TC03188

Appeal number: TC/2013/00400 & TC/2013/00759

SETTLEMENT – Income arising under a settlement where settlor retains interest – Appellants owning bulk shares in company – Appellants waiving right to receive dividends – Appellants' wives receiving significant dividend payments – Appeals dismissed.

FIRST-TIER TRIBUNAL
TAX CHAMBER

MR P DONOVAN **Appellant**
&
MR P MCLAREN

- and -

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

TRIBUNAL: JUDGE J. BLEWITT
MS RUTH WATTS DAVIES

Sitting in public at Bedford Square on 12 December 2013

Mr M Arthur for the Appellant

Mr J Hillier of HM Revenue and Customs for the Respondents

DECISION

1. By Notices of Appeal dated 9 January 2013 the Appellants appealed against the following HMRC decisions:

Appellant	Tax Year Ended	Decision of HMRC	Additional tax
Mr Donovan	5 April 2010	Closure Notice dated 21 June 2012	£4,749.98
Mr Donovan	5 April 2009	Discovery Assessment dated 21 June 2012	£3,689.77
Mr Donovan	5 April 2008	Discovery Assessment dated 22 March 2012	£5,350.85
Mr McLaren	5 April 2010	Closure Notice dated 19 June 2012	£4,731.07
Mr McLaren	5 April 2009	Discovery Assessment dated 19 June 2012	£3,715.20
Mr McLaren	5 April 2008	Discovery Assessment dated 22 March 2012	£5,350.85

2. The ground of appeal relied upon by the Appellants, as set out in their respective Notices of Appeal, is that "*HMRC's decision is wrong in law*".

Background

3. It was confirmed by Mr Arthur on behalf of the Appellants that no issue was taken with the backgrounds and facts set out in HMRC's Statement of Case dated 15 August 2013 and we therefore accepted the following facts:

4. On 16 December 2010 the Appellants filed Self Assessment tax returns for the tax year ended 5 April 2010. On 18 February 2011 HMRC Officer Haytack gave notice to the Appellants under section 9A Taxes Management Act 1970 of her intention to enquire into the tax returns for the year ended 5 April 2010.

5. The Appellants have been directors and shareholders of Victory Fire Limited ("the company") since 1992. The Appellants' wives became shareholders in the company following an allotment of shares being made in 2001.

6. The shareholdings following the allotment in 2001 were as follows:

Mr P. Donovan: 40 £1 ordinary shares (40%)

Mrs R. Donovan 10 £1 ordinary shares (10%)

Mr P. McLaren 40 £1 ordinary shares (40%)

Mrs A. McLaren 10 £1 ordinary shares (10%)

7. Prior to the allotment of shares and for the accounting period ended 31 March 2000 the relevant shareholdings were as follows:

Mr P. Donovan: 1 £1 ordinary shares (50%)

Mrs R. Donovan no shareholding

Mr P. McLaren 1 £1 ordinary shares (50%)

Mrs A. McLaren no shareholding

8. In the company's accounting period to 31 March 2010 a total of £130,000 of dividends were paid in respect of ordinary shares, divided as follows (the figure in brackets represents the percentage of the £130,000):

Mr P. Donovan: £33,000 (25.38%)

Mrs R. Donovan £32,000 (24.62%)

Mr P. McLaren £33,000 (25.38%)

Mrs A. McLaren £32,000 (24.62%)

9. On 6 April 2009 the company declared an interim dividend of £3,200 per ordinary share in respect of the accounting period ended 31 March 2010.

10. On the same date the Appellants signed deeds of dividend waiver, waiving entitlement to the interim dividend arising on their entire holding of ordinary shares in the company from that date for a period of one day.

11. On the same date the Appellants' wives were issued with dividend vouchers showing dividend payments of £32,000 and a 10% tax credit of £3,555.55.

12. On 8 April 2009 the company declared an interim dividend of £825 per ordinary share in respect of the accounting period ended 31 March 2010.

13. On the same date the Appellants' wives signed deeds of dividend waiver, waiving entitlement to the interim dividend arising on their entire holding of ordinary shares in the company from that date for a period of one day.

14. On the same date the Appellants were issued with dividend vouchers showing a dividend payment of £33,000 and a 10% tax credit of £3,666.66.

15. On reviewing the company's accounts and the tax returns of the Appellants for the earlier years, HMRC found the following information pertaining to dividend payments:

Company accounting period end date and total dividends paid	**Mr P Donovan and Mr P McLaren (each)**		**Mrs R Donovan and Mrs A McLaren (each)**	
	A	**B**	**A**	**B**
31 March 2010 £130,000	£52,000	£33,000	£13,000	£32,000
31 March 2009 £112,500	£45,000	£30,200	£11,250	£26,050
31 March 2008 £128,964	£51,585.60	£30,200	£12,896.40	£34,282
31 March 2007 £117,240	£46,896	£28,200	£11,724	£30,420
31 March 2006 £111,240	£44,496	£27,000	£11,124	£28,620
31 March 2005 £116,000	£46,400	£27,000	£11,600	£31,000
31 March 2004 £108,000	££43,200	£27,000	£11,600	£31,000
31 March 2003 £102,000	£40,800	£27,000	£10,200	£24,000

31 March 2002 £92,000	£36,800	£26,000	£9,200	£20,000
31 March 2001 £72,000	£28,800	£26,000	£7,200	£10,000
31 March 2000 £57,000	£28,500	£28,500	Nil	Nil

Figures in Column A represent the total dividend receivable by the individual based on their shareholding in the company. Column B represents the total dividend received in the relevant tax year and declared on the individual's tax return. The Appellants' wives did not file tax returns as they were liable to tax at the basic rate only; the amount of the dividend received by them has therefor been calculated by reference to the amounts received (as declared) by the Appellants and the total dividend amounts paid.

16. On the dates shown in the table at paragraph 1 of this decision HMRC issued the decisions which form the basis of these appeals to the Appellants.

17. Following a review HMRC notified the Appellants by letter dated 1 November 2012 of its intention to uphold the decisions.

18. The Appellants appealed to the Tribunal on 9 January 2013. The appeals were accepted by HMRC as valid despite being out of time.

Preliminary Matters

19. On the morning of the hearing Mr Arthur applied to adduce oral evidence of two witnesses; Mr Donovan (the Appellant) and Mr Wright (the company accountant). No written witness statements were produced and HMRC opposed the application on the basis that it had been given no prior warning of the application. Furthermore Mr Hillier drew our attention to a Tribunal direction dated 8 July 2013 which required that "*not later than 16 August 2013 both parties shall provide to the Tribunal and each other a statement detailing: (a) whether or not witnesses are to be called and if so their names…*" Mr Hillier submitted that not only had the Appellant failed to comply with the direction but had also confirmed by email dated 19 August 2013 that no witnesses would be called.

20. We considered the application carefully and were mindful of the overriding objective and balancing the interests of justice in respect of both parties. We indicated that we were prepared to admit the evidence but that HMRC should not be ambushed by new arguments and information. Consequently we took the view that HMRC should be permitted time to consider the evidence and its impact, if any, on the

appeals. We sought clarification from HMRC as to whether, in such circumstances, it would seek a postponement of the hearing, to which Mr Hillier replied in the affirmative. We indicated that we were prepared to accede to HMRC's request and in our view the Appellant should pay the wasted costs of the hearing on the basis that it had acted unreasonably in failing to comply with a Tribunal direction or give any prior notice of the application to adduce evidence.

21. At that point Mr Arthur, of his own motion, withdrew the application and invited the Tribunal to continue with the hearing; to which we consented.

Legislation

22. Although there was no dispute as to the legislation applicable to these appeals, it may assist to set out the relevant provisions:

Taxes Management Act 1970

29 Assessment where loss of tax discovered

29(1) *If an officer of the Board or the Board discover, as regards any person (the taxpayer) and a year of assessment–*

(a) that any income which ought to have been assessed to income tax, or chargeable gains which ought to have been assessed to capital gains tax, have not been assessed, or

(b) that an assessment to tax is or has become insufficient, or

(c) that any relief which has been given is or has become excessive,

the officer or, as the case may be, the Board may, subject to subsections (2) and (3) below, make an assessment in the amount, or the further amount, which ought in his or their opinion to be charged in order to make good to the Crown the loss of tax.

…

29(3) *Where the taxpayer has made and delivered a return under section 8 or 8A of this Act in respect of the relevant year of assessment, he shall not be assessed under subsection (1) above–*

(a) in respect of the year of assessment mentioned in that subsection; and

(b) in the same capacity as that in which he made and delivered the return,

unless one of the two conditions mentioned below is fulfilled.

…

29(5) *The second condition is that at the time when an officer of the Board–*

(a) ceased to be entitled to give notice of his intention to enquire into the taxpayer's return under section 8 or 8A of this Act in respect of the relevant year of assessment; or

(b) informed the taxpayer that he had completed his enquiries into that return,

the officer could not have been reasonably expected, on the basis of the information made available to him before that time, to be aware of the situation mentioned in subsection (1) above.

***29(6)** For the purposes of subsection (5) above, information is made available to an officer of the Board if–*

(a) it is contained in the taxpayer's return under section 8 or 8A of this Act in respect of the relevant year of assessment (the return), or in any accounts, statements or documents accompanying the return;

(b) it is contained in any claim made as regards the relevant year of assessment by the taxpayer acting in the same capacity as that in which he made the return, or in any accounts, statements or documents accompanying any such claim;

(c) it is contained in any documents, accounts or particulars which, for the purposes of any enquiries into the return or any such claim by an officer of the Board, are produced or furnished by the taxpayer to the officer; or

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

(i) could reasonably be expected to be inferred by an officer of the Board from information falling within paragraphs (a) to (c) above; or

(ii) are notified in writing by the taxpayer to an officer of the Board.

***29(7)** In subsection (6) above–*

(a)any reference to the taxpayer's return under section 8 or 8A of this Act in respect of the relevant year of assessment includes–

(i)a reference to any return of his under that section for either of the two immediately preceding years of assessment; and

(ii)where the return is under section 8 and the taxpayer carries on a trade, profession or business in partnership, a reference to any partnership return with respect to the partnership for the relevant year of assessment or either of those periods; and

(b) any reference in paragraphs (b) to (d) to the taxpayer includes a reference to a person acting on his behalf.

…

***29(9)** Any reference in this section to the relevant year of assessment is a reference to–*

(a) in the case of the situation mentioned in paragraph (a) or (b) of subsection (1) above, the year of assessment mentioned in that subsection; and

ITTOIA 2005

Meaning of "settlement" and "settlor"
620 (1) In this Chapter—
"settlement" includes any disposition, trust, covenant, agreement, arrangement or transfer of assets (except that it does not include a charitable loan arrangement), and
"settlor", in relation to a settlement, means any person by whom the settlement was made.

624 Income where settlor retains an interest
(1)Income which arises under a settlement is treated for income tax purposes as the income of the settlor and of the settlor alone if it arises—
(a)during the life of the settlor, and
(b)from property in which the settlor has an interest.

626 Exception for outright gifts between spouses

(1)The rule in section 624(1) does not apply in respect of an outright gift–
(a)of property from which income arises,
(b)made by one spouse to the other, and
(c) meeting conditions A and B.
(2)Condition A is that the gift carries a right to the whole of the income.
(3)Condition B is that the property is not wholly or substantially a right to income.
(4)A gift is not an outright gift for the purposes of this section if–
(a)it is subject to conditions, or
(b)there are any circumstances in which the property, or any related property–
(i)is payable to the giver,
(ii)is applicable for the benefit of the giver, or
(iii)will, or may become, so payable or applicable.
(5)"Related property" has the same meaning in this section as in section 625.

HMRC's Case

23. Mr Hillier helpfully provided us with a detailed skeleton argument setting out the case for HMRC. The matters in issue in this case are:

(a) Whether the dividend waivers executed by the Appellants in favour of their wives constitute a settlement for Income Tax purposes; and

(b) Whether HMRC were entitled to raise discovery assessments.

24. The burden of proof (in respect of which no issue was taken by Mr Arthur) rests with the Appellants to show that they were overcharged by the amended self-assessment following from the Closure Notices. HMRC must prove that that the

discovery assessments were made in accordance with Section 29 TMA 1970 whereafter the burden falls to the Appellants to show that they were overcharged by the assessments. The standard of proof on all matters is on the balance of probabilities.

Dividend Waivers

25. HMRC submitted that the effect of the dividend waivers, and the intention of them, was to allow higher dividends to be paid to the Appellants' wives than their respective shareholdings entitled and lower dividends to be received by the Appellants. In a letter from the Appellants' representative to HMRC dated 14 September 2012 it was contended that the dividends were waived because the Appellants did not want the dividends and not because they wanted increased dividends to be paid to their wives. HMRC submitted that this contention was contradicted by an earlier letter from the Appellants' representative to HMRC dated 16 December 2011 in which it was stated that the directors wished to vote different rates of dividend for the shareholders.

Settlement

26. HMRC referred us to Section 620 ITTOIA 2005 which provides the definition of "settlement" and "settlor" for the purposes of Part 5 Chapter 5 ITTOIA 2005. Mr Hillier submitted that both the Appellants' dividend waivers and the consequent payment of dividends to their wives constituted an "arrangement" in accordance with section 620 ITTOIA 2005 and that as it was the Appellants who waived the dividends, it is the Appellants who are the settlors.

27. HMRC cited *Jones v Garnett (HM Inspector of Taxes)* [2007] UKHL 35 in which the House of Lords endorsed a broad concept of "arrangement" which does not require any formal legal trust or settlement to bring the statutory provisions into operation. The earlier authorities references in *Jones* support the proposition that a definite plan, including a relatively simple one, to use a company's shares to divert income falls within the meaning of an arrangement.

28. HMRC invited the Tribunal to infer that the Appellants waived entitlement to dividends as part of a plan that dividend income otherwise due to the Appellants would be paid to their wives, which constitutes an arrangement. HMRC submitted that the following facts support such an inference:

(a) That the Appellants, on 6 April 2009, irrevocably waived their entitlement to dividends for a period of 1 day;

(b) On the same day a dividend of £3,200 per ordinary share was declared;

(c) The Appellants' wives on 8 April 2009 irrevocably waived their entitlement to dividends for a period of 1 day;

(d) On the same day a dividend of £825 per ordinary share was declared;

(e) The Appellants' wives subsequently received dividends of £32,000 each;

(f) The statement by the Appellants' representative (in its letter to HMRC dated 16 December 2011) that the Appellants wished for different rates of dividends to be paid to different shareholders;

(g) Similar dividend waiver arrangements have been enacted in the tax years ended 5 April 2008 and 5 April 2009;

(h) There were insufficient distributable reserves to pay out the dividends declared by VFL in each of the tax years ended 5 April 2008, 5 April 2009 and 5 April 2010.

29. Mr Hillier submitted that it is more likely than not that this plan was implemented with an intention to avoid tax; by seeking to bring about a near equalisation of their dividend income, the Appellants and their wives reduced their aggregate liability to Income Tax by taking advantage of the wives' unused basic rate band of tax. However, Mr Hillier relied on the submission that an intention to avoid tax is not essential for a settlement to exist citing Lord Walker and Lord Neuberger in *Jones* in support of this argument.

30. In response to the Appellant's assertion that the reason for executing the dividend waiver was to maintain reserves and cash balances in order to accumulate sufficient of each to fund the purchase of the company's own freehold property, Mr Hillier submitted that if such an assertion was true, the aim could have been achieved by voting a lower dividend per share. Mr Hillier also noted that there was no evidence to support the Appellants' contention beyond the statement having been made in a letter to HMRC dated 24 October 2011 and even if the assertion was correct, there still existed a plan in the minds of the Appellants which supports HMRC's argument that an arrangement, and therefore settlement, existed.

Bounty

31. For there to be a settlement in accordance with the relevant statutory provisions the arrangement requires an element of bounty. HMRC relied on the case of *Jones* in which it was said:

"Not every transfer of property is a settlement for the purposes of section 660A. There has to be an "element of bounty" in the transaction. This old-fashioned phrase, apparently derived from the judgment of Plowman J in Commissioners of Inland Revenue ***v*** *Leiner (1964) 41 TC 589, 596 and approved by the House of Lords in Inland Revenue Commissioners* ***v*** *Plummer [1980] AC 896, 913, conjuring up the image of Lady Bountiful in The Beaux' Stratagem, is perhaps not the happiest way of describing a provision for a spouse or minor children. A donation to a spouse or child is traditionally expressed in a deed to be "in consideration of natural love and affection" rather than the donor's bounty. It is nevertheless exactly the kind of thing at which the anti-avoidance provisions are aimed. In Chinn* ***v*** *Hochstrasser [1981] AC 533, 555 Lord Roskill cautioned against treating the word "bounty" as if it had been included in the statute. It seems to me that the general effect of the cases is that, under*

the arrangement, the settlor must provide a benefit which would not have been provided in a transaction at arms' length…

Carnwath LJ made a rather different point when he said, at para 108, that this was the first time in which the revenue had sought to apply the concept of a "settlement" in sections 660A or 660B to —

> *"a normal commercial transaction between two adults, to which each is making a substantial commercial contribution, albeit not of the same economic value."*

I cannot agree that this was a "normal commercial transaction between two adults." It made sense only on the basis that the two adults were married to each other. If Mrs Jones had been a stranger offering her services as a book keeper, it would have been a most abnormal transaction. It would not have been an arrangement into which Mr Jones would ever have entered with someone with whom he was dealing at arms' length. It was only "natural love and affection" which provided the consideration for the benefit he intended to confer upon his wife. That is sufficient to provide the necessary "element of bounty".

32. HMRC contended that the Appellants' arrangement was not one which would have been entered into with someone at arm's length and therefore the arrangement plainly contained an element of bounty.

33. There was no commercial purpose to the dividend waivers executed over a number of years. The retention of profits could have been more easily achieved by voting a lower rate of dividend; instead a series of waivers and payments at different rates to different shareholders was executed which only made sense on the basis that the Appellants and their wives were married. The Appellant conceded this point in a letter to HMRC dated 14 September 2012 in which it stated:

"I do not understand the Inspector's reference to the dividend waivers not being on arm's length terms and without commercial purpose. Dividend waivers are by their very nature not on arm's length or commercial…"

34. Mr Hillier submitted that there was further support for the element of bounty can be found in the fact that the company had insufficient distributable reserves to pay the dividends declared unless the dividend waivers were enacted. HMRC exhibited a document prepared from the company accounts which demonstrated the position with and without dividend waivers which confirmed that had the waivers not been executed in the tax years from 5 April 2001 to 5 April 2010 there would have been insufficient distributable profits to pay a divided in respect of each share in the company at the rate at which the Appellants' wives were paid a dividend for each accounting period from 31 March 2002 onwards. The Appellant's contention that there were sufficient distributable reserves is only true if the dividend waiver arrangements of previous years are ignored which, HMRC submitted, was not the correct approach as the arrangements have a cumulative effect year on year which should not be ignored.

35. HMRC argued that even if the company's distributable reserves is a relevant factor, the regularity, nature and consequences of the waivers is evidence of a single arrangement under which the parties have an understanding that their incomes from the dividends would be broadly equalised; the Appellants could have transferred any proportion of the company shares to their wives at any time yet chose not to do so in the tax years relevant to these appeals. Furthermore, irrespective as to whether or not there were sufficient distributable reserves, the dividend waiver arrangement would not have taken place at arm's length and this alone is sufficient to demonstrate the element of bounty.

Settlor's Interest

36. Sections 619 and 624 ITTOIA 2005 are satisfied on the basis that the income which arises from the dividend waiver arrangement clearly arises during the lives of the Appellants and the dividend income paid to their wives from their shares, together with the dividend rights attached to them, are benefits enjoyed by the Appellants' wives. They constitute property in which the Appellants have an interest by virtue of section 625 ITTOIA 2005.

Exception

37. The exception set out in section 626 ITTOIA 2005 does not apply in this case nor did the Appellant previously contend that it did. There is no outright gift but rather a dividend waiver that was declared in respect of shares, and the shares were retained by the Appellants and not given to their wives. The case of *Jones* in which the exception was held to apply can be distinguished as there had been a transfer of the ordinary share held by the wife; no such transfer took place in the instant appeals.

38. In support of it's submissions HMRC relied on the case of *Buck v R & C Commrs* [SpC 716] in which it was stated:

"For completeness, I turn now to section 660A(6). That was the provision that, on the basis of the decision of the House of Lords in Jones ***v*** *Garnett, excluded the wife's income under the arrangement in that case from being taxed as her husband's.*

Section 660A(6) excludes an "outright gift" of property from one spouse to the other from the scope of the taxation of settlor provisions. That exclusion does not however apply whereas here the property given is wholly or substantially a right to income: section 660A(6)(b). Here, income is diverted by means of a dividend waiver in anticipation of the declaration of a dividend. There is no "outright gift", merely a one-off waiver of any dividend that might be declared in respect of shares: and the shares in question are retained by the previous person making the waiver and not given to the other spouse."

Discovery Assessments

39. HMRC submitted that the requirements of section 29 TMA 1970 are satisfied. A discovery was made in that it became apparent to HMRC Officer Haytack that there was an error in the Appellant's tax return for the year ended 5 April 2010 which

caused the officer to seek information in relation to the dividends received by the Appellants and their wives in the tax years ended 5 April 2009 and 5 April 2008. Upon examination of the information the officer reached a conclusion that the self-assessments for each of the relevant tax years was insufficient and issued assessments to make good the loss of tax.

40. We were referred to the case of *Hankinson v R&C Commrs* [2011] EWCA Civ 1566 in which the meaning of "discovery" was discussed (paragraphs 15 and 16):

"*I begin with section 29 (1). This sub-section comes into operation if an officer of the Board "discovers" an undercharge. The word "discovers" in this context has a long history. Although the conditions under which a discovery assessment can be made have been tightened in recent years following the introduction of the self-assessment regime, the meaning of the word "discovers" in this context has not changed. In R* ***v*** *Commissioners for the General Purposes of the Income Tax for Kensington [1913] 3 KB 870 Bray J said that it meant "comes to the conclusion from the examination he makes and from any information he may choose to receive"; and Lush J said that it was equivalent to "finds" or "satisfies himself". In Cenlon Finance Co Ltd* ***v*** *Ellwood [1962] AC 782 the House of Lords considered the meaning of the word "discovers". They rejected the argument that a discovery entailed the ascertainment of a new fact. Viscount Simonds said:"I can see no reason for saying that a discovery of undercharge can only arise where a new fact has been discovered. The words are apt to include any case in which for any reason it newly appears that the taxpayer has been undercharged and the context supports rather than detracts from this interpretation."*

Lord Denning said:

"Mr. Shelbourne said that "discovery" means finding out something new about the facts. It does not mean a change of mind about the law. He said that everyone is presumed to know the law, even an inspector of taxes. I am afraid I cannot agree with Mr. Shelbourne about this. It is a mistake to say that everyone is presumed to know the law. The true proposition is that no one is to be excused from doing his duty by pleading that he did not know the law. Every lawyer who, in his researches in the books, finds out that he was mistaken about the law, makes a discovery. So also does an inspector of taxes."

41. The condition set out in section 29(5) TMA 1970 is satisfied on the basis that at the time specified in s29(5)(a) an officer could not have been reasonably expected, on the basis of the information made available to him before that time, to be aware of the insufficiency of the Appellants' self-assessment for the relevant tax years. Mr Hillier relied on *R & C Commrs v Lansdowne Partners Limited Partnership* [2010] EWHC 2582 (Ch) in which Lewison J cited the Special Commissioner in *Corbally-Stourton v R & C Commrs* (SpC 692) with approval:

"*In Corbally-Stourton Mr Hellier pointed out (correctly in my judgment) that:*

i) The statutory reference is to "an officer" of the Board, not to any particular officer;

ii) This entails a hypothetical officer rather than any real individual;

iii) The hypothetical officer must be endowed with knowledge of elementary arithmetic, some knowledge of tax law, and some tax law, all of which he will apply to the prescribed sources of information.

42. As to "information made available" as set out in s29(6) TMA 1970 HMRC relied on Auld LJ in Langham v Veltema [2004] EWCA Civ 193 at paragraph 36:

"*The answer to the second issue– as to the source of the information for the purpose of section 29(5) - though distinct from, may throw some light on, the answer to the first issue. It seems to me that the key to the scheme is that the Inspector is to be shut out from making a discovery assessment under the section only when the taxpayer or his representatives, in making an honest and accurate return or in responding to a section 9A enquiry, have clearly alerted him to the insufficiency of the assessment, not where the Inspector may have some other information, not normally part of his checks, that may put the sufficiency of the assessment in question. If that other information when seen by the Inspector does cause him to question the assessment, he has the option of making a section 9A enquiry before the discovery provisions of section 29(5) come into play. That scheme is clearly supported by the express identification in section 29(6) only of categories of information emanating from the taxpayer. It does not help, it seems to me, to consider how else the draftsman might have dealt with the matter. It is true, as Mr. Sherry suggested, he might have expressed the relevant passage in section 29(5) as "on the basis only of information made available to him", and the passage in section 29(6) as "For the purposes of subsection (5) above, information is made available to an officer of the Board if, but only if," it fell within the specified categories. However, if he had intended that the categories of information specified in section 29(6) should not be an exhaustive list, he could have expressed its opening words in an inclusive form, for example, "For the purposes of subsection (5) above, information … made available to an officer of the Board … includes any of the following".*

43. Mr Hillier submitted that there was no information upon which the hypothetical officer could reasonably have been expected to be aware of the insufficiency of the Appellants' self-assessment for the tax years 5 April 2008 and 5 April 2009 for the following reasons:

(a) The Appellants' tax returns for each of those tax years and the two preceding years do not state that dividend waivers were executed, do not give the dividends voted and paid by the company or the Appellants' shareholdings;

(b) No claims were made by the Appellants in respect of the two tax years or two years preceding;

(c) There were no enquiries into the Appellants; tax returns for those tax years or the two preceding years; and

(d) The Appellants did not write to an officer of the board providing details of the dividend waivers executed in those tax years.

44. There was no dispute that the discovery assessments were made within the time limit and HMRC submitted that the assessments were made in accordance with the legislation applicable.

The Appellants' Case

45. Mr Arthur on behalf of the Appellants took no issue with HMRC's skeleton argument. He stated that whilst it is the Appellant's responsibility to demonstrate the propriety of the case the taxpayer must be able to respond to HMRC's Statement of Case and the assertion that there was no commercial purpose to the dividend waivers.

46. Mr Arthur contended that HMRC had not produced any witness evidence in support of its case and, as a result, the Appellant is unable to challenge the case. He questioned the propriety of the appeals continuing in such circumstances.

47. It was submitted that HMRC was incorrect in asserting that the company did not have sufficient distributable reserves and a document was produced showing the reserves and cash balances from 2000 to 2013. Mr Arthur contended that the document supported the Appellant's argument that HMRC had not proved that the necessary element of bounty was present.

48. The reason that the commercial decision was taken to waive the dividend entitlement was to ensure that the company maintained workable reserves and cash balances in order to accumulate sufficient of each to fund the purchase of the company's own freehold property. Mr Arthur submitted that it made "tax planning sense" that the benefit of the dividends was used in the correct way.

49. On the issue of discovery Mr Arthur contended that, as there was no HMRC witness to question, what was known by the HMRC officer was a matter of speculation. He submitted that a competent inspector would have been aware of the dividends and their allocation which precluded a discovery assessment.

50. It was submitted that the Appellants' wives each paid £1 for the allotted shares. No actual monies were exchanged but the accounts were altered to reflect the position. In such circumstances the shares constitute a gift and therefore fall within the exception set out in section 626 ITTOIA 2005. It was accepted that this argument had not been raised prior to the hearing however the Appellant's representative only became aware of argument when HMRC outlined its position on the issue.

Discussion and Decision

51. We considered the submissions of both parties carefully, together with the bundle of documents exhibited by HMRC which contained, inter alia, the source documents in support of its case.

52. We were satisfied that there had been ample time for the Appellants and their representative to prepare the case and noted that it had been at the request of Mr Arthur that the hearing continued without any evidence from the Appellant. The lack of evidence did not prevent submissions being made on behalf of the Appellant and a challenge being made to HMRC's case in that manner.

53. We found the irresistible inference from the facts of these appeals to be that the Appellants waived their entitlement to dividends as part of a plan to ensure that the dividend income became payable to their wives. We agreed with Sir Stephen Oliver QC in *Buck v R&C Commrs* that:

"…there is no need for any formal legal trust or settlement to bring the statutory provisions into operation…a definite plan, including a relatively simple one, to use a company's shares to divert income falls within the meaning of an arrangement…"

54. We were satisfied on the balance of probabilities that the intention behind the plan was tax geared to bring about a near equalisation of the Appellants' and their wives' dividend income thereby reducing their aggregate liability to Income Tax. In reaching this decision we considered the Appellant's assertion (unsupported by evidence but set out in correspondence contained within the bundle provided to us) that the reason for executing the dividend waiver was to maintain reserves and cash balances in order to accumulate sufficient of each to fund the purchase of the company's own freehold property. On the balance of probabilities we preferred the submissions of HMRC and accepted, not least from the repeated dividend waivers over a significant number of years, that had this been the case the aim could have been achieved by other means such as voting a lower dividend per share.

55. However, even if we are not correct in drawing such an inference, there was, on any view, a plan in the minds of the Appellants which Mr Arthur accepted made "tax planning sense" and which was efficacious for tax avoidance. We followed the guidance in *Jones* (at paragraphs 48 and 75) and concluded that irrespective of whether or not there was an intention to avoid tax, an arrangement, and therefore a settlement, clearly existed in this case:

"An intention to avoid tax is not, I think, absolutely essential. It is possible to imagine that an arrangement planned for some other purpose (such as pre-empting the consequences of insolvency or divorce) could unexpectedly prove efficacious for tax avoidance and amount to an arrangement (and so to a settlement). But usually an intention to avoid or minimise tax can readily be inferred (in this case it was candidly admitted) and that intention is part of the factual material that has to be looked at in the round. Sir Wilfred Greene MR put it trenchantly in IRC ***v*** *Payne at 626:*

"It appears to me that the whole of what was done must be looked at; and when that is done, the true view, in my judgment, is that Mr Walter Payne deliberately placed himself into a certain relationship to the company as part of one definite scheme, the essential heads of which could have been put down in numbered paragraphs on half a sheet of notepaper. Those were the things which it was essential that Mr Payne should do if he wished to bring about the result desired. He did it by a combination of

obtaining the control of the company, entering into the covenant, and then dealing with the company in such a way as to achieve his object. Now, if a deliberate scheme, perfectly clear-cut, of that description is not an 'arrangement' within the meaning of the definition clause, I have difficulty myself in seeing what useful purpose was achieved by the Legislature in putting that word into the definition at all."

…The definition of "settlement" in section 660G (1) appears, on its face, to be very wide indeed, and its ambit (or, to be more accurate, the ambit of its statutory predecessors) has been somewhat circumscribed by the courts. It is not surprising that the legislature and the courts have been content for the law to develop in this way. One of the principal purposes of section 660A is (save in certain circumstances - see e.g. section 660A(6)) to defeat arrangements between spouses, not conducted at arm's length, which seek to equalise their income, thereby reducing their aggregate liability to income tax and national insurance charges. The legislature has given effect to this by defining "settlement" in very wide terms, and the courts have then given the definition a limited effect, by means of the technique of purposive interpretation, through the introduction of the concept of "bounty" - see for instance per Lord Wilberforce in Inland Revenue Commissioners ***v*** *Plummer [1980] AC 896 912E-F."*

56. As to the issue of bounty, we adopted the approach of Sir Stephen Oliver QC in *Buck* and Lord Hoffman in *Jones* by asking whether the arrangement which existed was one which the Appellants would have entered into with someone at arm's length. We noted the correspondence from the Appellants' accountant to HMRC dated 14 September 2012, which conceded that dividend waivers by their nature are not arm's length. The correspondence went on to state that the Appellants *"wanted increased dividends to be paid to their spouses…"* We found as a fact that there was no commercial purpose for the waivers and that they would not have taken place at arm's length.

57. We did not find that the issue of distributable reserves was the conclusive factor on the issue of bounty and we noted that in *Buck* Sir Stephen Oliver QC considered the point after making a determination on the issue of bounty which corroborated our view that it was not, in isolation, conclusive. However, to the extent that it is relevant we preferred the evidence of HMRC on the matter. We noted that the figures exhibited within the bundle provided to us which demonstrated that the company only held sufficient reserves if the earlier years' waivers were taken into account, were taken from the company accounts and we accepted that they reflected the picture accurately. We took the view that to view the figures by ignoring previous waivers was artificial and that the cumulative effect of the arrangements should not be ignored. In those circumstances we found that there was a lack of sufficient distributable reserves within the company were it not for the Appellants waiving the dividends.

58. There was no challenge to HMRC's submission that sections 619 and 624 ITTOIA 2005 are satisfied on the basis that the income which arises from the dividend waiver arrangement clearly arises during the lives of the Appellants and the dividend income paid to their wives from their shares, together with the dividend

rights attached to them, are benefits enjoyed by the Appellants' wives. We were satisfied that they constitute property in which the Appellants have an interest by virtue of section 625 ITTOIA 2005 which treats the settlor as having retained an interest if the property from which the income arises may be payable to his spouse.

59. The argument that the Appellants' case falls within the exception found in section 626 ITTOIA 2005 was raised for the first time during the hearing. It was conceded by Mr Arthur that there was no evidence in support of the assertion by the Appellants that the share allotments were "gifts" and we found, in the absence of any such evidence, that we could not be satisfied that the exception applies to this case. However, even if we were to accept that there had been a gift of the shares, we were satisfied that the instant appeals still do not fall within the exception. In so deciding we had regard to *Jones* and we concluded that the case is distinguishable for the same reasons set out in *Buck*:

"The exemption in section 660A(6) did apply in Jones **v** *Garnett because, in contrast to the present situation, the essential arrangement identified in that case was the transfer of the share from the husband to the wife. It follows in my view that the present situation does not come within section 660A(6). There is no outright gift of property from which income arises."*

60. On the issue of the discovery assessments we did not accept that the lack of a witness giving oral evidence for HMRC made its case in any way deficient. The statutory test applicable to this case is whether there was information available upon which a hypothetical officer could reasonably have been expected to be aware of the insufficiency of the Appellants' self-assessment for the tax years 5 April 2008 and 5 April 2009. Live evidence would not have altered the test to be applied and we accepted the unchallenged submissions of Mr Hillier that there was no such information available as the Appellants' tax returns for each of those tax years and the two preceding years did not state that dividend waivers were executed, did not give the dividends voted and paid by the company nor details as to the Appellants' shareholdings. Furthermore there were no enquiries into the Appellants' tax returns for those tax years or the two preceding years which may have uncovered such information, nor did the Appellants inform an officer of the board about the details of the dividend waivers executed in those tax years. For those reasons we were satisfied that the discovery assessments were valid and in accordance with the legislation applicable.

61. The appeals are dismissed.

62. 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.

J. BLEWITT
TRIBUNAL JUDGE

RELEASE DATE: 20 January 2014