[2016] UKFTT 0188 (TC)

TC04974

Appeal number: TC/2015/02813

INCOME TAX – termination payment –availability of Foreign Service Deduction-events arising from 2008 financial crisis-whether new employer "successor" to previous employer-penalty for careless inaccuracy-professional advice taken-whether taxpayer should have done more-whether took reasonable care-penalties for late payment-payments on account

FIRST-TIER TRIBUNAL
TAX CHAMBER

JARETT GEDIR **Appellant**

- and -

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

TRIBUNAL: JUDGE MARILYN MCKEEVER
MR MICHAEL SHARP

Sitting in public at the Royal Courts of Justice in London on 10 February 2016

Mr Ashvin Degnarain, tax advisor for the Appellant

Mrs Lynne Gray, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. *Background*

2. This appeal arises out of the unprecedented events surrounding the 2008 global financial crisis. The Appellant, Mr Gedir was employed by Bear Stearns, the American investment bank, as the managing director of its European risk arbitrage business. In the turbulent period between March and August 2008, Bear Stearns was acquired by JP Morgan. Mr Gedir, received an offer from JP Morgan to continue in his previous role at that bank, which he accepted. For reasons which may never be entirely clear, Mr Gedir was informed that he would be moving to Goldman Sachs, instead of JP Morgan and Mr Gedir took up employment with Goldman Sachs on 1 September 2008. In 2010, Mr Gedir left Goldman Sachs and received a termination payment of £627,965, which he duly reported in his 2010/11 tax return.

3. Mr Gedir claimed Foreign Service relief in respect of the termination payment which significantly reduced the taxable amount. The "foreign service" related to the period when Mr Gedir had been employed by Bear Stearns and he would only be entitled to the relief if he could show first, that his employment with Goldman Sachs was connected with his employment with Bear Stearns and secondly that part of the termination payment was referable to his service with Bear Stearns.

4. HMRC opened an enquiry into Mr Gedir's 2010/11 tax return and concluded that Foreign Service relief was not due. HMRC raised an assessment for additional tax and charged penalties for an inaccurate return as well as late payment penalties in respect of the increased payments on account which should have been made in 2011/12.

5. Mr Gedir's appeal raises three issues:

- Whether a Foreign Service deduction is due on the termination payment from Goldman Sachs;
- Whether a penalty for a careless inaccuracy is due under Schedule 24 Finance Act 2007; and
- Whether late payment penalties under Schedule 56 Finance Act 2009 should be chargeable.

6. *The facts and evidence*

7. We considered the bundles of documents and authorities before us, the arguments of Mr Degnarain and Mrs Gray and the witness evidence given by the Appellant. We also considered written submissions made after the hearing.

8. Mr Gedir was non-UK resident until 16 April 2004 when he came to the UK to take up employment with Bear Stearns. He was resident but not ordinarily resident in the UK from then until 5 April 2007. From 6 April 2007 he was both resident and ordinary resident in the UK.

9. Mr Gedir worked in the European risk arbitrage business of Bear Stearns and became the managing director of that unit a few months before the crash.

10. Bear Stearns got into financial difficulties and in early 2008 various other banks were in negotiations, facilitated by the US Federal Reserve, to take over all or most of Bear Stearns. Mr Gedir gave evidence that executives from JP Morgan came onto the trading floor and engaged in discussions to identify those business units and individuals they wanted to join JP Morgan.

11. On 16 March 2008, Bear Stearns was sold to JP Morgan. The Appellant himself was engaged in discussions with Mr Lee Cook, who was at that time head of the European Equities division of JP Morgan, between March and May 2008, about the transfer of the risk arbitrage unit, regarded as a "jewel" and which members of the team to keep. These discussions took place face-to-face and by telephone and email. Mr Gedir said that he spoke to Mr Cook five or six times a day for a month, although there are no records of these discussions.

12. In the event, out of the Bear Stearns team of twelve, six were made redundant and the remaining six, including the Appellant, were offered employment with JP Morgan. Mr Gedir received an offer of employment from JP Morgan on 24 April. Although the acceptance on the copy we saw was not signed, Mr Gedir confirmed that he accepted the offer within the time limit. Mr Gedir considered it an attractive offer, although he had some concerns as JP Morgan already had a strong risk arbitrage team in place in their subsidiary, Cazenove.

13. The employment was not to commence until completion of the acquisition which took place on 2 July 2008. The offer letter referred to the proposed merger and stated "you will remain employed by your current Bear Stearns employing entity until further notice".

14. The letter provided for a basic salary and bonus and a "Special Retention Stock Grant". It stated "As a retained employee, on the day following the Merger Date [completion of the acquisition] …you will be granted a one-time award of JPMorgan Chase Restricted Stock Units…equal to your total performance year 2007 bonus." This represented compensation for the 2007 bonus to which the Appellant would have been entitled from Bear Stearns, but which he would not now receive. It amounted to $1.42million worth of JP Morgan stock.

15. Mr Gedir had meetings with senior management at JP Morgan to discuss strategy and at a "Town Hall" meeting for JP Morgan employees, it was publicly announced that Mr Gedir would, on the closing of the Bear Stearns acquisition, become the new head of JP Morgan's European Equity Special Solutions desk.

16. On 28 May 2008 Mr Gedir was shocked to receive an email from Mr Cook telling him that he would be joining Goldman Sachs, not JP Morgan. He was told to go to the HR department of Bear Stearns, which he did, and was given an employment contract with Goldman Sachs.

17. This contract appeared to be in a standard form; the only personalised elements being the Appellant's name and his job title and the compensation he was to receive. There was no reference to Bear Stearns and the contract was not conditional on the sale of Bear Stearns or on the acquisition by Goldman Sachs of any element of its business. Indeed the letter contained a term that the Appellant would not disclose terms of the compensation details to his current employer. The offer was on identical terms to the offer from JP Morgan and, in particular, Mr Gedir was to be offered the opportunity to receive a one-time award of $1.42million in the form of Restricted Stock Units in Goldman Sachs. Unlike the JP Morgan letter, this sum was not specifically identified with his 2007 bonus entitlement from Bear Stearns.

18. Mr Gedir accepted this offer. It is unclear whether the JP Morgan offer was withdrawn. In the interim period, Mr Gedir continued to be employed by Bear Sterns. He was employed by Bear Sterns until the end of August 2008, despite the fact that the merger was completed in July, and he received a final payment of salary from Bear Sterns on 20 August 2008.. He took up his employment with Goldman Sachs on 1 September 2008. Mr Gedir believed he was never employed by JP Morgan.

19. Mr Gedir emphasised that the situation at this time was extraordinary. No one knew quite what was happening and he was in shock. Whether or not the offer from JP Morgan was formally withdrawn, so far as he was concerned the only job on the table was the one with Goldman Sachs. He felt that he had no choice, or at least, only the choice between Goldman Sachs and unemployment.

20. It will probably never be known exactly what happened. The information is not in the public domain, but it appears that there were continuing negotiations behind the scenes as to the fate of Bear Stearns and various of its businesses. It was suggested that the way in which the company and its business units were ultimately sold, and to whom, was largely as a result of the intervention of the US Federal Reserve. Mr Degnarain quoted at length from two books which documented the fall of Bear Stearns: *Street Fighters: The Last 72 Hours of Bear Stearns, The Toughest Firm of Wall Street* (Kate Kelly 2010) and *House of Cards: A Tale of Hubris and Wretched Excess on Wall Street* (William Cohan) 2009). Mr Degnarain suggested that these books provided some background to the uncertain situation, the state intervention and the turmoil which led to Mr Gedir's team moving to Goldman Sachs rather than JP Morgan.

21. Whatever went on behind the scenes, Mr Gedir said that the whole of his business unit together with all the employees (who had not been made redundant) were transferred to Goldman Sachs and kept as a single unit. Mr Gedir understood that at least one of those who transferred had a similar deal to him, but he does not know about everyone.

22. We were informed that Bear Stearns' client list went with the employees, but we were not provided with any evidence as to what other elements of the "business unit" were transferred to Goldman Sachs.

23. The Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE) were not offered to the former Bear Stearns employees. Where they apply, the TUPE regulations ensure that an employee does not suffer a detriment on a change of his employment.

24. TUPE does not apply in every case where a business is taken over; there are a number of exceptions. It was not fully explained why TUPE was not offered in the present case although it may have been connected with an "Agreement and Release" which was a US document under which Mr Gedir released any claims or potential claims relating to his employment with Bear Stearns with the exception of some specified claims which did not include those he might have under TUPE.

25. Shortly after Mr Gedir commenced his employment with Goldman Sachs Lehman Brothers went bankrupt, triggering the global financial crisis. Risk arbitrage depends on the amount of merger and acquisition activity in the financial markets and following Lehman Brothers' collapse there was very little. This made it difficult for Mr Gedir to grow the business, which had been his initial brief, and he was unable to meet the performance targets which he had been set.

26. Mr Gedir believed that it was in the interests of both parties to agree appropriate terms for his departure. In May 2010 there were discussions between Goldman Sachs' legal department and Mr Gedir's lawyers about how he might be compensated for the loss of his employment including the loss of the Restricted Stock Units in Goldman Sachs, which Mr Gedir submitted had been awarded by reference to the loss of his Bear Stearns 2007 bonus.

27. The Appellant left Goldman Sachs on 10 August 2010. He received a termination payment of £627,965. £265,050 of this related to compensation for loss of his employment with Goldman Sachs. The balance represented half of the value of the Restricted Stock Units, the amount of which was equal to the amount of the 2007 Bear Stearns bonus. Mr Gedir was not entitled to receive anything in respect of the stock units as none of them had vested. The payment was made ex gratia.

28. The Appellant submitted his 2010/11 tax return on 29 January 2012. The tax return showed the termination payment of £627,965. He claimed the tax free exemption under section 403 of the Income Tax (Employment and Pensions) Act 2003 (ITEPA) and he also claimed a Foreign Service deduction under section 414 ITEPA OF £280,572 leaving a payment taxable under section 401 ITEPA of £317,393.

29. HMRC opened an enquiry into the return on 1 November 2012 under section 9A Taxes Management Act 1970. The enquiry focussed on the termination payment.

30. On 13 February 2015 HMRC issued a closure notice relation to the enquiry, stating that the Foreign Service deduction was not due and the tax return was amended accordingly. This increased the tax due by £140,286.

31. On 18 February 2015 HMRC issued a penalty assessment in relation to an inaccurate return. HMRC determined that the inaccuracy (the claim for Foreign

Service deduction which was not due) was a result of the failure of Mr Gedir to take reasonable care and charged a penalty of 16.5%, a sum of £23,147.19.

32. On 24 February HMRC issued a penalty assessment in relation to the late payments on account for the tax year 2011/12 arising from the increase in tax payable for 2010/11 in relation to the termination payment. This sum amounted to £6,003.

33. The Appellant's representative, Ocean Tax, appealed against the closure notice assessment on 23 February 2015 and the two penalty assessments on 4 March 2015.

34. HMRC sent a "view of the matter" letter to Mr Gedir on 12 March 2015 reiterating their original view and Mr Gedir appealed to the Tribunal on 11 April 2015.

35. It will be convenient to consider each of the three issues in turn. In each case, the burden of proof is on the Appellant to show, on the balance of probabilities that the assessments are excessive.

36. *Foreign Service deduction*

37. *The Law*

38. Ex gratia payments made on the termination of an employee's employment would not be subject to income tax were it not for the provisions of Chapter 3 of Part 6 of ITEPA. References below to section numbers are to sections of ITEPA unless otherwise stated.

39. Section 401 applies to "payments and other benefits which are received directly or indirectly in consideration or in consequence of, or otherwise in connection with—

(*a*) the termination of a person's employment, ...by the person…"

40. Section 403 ITEPA imposes the charge to tax: "The amount of a payment or benefit to which this Chapter applies counts as employment income of the employee or former employee for the relevant tax year if and to the extent that it exceeds the £30,000 threshold"

41. Section 404, which is crucial to the present case explains how the "£30,000 threshold" is to be calculated.

42. Subsection (1) provides:

"For the purpose of the £30,000 threshold in section 403(4) and (5), the payments and other benefits provided in respect of an employee or former employee which are to be aggregated are those provided—

(*a*) in respect of the same employment,

(*b*) in respect of different employments with the same employer, and

(*c*) in respect of employments with employers who are associated.

(2) For this purpose employers are "associated" if on a termination or change date—

(*a*) one of them is under the control of the other, or

(*b*) one of them is under the control of a third person who on that termination or change date or another such date controls or is under the control of the other.

(3) In subsection (2)—

(*a*) references to an employer, or to a person controlling or controlled by an employer, include the successors of the employer or person…"

43. The Foreign Service deduction is dealt with in sections 413 and 414 ITEPA.

44. They provide, so far as relevant:

"413 Exception in certain cases of foreign service

(1) This Chapter does not apply if the service of the employee or former employee in the employment in respect of which the payment or other benefit is received included foreign service comprising—

(*a*) three-quarters or more of the whole period of service ending with the date of the termination or change in question, or

(*b*) if the period of service ending with that date exceeded 10 years, the whole of the last 10 years, or

(*c*) if the period of service ending with that date exceeded 20 years, one-half or more of that period, including any 10 of the last 20 years.

(2) In subsection (1) "foreign service" means service to which subsection [(2A),][2] (3), (4) or (6) applies….

(3) This subsection applies to service in or after the tax year 2003–04 [but before the tax year 2013–14][2] such that—

[(*a*) any earnings from the employment would not be relevant earnings, or][1]

(*b*) a deduction equal to the whole amount of the earnings from the employment was or would have been allowable under Chapter 6 of Part 5 (deductions from seafarers' earnings).

[(3ZA) In subsection (2A)(*a*) "relevant earnings" means earnings for a tax year that are earnings to which section 15 applies and to which that section would apply even if the employee made a claim under section 809B of ITA 2007 (claim for remittance basis) for that year.][2]

[(3A) In subsection (3)(*a*) "relevant earnings" means—

…(*b*) for service before the tax year 2008–09, general earnings to which section 15 or 21 as originally enacted applies.]…

414 Reduction in other cases of foreign service

(1) This section applies if—

(*a*) the service of the employee or former employee in the employment in respect of which the payment or other benefit is received includes foreign service, and

(*b*) section 413 (exception in certain cases of foreign service) does not apply.

(2) The taxable person may claim relief in the form of a proportionate reduction of the amount that would otherwise count as employment income under this Chapter.

(3) The proportion is that which the length of the foreign service bears to the whole length of service in the employment before the date of the termination or change in question….(6) In this section "foreign service" has the same meaning as in section 413(2).

45. In Mr Gedir's case, "Foreign Service" simply means employment during a period when he was not ordinarily resident in the UK. That was the period from his

arrival in the UK up to 5 April 2007, which was during the period when he was employed by Bear Stearns.

46. *The Appellant's Contentions*

47. Mr Gedir accepts that he is not entitled to full relief under section 413 ITEPA but contends that he is entitled to partial relief, on a pro-rated basis under section 414.

48. In order for Mr Gedir to be entitled to the Foreign Service deduction, two conditions must be satisfied:

- First, Mr Gedir's employments with Bear Stearns and Goldman Sachs must be connected for the purposes of section 404 ITEPA, so that the payments in respect of both employments may be aggregated in applying the charging provisions and reliefs; and
- Secondly, "the service of [Mr Gedir] in the employment in respect of which the payment or other benefit is received includes foreign service". That is to say, the payment made by Goldman Sachs must, at least in part, be referable to his service with Bear Stearns, during which he was in "Foreign Service".

49. The Appellant has never sought to argue that Bear Stearns and Goldman Sachs are "associated" employers under section 404(1)(c) ITEPA, that is to say, employers who are "connected" with each other in being members of the same group of companies. The Appellant's argument turns on section 404(3)(a) which provides that "references to an employer…include the successors of the employer…". Neither the legislation nor case law defines "successor" in this context.

50. Mr Degnerain submitted that Goldman Sachs was the "successor" to Bear Stearns, so that together they constituted a single employer and the payment received from Goldman Sachs was a payment in respect of different employments with the same employer within section 404(1)(b).

51. Further, Mr Degnerain argued that the element of the termination payment which was calculated by reference to the Restricted Stock Units in Goldman Sachs related back to the 2007 Bear Stearns bonus so that the payment was in respect of the Bear Stearns part of the employment with the single employer, and that employment included Foreign Service within section 414.

52. The Availability of the Foreign Service deduction turns on whether Goldman Sachs was the "successor" to Bear Stearns for the purposes of section 404. As the term is not defined, it should be given its ordinary meaning. Mr Degnerain submits that, in its ordinary meaning, a person is an "employer" if they are that party to the contract of service who first offered employment to and who first entered into the contract with the employee. The successor is therefore, any person who subsequently becomes a party to a contract of service and so stands in the shoes of the original employer. "Successor" (and hence an employer) is not defined anywhere in the Tax Acts and so the ordinary meaning is assumed to apply, being someone who follows another or comes in the place of another person to perform a like role and duties.

53. Mr Degnarain argues that as a result of the intervention of the US Federal Reserve, the whole of Mr Gedir's business unit at Bear Stearns was transferred to Goldman Sachs who accordingly "stood in the shoes" of Bear Stearns as employer, in the same way that JP Morgan would have done, had it acquired this business unit as originally planned.

54. *The Respondent's submissions*

55. Mrs Grey referred to the guidance contained in HMRC's Employment Income Manual at paragraphs 13690 and 13975 which set out HMRC's view on when the Foreign Service deduction applies. After setting out the definition of Foreign Service, paragraph 13690 states "For this purpose treat successive employments with different members of the same group of companies as if there were a single, continuing employment where the payment takes account of that service". Paragraph 13975 sets out an example where an individual is employed by one member of a group of companies and subsequently by another member of the group. Where the termination payment reflects the employee's whole service with both companies, the period of employment with both companies is aggregated in considering whether the Foreign Service deduction applies. If the termination payment represents compensation only for the loss of the second employment, only the period of employment with the second company is taken into account.

56. Mrs Grey took us through the provisions concerning when companies are connected with each other by virtue of control relationships and when they are members of the same group. We will not rehearse that here, as the Appellant has always accepted that Bear Stearns and Goldman Sachs were never members of the same group.

57. HMRC did not consider that there was any association between the two employers. Mrs Grey pointed to the fact that the JP Morgan contract specifically referred to the merger of Bear Stearns and JP Morgan. The Goldman Sachs contract did not. The 2007 Bear Stearns bonus was specifically referenced in the award of $1.42million in Restricted Stock Units by JP Morgan. The award of an equivalent amount by Goldman Sachs did not refer to Bear Stearns. TUPE was not offered in relation to Mr Gedir and his team's move to Goldman Sachs. The Compromise Agreement with Goldman Sachs under which the termination payment was made did not refer to Bear Stearns.

58. HMRC's view is that Mr Gedir chose to take up an employment with an unconnected company. The fact that the terms of the Goldman Sachs employment were identical to those of the JP Morgan employment, including an award of $1.42million worth of Restricted Stock Units is not evidence of continuous employment. It is not unusual for a company to "headhunt" an individual or a team and to match or exceed the offer made by the existing employer or another prospective employer in order to win the people they want.

59. Mr Gedir's employment with Goldman Sachs was not an employment with a company in the same group as Bear Stearns and was not otherwise continuous with it.

The Goldman Sachs employment was a stand-alone employment and Mr Gedir was resident and ordinarily resident throughout that employment, so there was no Foreign Service in that employment and the deduction is not due.

60. *Discussion*

61. The application of the Foreign Service deduction is clear where an employee has successive employments with companies in the same group. However, not all employers are corporate and not all transfers of businesses involve the acquisition of a company. It is to cover these situations that section 404 provides for "successors".

62. As there is no statutory definition of "successors", we agree that we must apply the ordinary meaning of the word, but construing it in the context of the legislation. We consider that chapter 3 of part 6 of ITEPA is intended to operate either in circumstances where an employee is employed by different members of the same group of companies, where there is an overarching common ownership or where there is a continuity in the existence of a business entity on a change of ownership.

63. For example, where one partnership merges with another and the combined entity carries on the business of both the original partnerships, we consider that the merged partnership would be the "successor" to each of the component partnerships. Similarly where an unincorporated business is acquired by a company or another unincorporated business and the enterprises are combined, the acquirer would be the "successor". Or where one element of a larger business is transferred lock, stock and barrel to a new owner and continues to be run as a discrete business one could say that the new owner is the successor to the old.

64. The common theme in these situations is that the business or part of the business is transferred as a whole and continues to operate as a business or is combined with another business, albeit with a different owner. We consider that the key element is the continuation of the whole business or a discrete part of a business whether or not in combination with another business. It is not sufficient that all the employees are transferred, even if they take their clients or customers with them. That is not the transfer of the enterprise itself, but only some components of it.

65. We consider that the circumstances in which the TUPE regulations can apply (whether or not they do in fact apply) encapsulates this concept.

66. Regulation 3 provides that TUPE applies to "a transfer of an undertaking, business or part of an undertaking or business…to another person where there is a transfer of an economic entity which retains its identity". "Economic entity" is defined as "an organised grouping of resources which has the objective of pursuing an economic activity…". We do not think that the undertaking or business must necessarily continue to retain its identity following transfer. A merger of undertakings which creates a new, larger, business would in our view qualify, but the transfer must be of an identifiable "economic entity".

67. Applying this test, we have not been provided with sufficient evidence that the risk arbitrage "business unit" of Bear Stearns was transferred as an identifiable

economic entity to Golman Sachs. Clearly some of the components of that entity were transferred; the employees (or at least those who did not lose their job) and the client lists, but we do not consider that that is sufficient to constitute Goldman Sachs as the "successor" to Bear Stearns for the purpose of the Foreign Service provisions.

68. We recognise Mr Gedir's difficulty in providing evidence in relation to what actually happened, why Goldman Sachs acquired the risk arbitrage business after it had been announced that Mr Gedir would be heading up that business at JP Morgan and what it was exactly that Goldman Sachs acquired. Those were turbulent times and we can well believe there was much activity going on behind the scenes which we do not know about. Having said that, the burden of proof is on Mr Gedir to provide evidence to support his case that Goldman Sachs was the successor to Bear Stearns, on the balance of probabilities, and he has been unable to discharge that burden.

69. Accordingly, we find that the Foreign Service deduction is not due in respect of Mr Gedir's termination payment.

70. Even if we are wrong about this, we do not consider that there is sufficient evidence to find that the Restricted Stock Unit element of the termination payment related to Mr Gedir's employment with Bear Stearns as opposed to representing an element of the compensation for the loss of his employment with Goldman Sachs.

71. *Penalty for inaccurate return*

72. *The law*

73. In this part of the decision, references to paragraph numbers are to paragraphs in Schedule 24 Finance Act 2007 which sets out the penalties for submitting inaccurate documents to HMRC.

74. Paragraph 1 provides:

"Error in taxpayer's document

1—

(1) A penalty is payable by a person (P) where—

(*a*) P gives HMRC a document of a kind listed in the Table below, and

(*b*) Conditions 1 and 2 are satisfied.

(2) Condition 1 is that the document contains an inaccuracy which amounts to, or leads to—

(*a*) an understatement of [a][1] liability to tax,…

(3) Condition 2 is that the inaccuracy was [careless (within the meaning of paragraph 3) or deliberate on P's part][1].”

75. A personal self-assessment tax return is one of the documents listed in the Table referred to in paragraph 1.

76. Different penalties are payable depending on the degree of culpability.

Paragraph 3 provides that “(1) [For the purposes of a penalty under paragraph 1, inaccuracy in][1] a document given by P to HMRC is—

(*a*) “careless” if the inaccuracy is due to failure by P to take reasonable care,…”

77. Paragraph 4 provides that the standard penalty for a careless action is 30% of the “potential lost revenue”

78. Paragraph 5 provides that “(1) “The potential lost revenue” in respect of an inaccuracy in a document [(including an inaccuracy attributable to a supply of false information or withholding of information)][1] or a failure to notify an under-assessment is the additional amount due or payable in respect of tax as a result of correcting the inaccuracy or assessment.”

79. Paragraphs 9 and 10 provide for the mitigation of the penalty where the taxpayer cooperates with HMRC in relation to the underpaid tax. They provide:

“9(1) A person discloses an inaccuracy[, a supply of false information or withholding of information,][1] or a failure to disclose an under-assessment by—

(*a*) telling HMRC about it,

(*b*) giving HMRC reasonable help in quantifying the inaccuracy[, the inaccuracy attributable to the [supply of false information][2] or withholding of information, or the][1] under-assessment, and

(*c*) allowing HMRC access to records for the purpose of ensuring that the inaccuracy[, the inaccuracy attributable to the [supply of false information][2] or withholding of information, or the][1] under-assessment is fully corrected.

(2) Disclosure—

(*a*) is "unprompted" if made at a time when the person making it has no reason to believe that HMRC have discovered or are about to discover the inaccuracy[, the supply of false information or withholding of information, or the under-assessment][1], and

(*b*) otherwise, is "prompted".

(3) In relation to disclosure "quality" includes timing, nature and extent.

10(1) If a person who would otherwise be liable to a penalty of a percentage shown in column 1 of the Table (a "standard percentage") has made a disclosure, HMRC must reduce the standard percentage to one that reflects the quality of the disclosure.

(2) But the standard percentage may not be reduced to a percentage that is below the minimum shown for it—

(*a*) in the case of a prompted disclosure, in column 2 of the Table, and

(*b*) in the case of an unprompted disclosure, in column 3 of the Table."

80. The table so far as relevant is set out below.

Standard %	*Minimum % for prompted disclosure*	*Minimum % for unprompted disclosure*
30%	15%	0%

81. On the basis that Foreign Service Deduction was not available, Mr Gedir had made an inaccurate return and HMRC assessed the additional tax due of £140,286. HMRC contended that the inaccuracy was due to Mr Gedir's failure to take reasonable care. The disclosure was prompted as it was given after the enquiry had commenced. They reduced the standard penalty of 30% to 16.5% to take account of Mr Gedir's co-operation. The reduction was a maximum of 30% for "telling" HMRC, 35% (out of a maximum of 40%) for "helping" HMRC understand it and 25% (out of a maximum of 30%) for "giving" HMRC access to records.

82. HMRC applied the total disclosure reduction of 90% to the difference between the minimum and maximum percentages (15% and 30%) ie 15%. 90% of 15% is 13.5% so the maximum penalty of 30% is reduced by 13.5% giving a penalty rate of 16.5%. The penalty chargeable, 16.5% of the £140,286 additional tax was £23,147.19.

83. Under paragraph 15, the taxpayer can appeal against HMRC's decision that a penalty is payable and /or as to the amount of the penalty. Under paragraph 17, the tribunal may affirm or cancel HMRC's decision that a penalty is payable and /or substitute for HMRC's decision about the amount of the penalty another decision that HMRC had power to make.

84. *The Appellant's contentions*

85. In the first place, the Appellant contends that no penalty can be due because there was no inaccuracy in the return: Mr Gedir was entitled to the Foreign Service deduction.

86. If there was an error, then no penalty should be due because Mr Gedir took reasonable care in submitting his tax return.

87. Mr Degnarain pointed to the length of time and extent of the correspondence before HMRC raised the assessment. If the matter were straightforward, he would have expected there to be a decision on the "successor" point much sooner.

88. Mr Degnarain had a telephone conversation with Mr Wright of HMRC on 11 February 2014. There was some dispute as to what was said. Mr Degnarain's note of the conversation stated "Mr Wright acknowledged that our evidence provides some support of Mr Gedir's continuous employment but his situation is unusual and unprecedented. …Mr Wright said that he had been referring Mr Gedir's case to a HMRC specialist team, their decision could go either way and ultimately it was not down to him because he does not have the expertise…".

89. Mr Degnarain quoted this in his letter to Mr Wright of 20 February 2014 in response to Mr Wright's letter of 14 February which said that his colleague who provided specialist advice was supportive of his, Mr Wright's, position that Foreign Service relief is not due.

90. In his letter of 20 March 2014, Mr Wright denied he had said that "the decision could go either way" but that he had agreed that they should await the view of his specialist colleague.

91. Mr Wright also said he did not say Mr Gedir's situation was "unusual and unprecedented". The letter states "What I did say was that I referred the issue for specialist advice because of its unusual nature. To clarify, I do not consider that Mr Gedir's situation was unusual . It is quite normal to see individuals leaving one employment for another, only to see that second employment terminated at some point in the future…What is unusual is Mr Gedir's claim to Foreign Service relief which is based on one employment with two non-associated employers."

92. There was further correspondence and in a letter dated 26 June Mr Wright acknowledged that he and Mr Degnarain had different views about the correct treatment of Mr Gedir's foreign service deduction and suggested that before he formally amended Mr Gedir's return (giving him the right of appeal to the tribunal) they consider Alternative Dispute Resolution (ADR). He asked some further

questions about what happened when Goldman Sachs took on the business unit from Bear Stearns. Mr Degnarain replied that he agreed ADR would be appropriate but submitted he had already replied to HMRC queries and it would be better to discuss matters directly with the ADR colleagues and answer any additional questions at that point. Mr Degnarain asserted that the dispute relates to an interpretation of the law.

93. Mrs Dixon of the ADR team confirmed HMRC'S view that there was no evidence that Mr Gedir's employments with Bear Stearns and Goldman Sachs were continuous. In Mr Wright's "state of the matter" letter of 12 March 2015, it was stated "Mr Degnarain said that he understood that the legislation does not allow the relief in [Mr Gedir's] circumstances but felt that the spirit of the legislation was such that it should." Mr Degnarain said that it was Mrs Dixon who had referred to the spirit of the legislation. His view was that the meaning of "successor" in section 404 ITEPA was a grey area, which had not hitherto been clarified and that on his interpretation of the legislation, Goldman Sachs was the successor to Bear Stearns and Mr Gedir was entitled to the Foreign Service deduction.

94. In summary, Mr Degnarain submits that the application of the legislation to Mr Gedir's circumstances was unclear, but that it was a tenable position to interpret the legislation as permitting the Foreign Service deduction and he so advised Mr Gedir.

95. Mr Gedir gave evidence that before the 2010/11 tax year, he completed his own tax returns. He felt that he needed professional advice in that year because his affairs had become more complex with the change in his employer and the position with the unvested stock to which he was entitled. Ocean Tax Limited were his wife's tax advisors and she recommended that he seek advice from them.

96. Mr Gedir had a meeting with his advisor from Ocean Tax in December 2011 and provided him with P60 forms from Goldman Sachs and his new employer, UBS, his Goldman Sachs payslips, the Compromise Agreement with Goldman Sachs, his employment contract with Goldman Sachs, the offer letters from both JP Morgan and Goldman Sachs and the equity/stock awards from both JP Morgan and Goldman Sachs.

97. Mr Gedir's advisor was a member of the Chartered Institute of Taxation with significant experience in the field of employment tax. Mr Gedir had no reason to doubt his advisor's competence or the quality of his advice.

98. Mr Gedir was aware of the existence of Foreign Service deduction as he had colleagues from all over the world. He believed that he might have suggested the possibility of a claim to his advisor. Ocean Tax carried out some research but were unable to find any case law on the matter. Whilst his advisor acknowledged the uncertainty of the position, having discussed the circumstances of how Mr Gedir came to be employed by Goldman Sachs, he was of the view that one could interpret the legislation to regard Goldman Sachs as the successor employer to Bear Stearns. Accordingly, he advised Mr Gedir that he could properly claim the Foreign Service deduction in his tax return.

99. Mr Gedir carrie out some informal checks of this advice. He reviewed the legislation which Ocean Tax had shown him and he acknowledged that it was not clear. He also asked around some of his colleagues and was told that some of them had filed their tax returns on the basis that the relief was available. He believed that he had a proper basis on which to make the claim.

100. Mr Degnarain submitted that Mr Gedir had acted reasonably in submitting his tax return on this basis and had not failed to take reasonable care.

101. In support of this, he drew our attention to the case of *J R Hanson v HMRC* [2012] UKFTT 314 which related to the application of Schedule 24 Finance Act 2007 in relation to capital gains tax and whether the taxpayer had taken reasonable care to avoid inaccuracy where he had relied on an agent.

102. The Tribunal considered what a taxpayer had to do to be considered as taking reasonable care. It said the following:

"15 Paragraph 18 [Finance Act 2007] deals with the liability of a taxpayer to penalties under the schedule where agents are acting on behalf of the taxpayer. It provides as follows in so far as relevant:
"(1) P is liable under paragraph 1(1)(a) where a document which contains a careless inaccuracy (within the meaning of paragraph 3) is given to HMRC on P's behalf.
…
(3) Despite sub-paragraphs (1) and (2), P is not liable to a penalty under paragraph 1 or 2 in respect of anything done or omitted by P's agent where P satisfies HMRC that P took reasonable care to avoid inaccuracy (in relation to paragraph 1)…"…

18 Paragraph 18 is specifically dealing with the reasonableness of reliance on a third party agent whose act or omission causes an inaccuracy in a return. It is plainly directed towards those professional advisers who assist taxpayers in completing their tax returns and documents associated therewith. …
19 In my view carelessness can be equated with "negligent conduct" in the context of discovery assessments under section 29 Taxes Management Act 1970 . In that context, negligent conduct is to be judged by reference to the reasonable taxpayer. The test was described by Judge Berner in *Anderson (deceased) v Revenue and Customs Commissioners* [2009] UKFTT 206 at [22], cited with approval by the *Upper Tribunal in Colin Moore v Revenue and Customs Commissioners [2011] UKUT 239 (TCC)* :
"The test to be applied, in my view, is to consider what a reasonable taxpayer, exercising reasonable diligence in the completion and submission of the return, would have done."
20 I am satisfied that the effect of *paragraph 18* is to remove the liability of a taxpayer to a penalty where:

- (1) a return is completed and lodged by an agent, and
- (2) an inaccuracy in the return is the result of something done or omitted by the agent, but
- (3) the taxpayer took reasonable care to avoid that inaccuracy.

21 What is reasonable care in any particular case will depend on all the circumstances. …. In my view, if a taxpayer reasonably relies on a reputable accountant for advice in relation to the content of his tax return then he will not be liable to a penalty under Schedule 24 .

22 I am fortified in these conclusions in relation to *paragraph 18* by the content of the HMRC Compliance Handbook at CH84540 which states in relation to paragraph 18 as follows:

"A person cannot simply appoint an agent and deny responsibility for their tax affairs. The person still has a duty to take reasonable care, within their ability and competence, to make sure that what they are signing for is correct. The person has to show that they took reasonable care, within their ability and competence, to avoid default by their agent. This will include

• making sure that they give the agent all relevant information with which to work …
• implementing the professional advice received, and not neglecting some vital step
• checking the agent's work to the extent that the person is able to do so. For example, an ordinary person cannot be expected to challenge specialist professional advice on a complex legal point. But they ought to be able to recognise the complete absence of a major transaction….

The benchmark is a person who goes to an apparently competent professional adviser

• gives the adviser a full and accurate set of facts
• checks the adviser's work or advice to the best of their ability and competence and
• adopts it.

The person will then have taken reasonable care to avoid inaccuracy on the part of themselves and their agent."

23 … At the other extreme an error might involve wrongly construing a complex piece of legislation. In those circumstances the possibility of a penalty may still arise because of the carelessness of the agent, but the taxpayer's liability to a penalty might well be excluded on the basis that he took reasonable care but did not identify the error.

24 I agree with the general thrust of the guidance given in the HMRC Compliance Handbook. In particular that a taxpayer cannot simply leave everything to his agent. A taxpayer must certainly satisfy himself that the agent has not made any obvious error. That might involve the taxpayer seeking to understand the basis upon which an entry on his return has been made by the agent. However in matters that would not be straightforward to a reasonable taxpayer and where advice from an agent has been sought which is ostensibly within the agent's area of competence, the taxpayer is entitled to rely upon that advice."

103. Mr Degnarain submitted that Mr Gedir had done all that a reasonable taxpayer could be expected to do in accordance with the above principles . He had engaged a competent and reputable professional advisor, he provided his advisor with a full and accurate set of facts, he relied on his advisor to identify the correct technical position in relation to a complex piece of legislation, he checked the adviser's advice to the best of his ability and he adopted it. Whilst it was acknowledged that the technical position was not clear, the advisor advised that the Foreign Service deduction could properly be claimed and Mr Gedir did what he could to check that there was no obvious error.

104.Taking account of all the circumstances, Mr Degnarain submits that Mr Gedir was entitled to rely on Ocean Tax to prepare an accurate tax return and accordingly took reasonable care to avoid an inaccuracy in his 2010/11 tax return.

105.In relation to the reduction in the penalty (if the penalty should be found to be due) Mr Degnerain submits that Mr Gedir should be entitled to the full reductions of 40% and 30% respectively for helping HMRC understand and giving access to records.

106.Mr Gedir has been fully co-operative throughout the course of the enquiry. He maintained accurate records and supplied HMRC with all the documents in his possession that they requested. In particular, he should be entitled to the full reduction for "helping" because he explained the payment of £265,050 in a letter sent to HMRC on 9 January 2013 which reconciled this sum to the figure in his compromise agreement. He should be entitled to the full reduction for "giving access" because he demonstrated that the termination payments included compensation for the period when he was employed by Bear Stearns, in a letter dated 31 October 2014.

107.*HMRC's contentions*

108.HMRC contend that Mr Gedir was careless as he failed to take reasonable care. Although Mr Gedir sought advice from his advisor, HMRC contend that this is not enough and there is still a requirement on Mr Gedir to consider the advice received and exercise reasonable diligence in agreeing the return submitted to HMRC.

109.HMRC said that the definition of carelessness or negligence was set out in the case of *Blyth v Birmingham Waterworks Co* (1856) 11ER 781. Alderson B said "Negligence is the omission to do something which a reasonable man, guided upon those considerations which ordinarily regulate the conduct of human affairs, would do, or doing something which a prudent and reasonable man would not do. The defendants might have been liable for negligence, if, unintentionally, they omitted to do that which a reasonable person would have done, or did that which a person taking reasonable precautions would not have done."

110.HMRC contend that Mr Gedir was negligent or careless according to this test.

111.Although Mr Gedir spoke to a tax advisor, he agreed that it was a grey area. It was an unusual and untested situation and there were no cases on the point. Mrs Gray submitted that in these circumstances the reasonable man would have taken further professional advice as to whether he had a valid claim and might seek the advice of HMRC before filing his tax return. Mr Gedir made some informal checks but did not take any further advice. Mrs Gray considered that he should have carried out further due diligence and so was careless. The penalty for careless inaccuracy was therefore properly assessed.

112.As to quantum, HMRC contend that Mr Gedir was not entitled to the full reduction of 40% of the penalty for helping HMRC to understand as he did not help HMRC to understand how the compensation payment of £265,050 was arrived at.

That is to say, he did not explain how that figure was arrived at and what was included in the compensation.

113. Nor was he entitled to the full deduction of 30% for giving HMRC access to records as evidence to show the payments included compensation for the period Mr Gedir was employed by Bear Stearns was never provided.

114. *Discussion*

115. We have quoted at length from the tribunal decision in the *Hanson* case, and we consider that this sets out the correct test for establishing whether a taxpayer who uses an agent to complete his tax return has taken reasonable care to avoid an inaccuracy in the return. The essential elements are:

- The taxpayer consulted an advisor he reasonably believed to be competent ;
- He provided the advisor with the relevant information and documents;
- He checked the advisor's work to the extent that he was able to do so; and
- He implemented the advice.

116. The passages quoted above, including the guidance in the HMRC manual, recognise that the taxpayer cannot necessarily be expected to identify an error by the advisor in relation to complex legal points.

117. What of the related, but different, point which arises in this case where a particular piece of legislation is open to different interpretations and there is no authority on the point and/or where the application of the legislation is uncertain?

118. HMRC contend that a taxpayer in this situation must take further advice from another advisor or from HMRC themselves if they are to be regarded as having taken reasonable care.

119. It is, unfortunately, far from unusual for a particular piece of tax legislation to contain a "grey area". It is commonplace for there to be more than one tenable interpretation of a provision or its application and for an advisor to "take a view" as to which interpretation should be adopted. That will generally be the interpretation which is most favourable to the taxpayer. It may be acknowledged that that interpretation is not beyond challenge, but provided the view is a reasonable one, the advisor is entitled to take it and to advise the taxpayer on that basis and the taxpayer is entitled to rely on that advice.

120. A taxpayer who consults an advisor he reasonably believes to be competent and experienced in the relevant field, and who is advised that his tax return may properly be completed on the basis of a particular view of the legislation, would normally be regarded as having taken reasonable care to submit an accurate return, even if he understood that there were other possible interpretations of that legislation. This would not be the case if the taxpayer should have realised that the return had been completed on the basis of a view that was obviously untenable,

121. We do not consider that a taxpayer is obliged to take advice from another advisor in this situation. Where there is scope for different views about a provision, there is no guarantee that another advisor's opinion will be the "correct" interpretation. We are, by definition, considering a situation where there is uncertainty which may ultimately need to be resolved by the tribunals or the courts; different people may well take different views, all of which are tenable.

122. Nor is a taxpayer obliged to seek advice from HMRC. There may be occasions when it is helpful to ascertain HMRC's view on a particular provision, but the taxpayer does not necessarily have to agree with it! In a case where a range of views are possible, HMRC would be expected, and entitled, to take the view which is most advantageous to it in the same way as the taxpayer would be expected, and entitled, to take the view which is most in his favour.

123. Although Mr Gedir had previously completed his tax returns himself, he recognised that his affairs were more complex in 2010/11 and decided to take professional advice, to make sure he got things right. He took the advice of advisors he reasonably believed to be competent and experienced in the field of employment tax. He provided them with the relevant information. He discussed the question of Foreign Service relief with Ocean Tax. He was advised that the legal meaning of "successor" was uncertain, but in the unusual circumstances in which he had come to be working for Goldman Sachs, one could properly argue that Goldman Sachs was the successor to Bear Stearns and that the Foreign Service deduction could properly be claimed. Mr Gedir adopted that advice.

124. In these circumstances, we consider that Mr Gedir took reasonable care to avoid an inaccuracy in his self-assessment tax return for 2010/11.

125. If the penalties were due, we would not seek to alter the reduction determined by HMRC.

126. *The late payment penalties*

127. At the hearing, HMRC contended that late payment penalties were due under schedule 56 Finance Act 2009 on the basis that

- Foreign Service relief was not due
- Therefore more tax should have been paid in 2010/11
- As a result, more tax should have been paid on account of the tax year 2011/12
- That increased payments on account had not been paid
- Therefore late payment penalties were due.

128. Mr Degnerain contended that as Foreign Service relief was due, there had been no late payment of the payments on account. In any event he did not accept that the penalties could be charged even if the relief was not due.

129. It was agreed that further written submissions would be made after the hearing.

130.Having reconsidered the issue, HMRC determined that they would no longer be charging the late payment penalties and agreed to cancel the late payment penalties of £6,003 in relation to the year ended 2012. We do not therefore need to consider this matter further.

131.*Decision*

132.For the reasons set out above we make the following decisions.

133.Mr Gedir was not entitled to the Foreign Service deduction in respect of the termination payment received in 2010/11 and accordingly the assessment dated 13 February 2015 shall stand good.

134. Mr Gedir took reasonable care to avoid an inaccuracy in his self-assessment tax return for 2010/11 and accordingly we allow the appeal against the penalty for careless inaccuracy and cancel the penalty.

135.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.

TRIBUNAL JUDGE
MARILYN MCKEEVER

RELEASE DATE: 15 MARCH 2016