



**TC05901**

**Appeal number: TC/2016/07331**

*Procedure – application for stay pending enquiry and expected proceedings relating to partnership of which appellant a former partner – stay granted for six months – application for allocation to complex category – application granted*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**ANDREY BADZYAN**

**Appellant**

**- and -**

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

**Respondents**

**TRIBUNAL: JUDGE THOMAS SCOTT**

**Sitting in public at The Royal Courts of Justice, Strand, London WC2 on  
11 April 2017**

**Andrew Gotch, CTA (Fellow), for the Appellant**

**Patrick Boch of HM Revenue and Customs Solicitor's Office for the  
Respondents**

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## DECISION

### *Introduction*

1. HMRC applied to stay Mr Badzyan's appeal against an assessment to income tax for 2011-2012 and against the issue by HMRC of information notices to Mr Badzyan.
2. HMRC also applied to re-allocate Mr Badzyan's proceedings to the "complex" category under the Tribunal Rules.
3. Mr Badzyan opposed both applications.

### *Background*

4. During the tax year 2011-12 Mr Badzyan was a member of a UK limited liability partnership, HFFX LLP (the "Partnership").
5. One of the partners in the Partnership was a corporate member. For 2011-12, the corporate member received a large portion of the partnership's profits. The corporate member would pay corporation tax on these profits, invest them, and then pay them to individual partners, such as Mr Badzyan, as "special capital". The payments by the corporate member to the individual partners would be made in tranches, spread over three years.
6. The partnership claims that the "special capital" payments are either capital in nature or a gift, and are therefore not taxable when received by the individual partners. The aim was that the profits would effectively be taxable only at the corporation tax rate and not at the rate of income tax that would have been payable had the individuals received partnership profits directly.
7. HMRC contest this tax analysis. They raise various arguments, including that the arrangements are a pre-arranged tax avoidance scheme, and/or that the corporate member was a mere conduit for the distribution of profits to individual members such as Mr Badzyan.
8. Mr Badzyan resigned from the Partnership shortly before he was due to receive his first tranche of "special capital" from the corporate member. The Partnership recommended to the corporate member that by so resigning Mr Badzyan should forfeit his "special capital" payment. The corporate member followed this recommendation.
9. On 22 March 2016 HMRC issued a discovery assessment on the Partnership for 2011-12. They also opened enquiries in respect of the accounting periods following 2011-12, of direct relevance to individual partners other than Mr Badzyan. The Partnership has appealed to HMRC against the 2011-12 assessment.
10. HMRC's view is that the discovery assessment which they have issued on the Partnership would enable them to make a consequential amendment to Mr Badzyan's tax return for 2011-12 pursuant to section 30B(2) of the Taxes Management Act 1970 ("TMA"). The Partnership contests this analysis. HMRC has therefore issued a separate discovery assessment on Mr Badzyan, on 31 March 2015. Mr Badzyan has appealed against that assessment.

### *Application to Stay*

11. Under the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009, the Tribunal has certain case management powers. In particular, and without restricting its general case management powers, under Rule 5(3)(j) the Tribunal may stay proceedings. In deciding whether to do so, the Tribunal must have regard to the overriding objective. This includes dealing with the case in ways which are proportionate to its importance, the complexity of the issues, the anticipated costs and the resources of the parties, and “avoiding delay, so far as compatible with proper consideration of the issues”.
12. The approach to be adopted in deciding whether to stay proceedings is that set out by Judge Berner in *Coast Telecom Limited v HMRC* [2012] UK FTT 307 (TC), where he stated, at paragraph 5:

“I start by reminding myself of the proper approach to the adopted in considering whether to grant a stay in the absence of agreement between the parties. Although neither party referred to it, I consider that the correct approach is to be derived from *Revenue and Customs Commissioners v RBS Deutschland Holdings GmbH* [2007] STC 814 where the Court of Session as the Court of Exchequer in Scotland held (at [22]) that a tribunal or court might sist, or stay, proceedings against the wish of a party if it considers that a decision in another court would be of material assistance (not necessarily determinative) in resolving issues before the tribunal or court in question, and that it is expedient to do so.”
13. In this application, the other decision which might arguably be of “material assistance” in determining Mr Badzyan’s appeal is an appeal by the Partnership against the 2011-12 assessment on it. Such an appeal has not yet been filed with the Tribunal, as HMRC enquiries are continuing. HMRC state that they expect to uphold the Partnership’s assessment on review, and that the Partnership will appeal that decision.
14. HMRC’s substantive arguments that the arrangements do not achieve their desired effect for tax purposes are as follows:
  - (a) For the purposes of section 850(2) of the Income Tax (Trading and Other Income) Act 2005, the profits allocated to the corporate member should be treated as having been allocated to the individual partners because the corporate partner does not have a genuine right to the profits.
  - (b) It follows from this analysis that individual partners are therefore taxable on those profits as a matter of partnership tax law in the year in which the profits arise, even though the profits are not paid as “special capital” until later years, or not paid at all if forfeited.
  - (c) Alternatively, the subsequent allocations to the individual partners of “special capital” are taxable on allocation because they are in reality remuneration forming part of an incentive plan.
  - (d) If, alternatively, the payments to individual partners are found to be genuine capital sums, then Chapter 4 (Sales of Occupation Income) of Part 13 of the Income Tax Act 2007 (“ITA 2007”) applies to render the “special capital” payments taxable.
15. HMRC raises three arguments in support of its application to stay the proceedings in Mr Badzyan’s appeal.

16. The first HMRC argument is that litigation against the Partnership would be more appropriate and efficient than litigation against Mr Badzyan. They submit that litigating the same issues in parallel proceedings would not be dealing with the case in a way that is “proportionate” within the overriding objective. That is because parallel litigation would entail HMRC and the Tribunal using considerable resources unnecessarily. HMRC argues that the case against Mr Badzyan raises the same factual and legal issues as the case against the Partnership, namely whether the individual partners are subject to tax on the monies paid to the corporate member and, if so, whether they are liable at the time the profits are declared and paid to the corporate member, or at the time when the “special capital” is allocated to the individual partners. With parallel cases, the same witnesses could be called to give evidence twice and two different tribunals could give different answers to the same questions.
17. In support of this argument, HMRC point out that under the TMA the approach is that partnership tax affairs are dealt with by the partnership and not individual partners. In the present case, they argue, issues such as whether “the main object. . . of the transactions or arrangements is the avoidance or reduction of liability to income tax” (section 773(2) ITA 2007) can only properly be resolved at the partnership level. The Partnership is the entity which will have the requisite information and documents about the relevant transaction.
18. HMRC’s second argument in favour of a stay is that in view of the uncertainty regarding the interpretation of section 30B(2) TMA they cannot prudently withdraw the discovery assessment against Mr Badzyan. If the Tribunal eventually accepts the Partnership’s interpretation of section 30B, HMRC will have to seek to recover tax from each individual partner. This means that they cannot withdraw any of the assessments, including the one issued against Mr Badzyan.
19. HMRC’s third argument is that the balance of convenience supports a stay of proceedings. By this they mean that, although a stay might result in uncertainty and inconvenience to Mr Badzyan personally, that concern is outweighed by the issues raised by their first two arguments.
20. For Mr Badzyan, Mr Gotch argues that treating his case as a “mere incident” in a larger tax avoidance case may prejudice Mr Badzyan’s case so that it may not be heard “fairly and justly” in accordance with the overriding objective.
21. Mr Gotch contests all of HMRC’s reasons in support of a stay. As regards the “parallel litigation” argument, he argues that the matters at issue in relation to the assessment against the Partnership, far from being largely the same, differ materially. That is so in two main respects. First, Mr Badzyan’s appeal is concerned primarily with the legality of the discovery assessment, whereas the central issue for the Partnership is the tax effect of the arrangements. Secondly, Mr Badzyan has not “used the scheme” — he retired before he received any payment, and forfeited his right to that payment. In Mr Gotch’s words:

“He received nothing and so avoided nothing and gained no tax advantage: if anything, the assessment gives him a tax disadvantage because it attempts to assess profits that he has never received and to which his entitlement lapsed on leaving the partnership. . .”

22. Further, argues Mr Gotch, if Mr Badzyan's case was stayed, he would in practice be forced to prepare a defence against HMRC's wider case alleging tax avoidance, which would not otherwise be required and which would substantially and unfairly increase the costs of the appeal to him.
23. As regards HMRC's "protective" issuance of a separate discovery assessment (the section 30B TMA point), Mr Gotch submits that it is irrelevant that other partners have been assessed, because their position is radically different; they received profits and Mr Badzyan did not.
24. The "balance of probabilities" argument, submits Mr Gotch, shows that HMRC fail to understand the distinct nature and separate focus of Mr Badzyan's appeal. Staying his appeal would be wrong because it would:
  - (a) be disproportionate to the importance and complexity of his case, considered on its own merits;
  - (b) impose significant financial and resource costs on him;
  - (c) deprive him of flexibility because his appeal would become dependent on HMRC's approach to another appeal; and
  - (d) introduce considerable additional delay, because any appeal by the Partnership has not even been notified to the Tribunal.
25. I will now consider the "material assistance" and "expediency" tests referred to in *Court Telecom*, and then consider the period of any stay.
26. As to the question whether a Tribunal decision on an appeal by the Partnership "would be of material assistance . . . in resolving issues" before the Tribunal in Mr Badzyan's appeal, in my judgment the answer is yes.
27. While there are indeed certain issues in Mr Badzyan's appeal which are distinct from those arising in respect of the Partnership assessment, there are also critical issues in common. So, while the validity of the discovery assessment in Mr Badzyan's case could be determined solely by hearing Mr Badzyan's appeal, the central issues regarding the tax effectiveness of the arrangements and the timing of any income tax charge could not. That is for the reasons put forward by HMRC and referred to above. Questions such as the degree to which the transactions fall to be analysed solely by reference to the Partnership Agreement, the extent to which the overall arrangements were motivated by tax avoidance, and the extent to which the corporate member invariably followed Partnership recommendations regarding "special capital" allocations, could not be properly and justly addressed by the Tribunal in Mr Badzyan's appeal. They would require evidence and disclosure from the Partnership to be considered and dealt with fairly and justly.
28. I accept, on the other hand, that a decision in relation to the Partnership assessment might well not resolve all the issues in Mr Badzyan's appeal. But the test in *Court Telecom* is not whether another decision would be determinative, or whether it would resolve all the issues.
29. If it were determined on the Partnership appeal that HMRC was wrong to tax the profit allocation as effectively made to the individual members via the

conduit of the corporate member, then that would clearly be of material assistance in determining whether a partner who forfeits his allocation, such as Mr Badzyan, could nevertheless be taxed in the year the profits arise to the corporate member. If it were determined on the Partnership appeal that HMRC's substantive arguments regarding the remuneration analysis and/or ITA 2007 analysis were wrong, then that would be of material assistance in determining the effectiveness of the arrangements as a whole.

30. I also conclude that on balance it would be "expedient" to stay Mr Badzyan's appeal. HMRC's arguments regarding parallel litigation (set out at [16] and [17] above) in my judgment clearly outweigh the admitted disadvantages to Mr Badzyan of a stay. The fact that Mr Badzyan has separate arguments to other partners in so far as he forfeited his right to the allocation by retiring does not outweigh the parallel litigation concern in the context of the overriding objective. A tribunal could still, in my judgment, determine Mr Badzyan's appeal "fairly and justly", without the "tainting" Mr Gotch suggests. Mr Gotch's argument that a stay would involve Mr Badzyan in greater expense in contesting the "tax avoidance" issues in my judgment has no merit: in practice, a stay means it is the Partnership which would bear the brunt of that expense. Finally, Mr Gotch's submission that a stay would be wrong because Mr Badzyan "had not used the scheme" begs the question. HMRC's position is that profits are allocated at the date when the corporate member received them, and what is later forfeited by a retiring partner such as Mr Badzyan is the right to benefit from the profits. It is for the Tribunal to determine whether that is right.
31. The final issue is the appropriate period for the stay. I am persuaded by the arguments put forward by Mr Gotch that an indefinite stay would not be appropriate. I was told by HMRC that discussions with the Partnership are continuing, but that HMRC have not yet issued a formal review decision. It is therefore possible, if perhaps unlikely, that the Partnership may not appeal against their assessment, or that HMRC may withdraw their assessment. The process may take many months to progress.
32. In the circumstances, I consider that an indefinite stay of Mr Badzyan's appeal would strike the wrong balance for the purposes of the overriding objective. HMRC's application did suggest that in the alternative a stay of six months might be appropriate. I consider that to be a reasonable approach in all the circumstances, and I therefore conclude that Mr Badzyan's appeal should be stayed for a period of six months from the date when this judgment is released to the parties. The Tribunal will likely be asked to review the appropriateness of any further stay at that stage, if that remains relevant.

#### *Application to reallocate as complex case*

33. Mr Badzyan's appeal is currently categorized as "basic". HMRC apply to have it re-allocated as "complex".
34. Rule 23 of the Tribunal Rules states, so far as relevant that:

“(4) The Tribunal may allocate a case as a Complex case under paragraph (1) or (3) only if the Tribunal considers that the case —

(a) will require lengthy or complex evidence or a lengthy hearing;

(b) involves a complex or important principle or issue; or

(c) involves a large financial sum. . .”

35. I approach this application guided by the decision in *Capital Air Services v HMRC* [2010] UKUT 373 (TCC) and by the Tribunal Practice Statement “*Categorisation of Cases in the Tax Chamber*”.

36. In *Capital Air Services*, the Upper Tribunal (Judges Warren and Oliver) stated at [25]:

“In any case, it is clear beyond argument, we think, that the assessment of what is ‘complex’ evidence or a ‘complex’ issue within 23(4)(a) and (b) is a matter of judgment. The task of making that judgment is assigned to the tribunal whose decision, if made applying the correct principles, can be overturned on an appeal to the Upper Tribunal only if it can be said that no reasonable tribunal could have reached that decision.”

37. At [4] the Tribunal Practice Statement considers complex cases, and having set out the relevant part of Rule 23, states:

“The Tribunal will assess whether, having regard to the nature of a particular case, any one or more of these criteria are satisfied. In making this assessment the Tribunal will take into account all the circumstances, including the implications of the costs-shifting regime (subject to the right of the taxpayer to opt out) and the fact that cases allocated to the Complex category are eligible, subject to various consents, to be transferred to the Upper Tribunal.

If on such an assessment the Tribunal considers that a case meets the stated criteria, it will, in the absence of special factors, allocate the case to the Complex category.

38. In *Dreams v HMRC* [2012] UKFTT 614 (TC) Judge Bishopp indicated (at [31]) that “special factors” meant “exceptional circumstances”.

39. In deciding whether or not to categorize Mr Badzyan’s appeal as a Complex case, I must first decide whether or not it meets one or more of the gateway criteria in Rule 23(4). In the words of Judge Sinfield in *JSM Construction Ltd. v HMRC* [2015] UKFTT 474 (TC) at [16]:

“Nothing in this decision [on categorisation] should be taken as indicating any view about the issues that arise in this appeal other than whether the case meets one or more of the criteria in the Rule 23(4)”.

40. In terms of whether the case will require lengthy or complex evidence or a complex hearing, HMRC estimated that Mr Badzyan’s appeal might take two to three days. Mr Gotch estimated that it would take a maximum of three days. HMRC considered that it might entail “relatively” complex evidence, while Mr Gotch disagreed.

41. This does not in my judgment amount to lengthy or complex evidence or a lengthy hearing, relative to similar cases before the Tribunal.

42. Does Mr Badzyan’s appeal involve a complex or important principle or issue? It is clear from [14] of *Capital Air Services* that what is complex or important should be assessed in the context of taxation and tax appeals. HMRC submitted that the issues of whether the Partnership was a conduit and whether individual partners were taxable when income was allocated to the corporate member were

both complex and important. Mr Gotch submitted that the latter point was merely “a short point of construction of the partnership deed”, while the former point was not relevant to Mr Badzyan because he had forfeited his right to profits.

43. In the context of tax appeals relating to partnership taxation I am not persuaded that the issues in Mr Badzyan’s appeal are unusually complex. I am, however, of the view that they are “important”, in part because they would be likely to be determinative of (or materially relevant to) certain issues in relation to the Partnership assessment, and also because of the precedential weight of those issues beyond Mr Badzyan’s appeal. HMRC stated during the proceedings that the total tax at stake in relation to the Partnership was approximately £30 million and in relation to variations of the arrangements was several hundreds of millions of pounds. While Mr Gotch submits that this unfairly conflates Mr Badzyan’s appeal with other assessments, in my judgment the overlap between the principles or issues in Mr Badzyan’s appeal and those other situations does render the points at issue in his appeal important.
44. Does the case involve a large financial sum? Having determined that Rule 23(4)(b) is engaged, strictly speaking it is not necessary for me to decide this point. I will, however, deal with it in case my decision on that point is the subject of appeal.
45. I take the correct approach to this question to be that adopted by Judge Sinfield in *JSM Construction*, at [26] to [29]. In this case, the amount assessed in the discovery assessment is approximately £300,000. However, in light of information which HMRC have discovered since they issued the assessment, they consider that the amount of undeclared tax for 2011-12 is closer to £800,000. Even without taking account of the “indirect” arguments discussed in *Babergh District Council v HMRC* [2011] UKFTT 341 (TC) in relation to “the taxpaying community as a whole”, which I would not regard as a proposition of general application in relation to Rule 24(4)(c), I regard £800,000 as a relatively large sum in context.
46. For the reasons given, I direct that Mr Badzyan’s appeal should be categorized as Complex.
47. 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 Rules. The application must be received by Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to “Guidance to accompanying a Decision from the First-tier Tribunal (Tax Chamber)” which accompanies and forms part of this decision notice.

**THOMAS SCOTT  
TRIBUNAL JUDGE**

**RELEASE DATE: 22 MAY 2017**