proportionate legitimate aim in the public interest. Mr Davey however replied that the current form was meant to protect policyholders and insurers as well as HMRC from unnecessarily complex calculations following numerous partial withdrawals and therefore formed a legitimate aim in the public interest.

87. He explained that prior to 1975 the formula in respect of a partial surrender was based on a calculation which involved ascertaining a deduction for the fractional part of the policy surrendered. This method proved unsatisfactory because of the requirement for a large number of computations and a valuation of the policy for each computation. For example, a 10 year policy with monthly part surrenders required 119 successive calculations with 119 successive valuations of the policy surrender value. The revised regime involves a simpler calculation taken at the end of the year in which the part surrender is made and does not give rise to tax charges on small part surrenders.

88. Ms McCarthy pointed out that today’s computers are sophisticated enough to conduct even the most complex calculations in split seconds and therefore avoiding complex calculations in 1975 is no longer in 2015 a good enough reason to convey a public benefit. However this legislation could be seen to have a legitimate aim in the public interest despite its complexity and the unintuitive nature of the particular rule relating to partial surrender. The other side of the coin of Ms McCarthy’s submissions is the fact that the legislation has stood the test of time.

89. (i) and (ii) of the *NKM* test however carry less weight in the determination of a breach of A1P1 if the test in favour of proportionality fails. It was said in *NKM* at [60],

5 “Even if [the interference with A1P1] has taken place subject to the conditions provided for by law –implying the absence of arbitrariness– and in the public interest, an interference with the right to the peaceful enjoyment of possessions must always strike a “fair balance” between the demands of the general interest of the community and the requirements of the protection of the individual’s fundamental rights. In particular, there must be a reasonable relationship of proportionality between the means employed and the aim sought to be realised by the impugned measure.”

15 90. The means employed to achieve the public interest in this case amount to depriving Mr Lobler and his family of all their personal finances and leaving him in a state of possible bankruptcy. Each case must be considered individually on its own merits. Is it possible to conclude that the legislation in question is generally “devoid of reasonable foundation”? In my view the scales tip, only just, in favour of reasonable foundation because the law is not irrational or arbitrary. While it would be fairer if the gain on partial surrenders was calculated using a different and more proportionate method, the fact that it is not does not make the current method of calculating tax on partial surrenders devoid of reasonable foundation. Again, while it would be fairer if the law was simpler, the fact that it is not does not mean that there is a breach of human rights.

30 91. The case is distinguishable from *Hentrich v. France* (1994) 18 EHRR 440, in which the French revenue authority had a right of pre-emption which was exercised after the applicant had bought some land because the price was thought to be too low. The sole purpose of the right was to deter possible underestimations of price. It was held that the pre-emption operated arbitrarily in the absence of adversarial proceedings which enabled the applicant to show that she had paid the proper price. There was no protection from the arbitrariness of the purchase after the event. In the present case the law was ascertainable from the outset.

35 ***If there was such a breach, how should the legislation be construed?***

(1) S.3 HRA

40 92. If I am wrong and interference with A1P1 was established and no justification for that interference were to exist, the route available to the court to avoid breach of Mr Lobler’s rights under the ECHR would be found through s. 3 HRA whereby the relevant legislation is to be construed so that it would achieve the effect of no breach. S. 3(1) HRA states,

“As far as it is possible to do so, primary legislation and subordinate legislation must be read and given effect in a way which is compatible with the Convention rights.”

5 93. Ms McCarthy and Mr Firth take different views as to how s. 3 HRA should be applied. The specific provision that Ms McCarthy has asked the Court to review and construe, s. 539 of ITTOIA, was not raised at first instance, but in the circumstances I propose to deal with it in any event.

10 94. S. 539 deals with deficiency relief. Deficiency relief is available to an individual for a tax year in which a deficiency arises from a policy or a contract on a chargeable event if (a) where a gain had arisen on the chargeable event, the individual would have been liable to income tax on the gain for the year, or the individual would have been so liable apart from the requirement in s. 465(1) that the individual must be UK resident in the tax year in which the gain arises, (b) the individual would (apart from s. 539) be liable to income tax at the higher rate or the dividend upper rate (or both) for the tax year and (c) the individual makes a claim.

20 95. Deficiencies for the purposes of s. 539 are calculated as the total amounts received under the policy, less the premium paid for it and less any amount previously treated as a gain. The relief is not given by setting the deficiency against income in the tax year; instead, there is a calculation of a tax reduction and the total amount of tax due from the taxpayer in the year is reduced by that amount. In other words, the relief is set against the tax due rather than income. The overall effect is that income that would otherwise be taxed at the higher rate or dividend upper rate is taxed at the basic rate or dividend ordinary rate. Deficiency relief is only available to reduce tax in the tax year in which the deficiency arises, and it is only available to be set against income liable to the dividend upper rate or to the higher rate. It is not available to set against income charged to tax at the basic rate or at the additional dividend rate or the additional rate.

30 96. Mr Lobler was not able to rely on deficiency relief for two reasons: first, notwithstanding the deficiency of some \$1,230,000 in 2008/2009 he did not have any other income that would fall within the higher rate or the dividend upper rate as specified in the conditions for deficiency relief in s. 539; and secondly, even if Mr Lobler had surrendered all the rights under the policies in 2011/2012, then even if he had income approaching \$1,230,000, he would not have obtained relief on most of that income which would have been charged to tax at the additional rate of 50%.

40 97. Ms McCarthy therefore submitted that a s. 3 HRA-compliant interpretation of s. 539 would involve: (i) allowing a taxpayer to carry back a deficiency to the tax year(s) in which chargeable event gains have previously arisen and been subject to income tax, in addition to being able to use it in the tax year in which the deficiency arises, and (ii) removing the current restriction for use of the relief only on income liable at the dividend upper rate or higher rate insofar as chargeable

event gains had been charged to tax at other tax rates in the years of part surrender.

98. Mr Davey said, first, that Ms McCarthy's interpretation would open the floodgates to all litigants who made partial surrenders, were governed by ITTOIA and were subsequently taxed at a level which they found surprising. The courts would be flooded with litigants who argued the disproportionate effect of ITTOIA in their cases. Ms McCarthy riposted that any such claim would have to be assessed against the proportionality of the tax incurred in each individual case rather than generally (see for example *R (oao T)* at [51]-[52]) and as it would be very rare that a case was disproportionate to the extent encountered in Mr Lobler's case, this would dismiss the floodgates argument outright. In any event, it seems to me that if that is the proper result of s. 3 HRA, the court must bear the burden of the increased litigation that would flow from it.

99. Secondly, Mr Davey said that s. 539 cannot in itself give rise to a breach of AIP1 so that the interpretative obligation under s. 3 HRA cannot be directed at s. 539. Ms McCarthy argued that s. 539 did give rise to a breach of AIP1 because the inadequacy of the deficiency relief rules was one of the elements causing the disproportionate effect of the legislation in Mr Lobler's case. It was the operation of the regime in the tax legislation taken as a whole that resulted in the breach: see *Energys Holdings UK Ltd v HMRC* [2010] UKFTT 20 (TC) esp at [24]-[25], [45], [56]-[57], [60] and [70]. Even if such an assumption was erroneous and s. 539 did not in itself give rise to a breach, the tribunal was still bound to consider the entire scheme of Chapter 9 of Part 4 of ITTOIA: *Vodafone 2 v HMRC* [2009] STC 1480 at [32]-[36].

100. Thirdly, Mr Davey argued that it was simply not possible to read the requisite language into s. 539 (and he said that it was still not clear to him precisely how s. 539 would have to be construed to make it compatible with ECHR rights) without going against the thrust of the legislation and parliamentary intent. Ms McCarthy relied on *Ghaidan*, which says that an ECHR-compliant interpretation of the law must be given unless such interpretation would go against the "fundamental features of the legislative scheme".

101. One question is therefore whether the reading of s. 539 contended for by Ms McCarthy would go against the fundamental features of the legislation in relation to deficiency relief. In taxation law the cardinal principle or "grain" of the legislation is famously difficult to discern, contrasting the position under the Children Act 1989 *per* Lord Nicholls at [23] of *Re S (Care Order: Implementation of Care Plan)* [2002] UKHL 10; [2002] 2 AC 291. In relation to tax relief legislation, there are often a number of elements, which apply in different ways and circumstances. However, Mr Davey submitted that the fundamental features of tax legislation concerned basic matters such as rate and tax year. Ms McCarthy on the other hand (relying on *R (oao Wilkinson) v IRC* [2005] UKHL 30 at [15] and [19] *per* Lord Hoffmann) gave hypothetical examples of situations where she said an ECHR-compliant interpretation would not be possible, to demonstrate that the current case is distinguishable and that requisite changes could be read into s. 539 to make it compatible.

102. On the one hand the relevant legislation is clear in its consequences and serves a legitimate public interest. On the other hand in this particular instance it produced an unfair result. Could a breach of A1P1 in relation to Mr Lobler's rights be remedied by reading s. 539 in a way that is consistent with human rights? In other words, is it possible to do so within A1P1? To turn a piece of legislation that is black and white in its consequences into one where in some cases the consequences might be grey is a dangerous decision to make. Moreover, a court would have to be cautious in interfering with the Revenue's wide margin of appreciation especially where the effects of the laws in question are clearly foreseeable and carry a legitimate aim in the public interest. I bear in mind Lord Hutton's strictures in *R oao Rusbridger and Another v Attorney-General* [2003] UKHL 38; [2004] 1 AC 357 that, "sections 3 and 4 of the Human Rights Act 1998 are not intended to be an instrument by which the courts can chivvy Parliament into spring-cleaning the statute book." In any event I agree with Mr Davey that the tax year and rate are the fundamental features of the legislative scheme and that they should not be altered.

103. I therefore dismiss Ms McCarthy's persuasive suggestions.

104. Mr Firth adopted a different approach contending that I should use the (undefined) term "overcharged" in s. 50(6)(a) of the Taxes Management Act 1970 ("TMA 1970") to cover Mr Lobler's case. S. 50(6) was raised as an (unopposed by HMRC) amendment to the grounds of appeal against the FTT decision. In order to avoid a breach of s. 3 HRA Mr Firth contends that I should simply reduce what I perceive to be the over-assessment.

105. Mr Firth argues that the court has gone much further than what he calls, "a simple gloss on an inherently flexible word", in the past, relying for that proposition on *Secretary of State for the Home Department v. MB* [2007] UKHL 46. In that case words obliging the court to, "give permission to the Secretary of State to withhold closed material where it considers that disclosure of that material would be contrary to the public interest" were qualified by further wording "except where to do so would be incompatible with the right of the controlled person to a fair trial".

106. He relied on *Willey v. HMRC* [2013] UKFTT 328 (TC), in which the FTT held that the term "overcharged" in s. 50(6) included an assessment which overcharged the taxpayer by virtue of the assessment being devoid of reasonable foundation in the case of a charge to tax or disproportionate in the case of a penalty. However in that case the FTT did not allow the appeal, finding that the charge was not disproportionate, nor devoid of reasonable foundation, nor outside the wide margin of appreciation enjoyed by Parliament.

107. It seems to me that, as Mr Firth admits, the word "overcharged" in s. 50(6)(a) TMA 1970 primarily refers to being overcharged by reference to the tax legislation. Mr Lobler has incurred the tax charge that was envisaged under the legislation and there is no element of "overcharge", as that term is usually understood.

108. The law is set out in primary legislation and HMRC’s website publishes guidance about it, so that the legislation does not leave the tax position uncertain and the consequence of falling within the relevant rule is clear. The rule has the legitimate aim of charging to income tax the value taken from life assurance policies. It would be surprising if s. 50(6) left it to the FTT to decide whether or not a particular charge to tax were reasonable. In *HMRC v. Boshier* [2013] UKUT 0579 (TCC) esp at [45]-[62] and [68], the UT (Warren J and Judge Bishopp) said,

“[45]...The correct approach is to interpret the legislation according to ordinary canons of construction, bearing in mind the Convention as one would bear in mind any treaty, but not having regard to the powerful interpretative direction found in s. 3. Where the legislation is ambiguous, then an interpretation which better reflects the Convention rights is clearly to be preferred. It is only where the unambiguous meaning (or each of a set of ambiguous meanings) is clearly incompatible with the Convention rights that section 3 comes into play. In other words, construe the legislation and, if that construction is not compatible with the Convention rights, find a construction which is compatible “so far as it is possible to do so”. This it seems to us was the approach adopted in *Ghaidan*...

[46] On that approach, it is clear that the powers of the Tax Chamber under section 100B(2)(a)(iii) relate only to the correctness of the amount of the penalty ascertained in accordance with the provisions of s. 98A(2). In the present case, there is no doubt that the penalties under appeal were not “incorrect” in that sense. We do not understand Mr Gordon to disagree with that. His whole challenge is to the proportionality of the total amount of the penalties which is why he seeks, under s. 3, to impose an interpretation of s. 100B which on any ordinary reading it does not bear.”

109. I agree. All of the tax was properly imposed in accordance with the legislation. Mr Lobler’s right of appeal is limited to the situation where the charge was an overcharge under the provisions of the legislation. It was not. Mr Lobler’s argument appears to be that the effect of the legislation is prescriptive rather than intuitive, but that is not the test.

35 (2) *Article 14 ECHR (read together with AIP1)*

110. Article 14 provides as follows:

“The enjoyment of the rights and freedoms set forth in [the] Convention shall be secured without discrimination on any ground such as sex, race, colour, language, religion, political or other opinion, national or social origin, association with a national minority, property, birth or other status.”

111. Mr Firth cited in support of his argument *National & Provincial Building Society v The United Kingdom* [1997] 69 TC 540 where the discriminatory status was interpreted broadly. The ECtHR said at [80] (dismissing the applications),

5 “...an interference, including one resulting from a measure to secure the payment of taxes, must strike a “fair balance” between the demands of the general interest of the community and the requirements of the protection of the individual’s fundamental rights...there must therefore be a reasonable relationship of proportionality between the means employed and the aims pursued.”

10 And at [88],

15 “The Court reiterates that Article 14 of the Convention affords protection against discrimination in the enjoyment of the rights and freedoms safeguarded by the other substantive provisions of the Convention. However not every difference in treatment will amount to a violation of this Article. Instead, it must be established that other persons in an analogous or relevantly similar situation enjoy preferential treatment, and that there is no reasonable or objective justification for this distinction. Furthermore, Contracting States enjoy a margin of appreciation in assessing whether or to what extent differences in otherwise similar situations justify a different treatment in law...”

112. Mr Firth submitted that there was no difference between a person who surrendered 100 per cent and one that surrendered 97.5 per cent of their policies and yet the tax treatment was radically different.

25 113. I agree that the legislation can in certain situations be unfair, but it is not discriminatory in the sense in which Article 14 intends the term to apply. All holders of life insurance policies are treated the same way. They can do what they want with their policies. If they opt for partial surrender certain tax consequences follow and the consequences are the same for everyone. While different choices lead to different results, different persons would not be treated differently. In order to be discriminated against Mr Lobler must have some kind of identifiable status which differentiates him from persons subject to different treatment. The only conceivable status in this respect is that of someone who holds a life insurance policy and decides to part surrender an amount of more than five per cent. This is not to my mind the type of status intended to be addressed by Article 14.

114. In any event Article 14 is not a freestanding provision of the ECHR and I have already found that there was no breach of A1P1.

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Public Law

Was the FTT's decision as to its jurisdiction wrong?

115. Judicial Review proceedings have been commenced in this case on 25 July 2013 but they have been stayed pending the outcome of this appeal. They are not
5 in the appeal bundle and the only reference to them I have been able to find, apart from the oral submissions, is in Ms McCarthy's written submissions.

116. Mr Firth submitted that the FTT's decision in relation to its judicial review jurisdiction was erroneous. The FTT said in [27] of its decision:

10 "It seems to us to be clear that HMRC could not have acted differently in their interpretation of the legislation, but it may be arguable that they could have decided not to make the changes to Mr Lobler's self assessments in reliance on their power of management of the tax system. But the jurisdiction given to this tribunal in a case such as this does not extend to making orders to overturn (or "review") the
15 administrative process of HMRC."

117. The source of appeals against income tax assessments and amendments to tax returns can be found in s. 31(1)(a) of the TMA 1970 which provides that an appeal may be brought against any amendment of a self-assessment under certain sections of the Act. Notice of appeal must then be given to HMRC under that
20 section. Mr Firth averred that the FTT had jurisdiction to decide any appeal against any conclusion or amendment made by a closure notice and there was no restriction on which elements of domestic law it could apply in deciding such appeals.

118. With respect to the FTT's decision that it had no judicial review jurisdiction and therefore no jurisdiction to decide on the validity of public law claims, Mr Firth argued that the question whether the tribunal has judicial review jurisdiction was irrelevant because it had not been asked for a judicial review remedy. The FTT had only he said been asked to determine whether the tax assessment and resulting charge imposed on Mr Lobler were valid.

30 119. At paragraph [36] of *The Commissioners for her Majesty's Revenue and Customs v Hok Limited* [2012] UKUT 363 (TCC) the UT records that it is important to bear in mind how the FTT came into being:

35 "It was created by s 3(1) of the Tribunals, Courts and Enforcement Act 2007, "for the purpose of exercising the functions conferred to it under or by virtue of this Act or any other Act". It follows that its jurisdiction is derived wholly from statute. As Mr Vallat correctly submitted, the statutory provision relevant here, [namely TMA 100B], permits the tribunal to set aside a penalty which has not in fact been incurred, or to correct a penalty which has been incurred but has not
40 been imposed in an incorrect amount, but it goes no further. In particular, neither that provision nor any other gives the tribunal a

discretion to adjust a penalty of the kind imposed in this case, because of a perception that it is unfair or for any similar reason. Pausing there, it is plain that the First-tier Tribunal has no statutory power to discharge, or adjust, a penalty because of the perception that it is unfair.”

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120. At paragraphs [39] and [41] the UT states:

“Ordinarily challenges to administrative actions of government departments for which no clear avenue of appeal is provided must be made by way of judicial review: so much was made clear by the Court of Appeal in *Aspin v Estill* [1987] STC 723 ... At that time judicial review was a comparatively rarely used remedy, and the jurisprudence was at an early stage of development. On this point however, it has remained constant...

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...There is in our judgment no room for doubt that the First-tier Tribunal does not have judicial review jurisdiction.”

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121. Again, in *Bosher*, the UT referred its decision in *Hok*, saying (at [47g]),

“Since the Tax Chamber has itself no judicial review powers...the application for judicial review must be commenced in the Administrative Court. It may, in due course, be transferred to the Upper Tribunal.”

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122. I should flag the point that Mr Firth disputes that *Hok* and *Bosher* were correctly decided. I think they were and he must therefore take the matter to a higher court. In any event I take into account the analogous reasoning in both *Aspin* at 725 and *Customs and Excise Commissioners v. JH Corbitt (Numismatists) Limited* [1981] AC 22 at 60-61 although Mr Firth argues that it is irrelevant to this issue and *Aspin* (a Court of Appeal decision) is inconsistent with House of Lords authorities such as *R v. Home Secretary ex p. Pierson* [1998] AC 539, *R v. Lord President of the Privy Council. ex parte Page* [1993] AC 682, *O'Reilly v. Mackman* [1983] 2 AC 237 and *Fairmount Investments Limited v. Secretary of State for the Environment* [1976] 1 WLR 1255 at 1263.

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123. Mr Firth referred to the case of *Foresight Financial Services Ltd v Revenue and Customs Commissioners* [2011] UKFTT 647 (TC). The question considered by the judge (Geraint Jones QC) was “whether sound common law principles must be left outside the door of the Tribunal room never to cross its threshold”. However, *Foresight* was disapproved in *Hok*, where the UT said (at [55]),

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“Paragraph 12 of his decision in *Foresight Financial Services Ltd* represents an attempt by the judge to circumvent that difficulty [namely (see *Hok* at [54]) whether HMRC should be precluded from imposing or collecting penalties was a separate question of administration capable of review only by way of judicial review] by drawing a distinction between judicial review and the application of

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common law principles. We do not accept that there is any warrant for drawing such a distinction; indeed we think it is a false distinction.”

And the UT went on in the same paragraph,

5 “But even if it is not, we do not accept the judge’s view that the First-
tier Tribunal is able to give effect to common law principles in order
to override the clear words of a statute; indeed it must be doubtful
whether the High Court could ever legitimately do so. The reality,
10 moreover, is that the judge was not determining that the penalties were
not due by reason of some common-law impediment, but that HMRC
should not have imposed them. That is classically a matter for judicial
review.”

124. Mr Firth relies on the decision of Sales J in *Oxfam v Revenue and Customs
Commissioners* [2010] STC 686 at [74]-[78] and [66] and [67]. In the latter
15 paragraphs it was considered whether Oxfam’s legitimate expectation argument
could be dealt with by the FTT. Sales J said,

20 “[66] However, the parties thought that the Tribunal did not have
jurisdiction to consider Oxfam's alternative legitimate expectation
argument. In my view, this is not correct. By the same construction of
section 83(1)(c) and the same reasoning which led to the conclusion
that Oxfam's contract claim was within the jurisdiction of the
Tribunal, Oxfam's legitimate expectation argument also fell within the
jurisdiction of the Tribunal. I can see no sensible basis in the language
of that provision for differentiating between Oxfam's contract claim
25 and its legitimate expectation claim. In both cases, if Oxfam's claim
had been made out, an error of law on the part of HMRC in arriving at
its decision on the amount of input tax to be credited to Oxfam would
have been established (either a failure to respect Oxfam's contractual
rights or a failure to treat Oxfam fairly, in breach of Oxfam's
30 legitimate expectation) which would, on the face of it, be a proper
basis for an appeal to the Tribunal against HMRC's decision within
the terms of section 83(1)(c) .

35 [67] Usually, of course, an appeal under one of the sub-paragraphs of
section 83(1) will be on the merits of decision taken by HMRC, and
questions of private law or public law (such as whether HMRC took
into account irrelevant considerations or failed to take account of
relevant considerations) will simply not be relevant to the Tribunal's
task on the appeal. But in my view it does not follow from this that the
Tribunal will never have jurisdiction to consider issues of general
40 private law and general public law where that is necessary for it to
determine the outcome of an appeal against a decision of HMRC
whose subject matter falls within one of the sub-paragraphs of section
83(1)...

[69] The tribunal is used to dealing with complex issues of tax law. There is no reason to think that it would not be competent to deal with issues of public law, in so far as they might be relevant to determine the outcome of any appeal.”

5 125. In *Foresight* the FTT had said at paragraphs [13] and [14]

10 “What, in my judgment, Sales J decided in the *Oxfam* case was that sound principles of the common law are not to be left languishing outside the Tribunal room door when an appeal is heard in the FTT. He decided that they are a welcome participant at the appeal proceedings and, in appropriate circumstances, must be applied. There is plainly a stark distinction between the FTT, on the one hand, applying sound common law principles, which amounts to the application of substantive common law to the appeal proceedings and, on the other hand, seeking to exercise a supervisory power by way of
15 Judicial Review.”

126. However all issues cannot be decided or considered by the FTT. As the UT said in *Hok* at [53]-[54],

“At first glance, what Sales J said in *Oxfam* leads to a different conclusion, but on closer analysis we do not think it does....

20 ...it becomes clear that the issue in that case and the issue here are quite different. There the tribunal was required to decide the amount of input tax which Oxfam could recover, a question which, as Sales J said at [63], comes four-square within the ambit of s. 83(1)(c) of VATA. Here the question is not the amount of a penalty, or even whether one is due as a matter of law- there is no dispute that s. 98A was engaged, and that it imposed a liability for five monthly penalties of £100 each- but whether HMRC should be precluded from imposing the penalties prescribed by that section, or from collecting them if imposed. That in our judgment, is a quite separate question of
25 administration, one which, in accordance with the authorities to which we have already referred, is capable of determination only by way of
30 judicial review and therefore not by the First-tier Tribunal.”

35 127. On the facts in *Hok* the question was therefore a different one and one which is not dissimilar to that in the present case. There is no dispute that ITTOIA applies and that the liability incurred is a direct result of the statute. The question is whether HMRC should be precluded from imposing and collecting a disproportionate tax charge, namely whether it would be fair and reasonable of them to do so. In *Hok* the tribunal concluded (at [59]), “...accordingly, it is unnecessary for this decision for us to consider whether HMRC’s conduct was in
40 fact unfair...”

128. I do not consider that the FTT would have had jurisdiction to decide this matter and therefore I dismiss this ground of appeal.

Lawfulness of HMRC's conduct

129. Mr Firth argued as his second public law ground that the basis upon which relief should be granted by the UT is HMRC's alleged unlawful exercise of its power to assess tax or amend tax returns in the light of the relevant human rights provisions.

130. Mr Firth's point was that it was open to the FTT to reach the conclusion that there was no valid amendment. The basis is that the House of Lords has established that a decision that breaches public law principles is *ultra vires* the power conferred by the legislation (or alternatively is an abuse of process, see below) and thus not a valid decision at all within the meaning of the legislation.

131. Where judicial review proceedings have already been commenced such proceedings are often transferred to the UT to be considered jointly with an appeal. I have no doubt that the Administrative Court is the correct court, at least initially, to deal with public law questions and the choice has already been made to bring judicial review proceedings. However I will set out counsel's arguments to the contrary as a matter of courtesy, although nothing I say should be taken as binding in any way on any court or tribunal in the future.

132. Mr Firth argued that for the FTT to assess principles of public law would not amount to an abuse of process. He said that there was plainly no disadvantage for HMRC, Mr Lobler, the public or the tribunal in asking the UT to determine a question of public law in this forum. He relied on the decisions in *Winder v. Wandsworth LBC* [1985] AC 46 and *Pawlowski v Dunnington* [1991] STC 550 where the Court of Appeal adopted the following formulation from *Dennis Rye Pensions Fund v Sheffield CC* [1998] 1 WLR 840 at 849:

"If the choice has no significant disadvantages for the parties, the public or the court, then it should not normally be regarded as constituting abuse."

133. However, *Dennis Rye* was a completely different case, not one in which the UT was asked on an appeal from the FTT, a body without judicial review jurisdiction, to exercise public law jurisdiction. I have no doubt that the Administrative Court is the appropriate forum in the first instance. There has been no order for the UT to hear judicial review proceedings concurrently with the appeal.

134. The point raised by Mr Firth was that HMRC generally carried the power to decide not to make an amendment to a self-assessment return or to refrain from assessing tax believed to be due because the Revenue has a discretion not to assess the tax in cases of hardship at the margins: *Vestey v IRC* [1980] AC 1148 at 1173 per Lord Wilberforce, and *Wilkinson* at [21] per Lord Hoffmann. He argued that Mr Lobler qualifies as a case of "hardship at the margins" because of the

obvious effect of the pending tax charge on his personal net worth and the unfair result referred to in the lower tribunal's decision.

135. Mr Davey disputed that this was a genuine case of "hardship at the margins." When prompted, he provided three examples of what might qualify as cases of "hardship at the margins": (a) a child trust fund tax charge resulting from the criminal activity of a third party; (b) a pensions provider who provided death benefits late to a widow who incurred a tax charge as a result; and (c) a person in intensive care where there was evidence that their condition would worsen should tax be pursued.

136. Mr Firth's response was that a case at the margins was a case that was sufficiently rare in its occurrence, such as that of Mr Lobler. He further argued that HMRC's decision to amend Mr Lobler's tax return in the way that they did was wholly unreasonable or an abuse of power, submitting that it was precisely in a case such as this that one would expect HMRC to exercise their discretion to refrain from assessing tax. Any decision to the contrary would be unreasonable to the point of caprice. In support, Mr Firth quoted the Insurance Premium Taxation Manual IPTM1510,

"The operation of the rules – which are described in more detail in IPTM3540 onwards – can, from the policyholder's, or chargeable person's standpoint, seem capricious. This is particularly so if withdrawals from the policy are made that do not correspond with the underlying growth in value or if, for example, the value of the bond falls due to adverse stock market conditions."

137. In the alternative, Mr Firth submitted that the decision to amend Mr Lobler's self-assessment tax return was so unfair as to amount to an abuse of power, relying on Simon Brown LJ's statement in *R v IRC ex p. Unilever Plc* [1996] STC at 695,

"Unfairness amounting to an abuse of power as envisaged in *Preston* [*Preston v. IRC* [1985] STC 282] and the other Revenue cases is unlawful not because it involves conduct such as would offend some equivalent private law principle, not principally indeed because it breaches a legitimate expectation that some different substantive decision will be taken, but rather because either it is illogical or immoral or both for a public authority to act with conspicuous unfairness and in that sense abuse its power."

138. Mr Firth also argued that HMRC's decision to amend Mr Lobler's self-assessment was *ultra vires*, both the FTT and the UT having power to grant relief in respect of HMRC's unlawful act.

139. Mr Firth said that HMRC's power to refrain from assessing tax or amending a self-assessment in cases of hardship derives from s. 1 TMA 1970 and that nothing in that section prescribes the particular contours of this power. Instead he argued that such contours must be implied. Where any amendment or assessment

of tax in a case of hardship would also breach the taxpayer's human rights there was an implied duty on HMRC not to amend or assess. The legislation can be given effect in line with the relevant human right and therefore s. 3 HRA 1998 requires that it be so given effect. Mr Firth says that on that basis HMRC had no
5 power to make the amendment without acting *ultra vires*.

140. Secondly, relief. Mr Firth submits that it is unlawful for a public authority to act in a way which is incompatible with an ECHR right (s. 6(1) HRA 1998), subject to the defences in s. 6(2) HRA 1998, which do not apply in this case. A person who claims that a public authority has acted in a way which is unlawful
10 under s. 6(1) HRA 1998 may rely on the ECHR right in any legal proceedings: s. 7(1)(b)) HRA 1998. Where the court finds that an act was unlawful, it may grant "such relief or remedy, or make such order, within its powers as it considers just and appropriate": s. 8(1) HRA 1998. Mr Firth submitted that this would provide a new basis on which the FTT and the UT may grant relief under s. 50(6) TMA
15 1970.

141. HMRC might have used their discretion to amend Mr Lobler's return. However, whether or not they acted unlawfully or *ultra vires* by refusing to do so is a question for judicial review, not for an appeal.

142. Accordingly I allow the appeal on the ground of rectification alone.

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TRIBUNAL JUDGE: The Hon Mrs Justice Proudman DBE

RELEASE DATE: 26 March 2015