DEFINING THE AMBIT OF TAX APPEALS BY REFERENCE TO CLOSURE NOTICES

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The fundamental question considered in this paper is the following: if the UK tax authorities (HMRC) purport to amend a UK taxpayer's self-assessed tax return on the basis of one particular technical argument, to what extent can they subsequently rely upon any other technical arguments in the event that the taxpayer appeals to a specialist tax tribunal against HMRC's amendment of the tax return and/or the effects of such an amendment?

There is a general question of policy here, but there is also a question of statutory interpretation, since the answer to the fundamental question lies (or, at least, ought to lie) in those provisions of current UK tax legislation concerned with the scope of taxpayer appeals under the various self-assessment systems by means of which taxpayers now report their liabilities to UK income tax, capital gains tax, corporation tax and stamp duty land tax.

In the summer of 2008 the fundamental question was considered for the first time by the High Court during the course of an appeal from the decision of a tax tribunal in Tower MCashback LLP v Revenue and Customs Commissioners [2008] STC 3366. However, the question had already been considered at tribunal level in a case that was analysed by the High Court in the Tower appeal. Furthermore, the same issue was also relevant to the outcome of two other tax appeals that were heard by tribunals at about the same time as the High Court's decision in Tower was first made public, so that the issue was immediately placed back under the judicial spotlight for further consideration.

When the issue first arose at tribunal level, HMRC were not prevented from developing new arguments during the course of the appeal, but the High Court's first

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decision on this issue might initially have appeared to be quite restrictive when viewed from HMRC's perspective. However, the tax tribunals have evidently felt entitled to interpret the High Court's decision in Tower in a manner which offered the tax authorities greater administrative and/or tactical flexibility than they had been permitted by the High Court on the facts of the Tower case itself. It is submitted that the tribunals were generally correct in their approach because the High Court's decision in Tower on the question of general principle was more liberal (considered from HMRC's perspective) than its decision about the appropriate means of disposing of the specific dispute then before the court. However, one tribunal might have gone too far, as explained below

Although current judicial authority in this area consists of one fairly restrictive decision of a superior court and a small group of more liberal decisions by inferior tribunals, it is important to appreciate that, when properly understood, these various decisions are not necessarily inconsistent with each other. The High Court did not purport to over-rule the original tribunal decision on this issue, even though the actual outcomes of the two cases were markedly different from each other, whilst the later tribunal decisions purport to be (and, on the whole, actually are) faithful applications of the approach originally developed at tribunal level and then endorsed by the High Court in the Tower case, although one tribunal might have erred in its application of the key principles.

The Tower MCashback case

The Tower case concerned claims for capital allowances in respect of substantial expenditure on commercial software development. The appellant taxpayers were two LLPs comprised of individual investors, so that the case was governed by the statutory self-assessment rules applicable to individuals rather than the slightly different self-assessment rules applicable to companies that are liable to corporation tax. Much of the discussion in the Tower case relates to substantive questions about the legitimacy of the taxpayers' claims for tax relief, but a preliminary question arose as to HMRC's basic entitlement to raise a number of the arguments on which they wished to rely.

This was because HMRC had originally refused the taxpayers' claims (which can be regarded as identical for present purposes) on a highly specific basis, the sole initial ground for refusal of relief being that, in HMRC's opinion, such claims were barred by section 45(4) of the Capital Allowances Act 2001 ('CAA 2001'). That provision (which was repealed in 2008) prevented tax relief being claimed under the capital allowances code if a person potentially entitled to allowances in respect of software development had incurred expenditure on such software "with a view to granting to another person a right to use or otherwise deal with" any of the software.

After inquiring into the tax returns in which the disputed capital allowances were claimed, HMRC, as required by the relevant self-assessment legislation, formally terminated their inquiries by issuing a “closure notice” to the taxpayers, in which HMRC stated the conclusion reached as a result of their inquiries. The conclusion was to the effect that the taxpayers were not entitled to claim any capital allowances. This was on the basis that their relationship with a foreign supermarket chain fell foul of section 45(4) CAA 2001, but it was later conceded by HMRC that the circumstances were not such as to engage this particular provision.

However, instead of then acceding to the taxpayers’ claims for capital allowances, HMRC sought to defend their original refusal of tax relief on completely different technical grounds, namely that the taxpayers had not spent all of the relevant sums on the acquisition of software rights, but that they had spent a large percentage of the total amount on a form of (as HMRC saw it) highly contrived financial engineering that was designed to provide an arbitrary and improper increase in the amount of tax relief available to the underlying investors in the software development project. In other words, HMRC regarded a substantial element of the total claim for capital allowances (about 75%) as relating to a commercially meaningless scheme to manufacture tax relief for individuals in possession of unsheltered taxable income.

At tribunal level HMRC had been permitted to advance that alternative argument and, albeit in a somewhat convoluted manner, that argument had essentially been accepted as correct, resulting in partial disallowance of the taxpayers’ claims. (Strictly speaking, HMRC’s argument did not prevail at tribunal level but, in terms of loss of tax relief, the decision took effect as though HMRC’s alternative argument had prevailed, and the key point for present purposes is that HMRC were not formally prevented from mounting a novel defence at tribunal level after initially refusing tax relief on a completely different basis).

On appeal to the High Court, Henderson J rejected HMRC’s alternative argument on the merits. However, crucially for present purposes, he also ruled that HMRC had not been entitled to advance such an argument in the first place. The sole basis of the original tribunal appeal in this case had been the two taxpayers’ objections to the contents of HMRC’s closure notice. When HMRC had issued the closure notice, the sole basis for refusing the tax relief claimed by the taxpayers had been HMRC’s belief that the taxpayers had disabled themselves from claiming such relief because the taxpayers intended to grant licences to third parties over the subject matter of the claim. Once that objection had fallen away, there was nothing left to appeal against, and HMRC could not then introduce wholly novel objections (as opposed to novel arguments in support of previously stated objections) to the contents of a person’s tax return when an appeal against an amendment to the return was already in progress.

On the facts of Tower itself, HMRC had committed themselves exclusively to a very narrow form of objection to the taxpayers' claims for tax relief. However, in holding HMRC rigidly to their original position, the High Court was not necessarily ruling that HMRC could never introduce *any* novel arguments into a self-assessment appeals process at *any* time after a closure notice had been issued. Furthermore, in the Bayfine case a tax tribunal has now elected to interpret the Tower decision fairly liberally on HMRC's behalf.

This is not entirely surprising because the tribunal in the Bayfine case included the redoubtable Dr John Avery Jones CBE, who had had occasion to consider this issue in detail in an earlier tribunal case about the scope of self-assessment appeal rights. Dr Avery Jones's initial decision on this point had been highly influential on the outcome of the High Court proceedings in the Tower case. Before considering the application of the Tower judgment in the Bayfine case, it is therefore necessary to examine the prehistory of the Tower judgment in the D'Arcy case.

Prehistory – the D'Arcy case

The D'Arcy case was heard at tribunal level in May 2006. The original tribunal decision was later (unsuccessfully) appealed to the High Court (D'Arcy v Revenue and Customs Commissioners [2008] STC 1329), but that appeal was only concerned with matters of substance and not with any questions of procedure. Therefore, the High Court in the Tower case only had to consider the D'Arcy case at tribunal level when seeking prior guidance on the proper scope of self-assessment appeals.

The substantive issue in D'Arcy was whether a particular type of tax avoidance scheme (based upon an arbitrary difference in the taxability and tax-deductibility of matching inward and outward repo-type transactions) worked in the manner alleged by the taxpayer who had implemented it. The key procedural question was whether HMRC could attack the scheme by reference to certain specific statutory anti-avoidance rules when they had previously investigated the taxpayer's use of the scheme and then issued a closure notice in which the only stated ground of objection was based upon the judicial anti-avoidance doctrine commonly known as the "Ramsay principle."

It was argued on behalf of the taxpayer that an appeal against an amendment to a self-assessed tax return should be confined exclusively to those technical issues mentioned in the closure notice that effected the amendment of the tax return. Starting their counter-arguments at the extreme opposite end of the spectrum, HMRC asserted that the statutory right of appeal against the content of a closure notice was merely the trigger mechanism by means of which the entire contents of a person's tax return became amenable to scrutiny by a tax tribunal.

The problem with the self-assessment appeals system, as Dr Avery Jones observed in his discussion of these issues in the D'Arcy decision, is that the relevant administrative and procedural rules have been shoehorned into an existing body of administrative legislation dealing with appeals against a fundamentally different type of tax assessment and dating from an era when the tax tribunals exercised a somewhat different administrative function.

On the one hand, the appeals legislation applicable to UK direct taxes still appears to impose upon such tribunals a continuing general duty, as it did in the days before the introduction of self-assessment, to ensure that the taxpayer is ultimately assessed to the objectively correct amount of tax. This suggests that all potentially relevant technical arguments should be capable of being aired before an appeal tribunal during the appeals process, regardless of the precise content of any formal pleadings initially submitted to such a tribunal by either the appellant or the defendant.

On the other hand, the taxpayer is supposed to be protected under the self-assessment regime from exposure to arbitrary inquiries into his tax affairs once he has complied with the statutory obligation (which is frequently an onerous and expensive obligation) to undertake a comprehensive assessment of his own tax liabilities. That consideration (which is most recently reflected in the 2008 legislation vesting HMRC with new and more expansive information-gathering powers, since such powers cannot generally be exercised after a tax return has been submitted) points towards a restrictive reading of the appeals legislation, so as to prevent the whole of a taxpayer's affairs being raked over during the course of an appeal that supposedly relates only to one or two specific issues.

It is notable in this respect that the self-assessment legislation delineates rights of appeal only by reference to the contents of HMRC's closure notice and not by reference to the amended self-assessed tax return itself. This suggests that the contents of a tax return cannot be questioned during an appeal process except to the extent that any particular aspect of the content has previously been challenged by means of a suitable statement in a closure notice.

In effect, the tribunal reconciled these conflicting policy aims and apparently inconsistent statutory provisions by ruling that the statutory reference to a "conclusion" in a closure notice should be read as referring to any statement which determined the "factual compass" of a dispute between a taxpayer and HMRC, but not to any particular legal argument(s) advanced in support of HMRC's view of the taxpayer's affairs. Since a tribunal was entitled to form its own view of the law, and since nothing in the appeals legislation specifically granted a taxpayer rights of appeal against any particular line of reasoning adopted by HMRC, it was not appropriate to read the self-assessment legislation as restricting HMRC to any particular legal argument merely because they might have failed to mention other potentially relevant arguments when issuing a closure notice.

On the facts of the D'Arcy case, HMRC had issued a closure notice in which they expressed a formal "conclusion" to the effect that certain transactions "should be regarded as a composite whole which was circular and self-cancelling." It was possible, in principle, to read that statement as a specific conclusion of law, along the following lines: "the transactions are fiscally ineffective because the Ramsay principle applies so as to deprive those transactions of their ordinary effects for tax purposes." Such a reading would, presumably, have prevented HMRC from defending any appeal against their "conclusion" by reference to anything other than the contents of the established Ramsay case law.

However, since the tribunal took the view that it should decide questions of law for itself, it was more appropriate, when seeking to determine the scope of rights of appeal, to interpret HMRC's statement thus: "the taxpayer's view of the fiscal effects of these transactions is not accepted by us." This entitled HMRC (subject to general considerations of proper case management) to develop any reasonably relevant and plausible argument in support of such a view once the appeals process was under way.

Developments after D'Arcy – determining the "factual compass"

When the Tower case reached the High Court, both litigants and the judge were content to adopt the reasoning of the tribunal in the D'Arcy case, although they differed as to the consequences of doing so. In this respect, it is important to look at precisely what is meant when reference is made in these cases to the "factual compass" of a tax appeal.

It will be recalled that HMRC issued a closure notice in the Tower case in which they expressed the opinion that the taxpayers' claims for tax relief failed on the sole basis that section 45(4) CAA 2001 applied so as to defeat those claims. At first sight, that appears to be a conclusion of law. However, it is important to appreciate that Henderson J ultimately decided the procedural aspect of the Tower case against HMRC on the basis that their formal statement about section 45(4) CAA 2001 determined the *factual* compass, not the legal compass, of the appeal.

The true significance of HMRC's selection of section 45(4) CAA 2001 to the exclusion of all other options was not that it precluded them from advancing any other technical arguments about the taxpayers' entitlement to capital allowances during the subsequent development of the appeal, but that it precluded them from subsequently disputing any factual issues which were irrelevant to an argument based solely upon section 45(4) CAA 2001.

It was implicit in a formal conclusion to the effect that section 45(4) CAA 2001 applied that HMRC accepted the essential validity of the taxpayers' claims but for the alleged intention to grant licences of a kind prohibited under section 45(4) CAA

2001. In other words, HMRC had decided to proceed on the basis that the taxpayers had provisionally qualified for relief and then been disqualified, as opposed to never having qualified for relief in the first place.

Therefore, once HMRC had belatedly acknowledged that no impermissible licensing arrangements had ever been in contemplation so as to taint the relevant claims for tax relief, it was not then open to HMRC to contend by way of fall-back position that the taxpayers had simply never had any valid claims for relief on any basis at all, even in the absence of such impermissible licensing arrangements. This was simply outside the scope of a "conclusion" based exclusively on section 45(4) CAA 2001.

As Henderson J emphasised in his judgment in the Tower case, the UK's self-assessment legislation only permitted a closure notice to be issued to a taxpayer on a "once and for all" basis as at a certain point in time. There was no statutory mechanism enabling a notice to be recalled, reissued or amended once it had first been issued, and so it was incumbent on the tax authorities to finalise their view (or, as discussed briefly below in relation to the Chappell case, a range of different views) before taking the irrevocable step of issuing a formal closure notice against which the taxpayer could then appeal.

Therefore, Henderson J effectively endorsed the tribunal's earlier conclusion in the D'Arcy case – namely, that a tribunal should permit all relevant legal issues to be raised and should then determine any relevant questions of law for itself – but he subjected this to the qualification that the legal scope of an appeal was necessarily circumscribed by any statements in HMRC's formal "conclusion" that narrowed the underlying factual scope of the appeal.

HMRC had made a fatal mistake in the Tower case by stating a conclusion that, through reliance upon an extremely narrow legal argument about third party licensing arrangements, incidentally confined the factual scope of the appeal to questions about such licensing arrangements. If HMRC had expressed more general reservations in the closure notice about the taxpayers' entitlement to claim capital allowances, they could subsequently have developed a wider range of arguments about the proper statutory and/or judicial authority for refusal of the taxpayers' claims.

In stating that HMRC should have expressed "general" reservations, it is important to appreciate that HMRC would not have needed to be deliberately vague in order to keep their options open. Even if HMRC had initially made reference to specific statutory provisions and/or specific technical arguments, it is submitted that, in the light of Henderson J's observations about the proper scope of self-assessment appeals, HMRC would still have been entitled to develop other arguments at a later stage, provided that the initial arguments were of a kind that put the whole disputed transaction in issue and not merely some particular element thereof, such as the possibility of entering into third party licensing arrangements.

(It appears from the reported judgment in the Tower case that HMRC had rushed into issuing their formal conclusion in an effort to comply with a specific request from the taxpayers to finalise their position. But it is not clear exactly why HMRC behaved in this way. As Henderson J noted in the judgment, HMRC were not obliged to yield to pressure from the taxpayers and HMRC ought to have delayed issue of the closure notice if they were still not sure of their ground. If dissatisfied with HMRC's continuing failure to finalise their views, the taxpayers could have exercised a specific statutory right to apply to an appeal tribunal for a direction requiring HMRC to close the inquiry. However, no such application had been made by the taxpayers at the time when HMRC committed themselves irrevocably to what turned out to be a premature and misconceived statement of their final position.)

The Bayfine case – application of the Tower principle

The Bayfine case was heard at tribunal level in October 2008 at just about the same time as the High Court's decision in the Tower case first entered the public domain: the High Court judgment is officially dated 13 October 2008 and the Bayfine hearing dates are listed on the cover of the published decision as 13-15 October 2008. The dispute in the Bayfine case concerned an attempt to manufacture both tax-deductible losses and tax-exempt profits in the UK by means of a tax avoidance scheme involving cross-border interest rate transactions.

In essence, a pair of related UK companies entered into contracts with a pair of related US companies (the two pairs not being related to each other) under which members of each pair effectively took equal and opposite positions on specified future interest rates, so that the two contracts would effectively cancel each other out in purely financial terms, but not (so it was hoped) in UK fiscal terms. For tax purposes, it was intended that a loss would be created, which could be utilised under the group relief rules, whilst an almost identical profit would be sheltered from UK corporation tax under the provisions of the UK-USA double tax treaty.

HMRC sought to attack the tax loss element of the scheme by invoking certain special anti-avoidance provisions (now repealed) contained in the Finance Act 1994. They also sought to prevent the profit element being treated as tax-exempt under the terms of the UK-USA double tax treaty, either directly, through restrictive interpretation of the treaty itself, or indirectly, through disapplication of the normal treaty regime under section 795A Income and Corporation Taxes Act 1988 ('ICTA 1988') (on the basis that the relevant parties had failed to take reasonable steps to obtain available foreign tax credits, which would have reduced the need to claim treaty relief against applicable foreign taxes).

However, after initially setting out their objections on the above basis, HMRC later sought to deploy a broader range of technical arguments as regards both the loss element and the profit element of the disputed transactions. In respect of the losses claimed, HMRC sought to invoke additional anti-avoidance rules from the same body of legislation originally placed in issue. As regards the profit element, HMRC later sought to prevent the taxpayers from obtaining double tax relief under the statutory rules relating to unilateral relief as an alternative to the double tax treaty. Therefore, before evaluating the full range of technical arguments on the merits, the tribunal in the Bayfine appeal first had to decide whether a number of HMRC's arguments could legitimately be raised at all.

If the only prior source of authority or guidance had been the D'Arcy decision, it seems pretty clear that the tribunal in the Bayfine case would have allowed HMRC to develop a broader range of technical arguments than they had originally stated in the relevant closure notice. Nonetheless, was a more restrictive approach now required in the light of the High Court's decision in the Tower case? The tribunal in Bayfine decided that it was not.

Although a restrictive approach had been taken on the particular facts of the Tower case, the broader approach previously taken in the D'Arcy case had been endorsed as a matter of principle. Therefore, it was not essential for HMRC to raise all potentially relevant technical arguments in the closure notice itself (or, as actually seems to have happened on the facts of the Tower case, in any pre-litigation correspondence to which the closure notice made cross-reference). New arguments could be developed after issue of a closure notice, provided that any such arguments were not fundamentally inconsistent with any formal conclusion stated in the closure notice nor with any underlying conclusions on which such conclusions were necessarily based.

Since the closure notice in Bayfine dealt with both the deduction of losses and the taxability of profits in an entirely general manner – i.e. disputing the tax effects of each element of the transactions in terms which (unlike HMRC's exclusive reliance upon section 45(4) CAA 2001 in the Tower case) did not place any aspects of the overall transactional matrix beyond the scope of any further technical challenge – it was perfectly proper for HMRC to introduce new arguments in support of their basic contentions that relevant profits were taxable and that relevant losses were not deductible.

The Chappell case – reliance upon alternative conclusions

One of the reasons advanced by HMRC in the D'Arcy case in support of their assertion that an entire tax return could legitimately be scrutinised during the course of a tax appeal was that HMRC could not adopt inconsistent alternative positions in the text of the closure notice by means of which a self-assessment inquiry process was formally terminated. In refusing to accept that an entire tax return could always be scrutinised on appeal just because HMRC so wished, Dr Avery Jones had expressed the view that there was nothing in the current self-assessment legislation to prevent HMRC stating a number of alternative conclusions in a single closure notice.

It seems that HMRC took their cue from these comments in finalising their formal response at the end of another self-assessment inquiry, which led to one of the first two post-Tower cases to feature consideration of the High Court’s landmark decision in the Tower case. In Chappell v Revenue and Customs Commissioners [2009] STC (SCD) 11 the taxpayer was unrepresented and so the tribunal (which again included Dr Avery Jones) took the initiative in deciding whether HMRC could pursue more than one line of argument in seeking to treat a particular sum as taxable. However, the decision is probably noteworthy more for what it does not say than for what it does.

The fine details of the dispute in the Chappell case do not matter for present purposes. In essence, an individual received a certain sum of money, which might have been liable to either UK income tax or UK capital gains tax (and, in the latter case, either with or without the benefit of business taper relief, all relevant events having occurred prior to the abolition of such relief). As a result of an inquiry into the taxpayer’s self-assessment return for the relevant tax year, HMRC issued a closure notice in which they appear to have expressed the alternative conclusions that the disputed sum was either taxable as trading income or as a capital gain without the benefit of taper relief.

The Tower principle was aired briefly in the formal written decision in the Chappell case because, having initially framed an income tax argument solely in terms of trading, HMRC later sought to assert in the alternative that the taxpayer was liable to income tax on a residual basis, under what was then Schedule D Case VI (the schedular system of income tax still being in force at the relevant time).

What is significant is that, for the unrepresented taxpayer’s general protection, the tribunal was only prepared to raise the Tower principle of its own motion in relation to HMRC’s belated introduction of a Case VI income tax argument (only to later dismiss that point on the ground that both the Case I and Case VI income tax arguments fell within the same “factual compass”). By contrast, the tribunal apparently saw no reason to raise a similar objection in relation to HMRC’s attempt to pursue inconsistent lines of argument about their alleged entitlements to impose income tax and capital gains tax on the same receipt.

Therefore, the Chappell decision provides support (albeit only negative and implicit support) for the view that, as suggested on a speculative basis in the earlier D’Arcy case, HMRC are entitled to advance fundamentally inconsistent arguments during an appeal process, provided that suitable inconsistent conclusions have previously been stated in an applicable closure notice. This seems perfectly logical and would in fact appear to be vital from HMRC's perspective, given that they apparently have no legal right to issue more than one closure notice per inquiry into any particular tax return.

Since an argument about loss of entitlement to capital allowances under section 45(4) CAA 2001 would necessarily always be analytically inconsistent with any argument based upon an underlying failure to have qualified for allowances under general principles of capital allowances law, HMRC could presumably have retained the right to challenge the taxpayers' expenditure in the Tower case by raising their objection to the taxpayers' funding arrangements in the closure notice, as an alternative objection to that framed by reference to section 45(4) CAA 2001.

The Chappell case – what is "the same factual compass"?

Although interesting in terms of the tribunal's handling of HMRC's attempts to advance inconsistent alternative arguments, the decision in the Chappell case seems rather dubious in one fundamental respect. As mentioned above, HMRC originally advanced two alternative arguments against the taxpayer, to the effect that a disputed receipt was either trading income or a capital sum, but they then belatedly sought to argue that the sum might also possibly be taxable under what at the relevant time (prior to abolition of the schedular system) was known as Schedule D Case VI.
According to the text of the relevant legislation, income could only be taxed under Schedule D Case VI if it was not taxable under any other Case within Schedule D, which suggests that a single item of income could never be both trading income and Case VI income. In other words, the conclusions that income was taxable under the trading provisions and under Case VI were conclusions that were inconsistent and mutually exclusive; the income had to be taxable under one or the other (or under some different provision entirely), but not both.

The tribunal ultimately rejected HMRC's Case VI argument on its merits, but the tribunal did not formally prevent such an argument being advanced by HMRC in the first place, even though that argument had not been raised in the closure notice against which the taxpayer was appealing. The tribunal felt that development of such an argument was still permissible after issue of a closure notice from which it had been omitted, because in essence, the argument arose from the same facts as those arguments that had been explicitly outlined in the closure notice. However, was this the correct approach, in the light of the High Court's then recently published judgment in the Tower case?

The background to a legal dispute is frequently referred to as the "factual matrix", but the Tower case law contains references to the "factual compass" of a tax appeal. It seems strongly arguable that the "factual compass" of an appeal is not the same as its factual matrix, if the latter term is simply understood as a reference to general background events. The possible relevance of the Tower principle to the outcome of the Chappell case was raised and dismissed in a single paragraph in the tribunal's written decision, and in that paragraph the tribunal used the imprecise phrase "factual background" when referring to the range of arguments that might legitimately be deployed by HMRC during a tax appeal.

However, if all relevant background events could legitimately be taken into account in determining the permissibility of any particular technical defence that HMRC might wish to rely upon, it is difficult to understand how Henderson J could have decided the Tower case (as regards the purely procedural side of that dispute) in favour of the taxpayers. The tribunal in Chappell took the view that references to the taxation of trading income and taxation of Case VI income were simply "different arguments of law" relating to the same facts, so that both arguments could be developed during the appeal even though one of those arguments had not been notified to the taxpayer in the relevant closure notice.

It will be recalled that HMRC's two separate grounds for refusing claims for capital allowances in the Tower case were both based upon the same set of underlying facts and circumstances. However, as explained earlier in this paper, one of the two arguments was eventually held to be impermissible because it was at odds with the only stance adopted by HMRC in the closure notices that had been issued to the appellant taxpayers in that case. Thus, two "different arguments of law" were not regarded by the High Court as being equally permissible if the two were mutually incompatible and only one of them had been advanced as part of HMRC's formal conclusion about the scope of a taxpayer's liabilities.

There seems no doubt that, as a matter of pure analytical principle (i.e. considering the claims purely on their substantive merits, but disregarding the niceties of the procedural regime contained in the UK's current income tax and/or corporation tax self-assessment legislation), HMRC could legitimately have argued that the transactions at issue in the Tower case had never been capable of generating tax relief under any circumstances. However, HMRC were prohibited from raising such an argument, despite its apparent analytical relevance, because no suitable conclusion to that effect had actually been stated in the closure notices against which the appeal was being brought (nor it seems – see the Collins case, discussed below – could any such conclusion legitimately be inferred in the circumstances of that case). If HMRC were effectively estopped in the Tower case from raising an argument about a taxpayer's lack of any underlying entitlement to claim capital allowances because they had issued a single formal conclusion in which such an entitlement was assumed (albeit initially contested for a specific reason, later abandoned), why were HMRC not similarly estopped in the Chappell case from asserting that a particular sum could be taxed as non-trading income after they had stated a formal conclusion to the effect that trading was the only possible income-oriented basis on which the sum could be taxed?

An argument based upon Case VI would appear to have arisen from the same factual matrix as an argument about liability for tax on trading income, but applying the analysis in the Tower case, it seems that HMRC had narrowed the “factual compass” of the appeal by issuing a closure notice in which alleged trading was the only live issue identified in relation to possible income tax liabilities. Since Case VI was not concerned with trading, any formal conclusion expressed by HMRC solely in terms of trading ought to have precluded subsequent reliance upon an alternative argument about possible Case VI liabilities.

The Collins case – a different type of closure notice

The D’Arcy, Tower, Bayfine and Chappell cases analysed earlier in this paper were all concerned with closure notices issued to taxpayers by HMRC at the termination of official inquiries by tax inspectors into the contents of taxpayers’ ordinary tax returns. But a similar legislative mechanism also applies in relation to official inquiries into free-standing statutory claims for tax relief, such as that permitted under section 48 of the Taxation of Chargeable Gains Act 1992 (‘TCGA 1992’) in relation to any part of the deferred consideration for a capital disposal, which a taxpayer ultimately fails to obtain after he has already brought the relevant sum into account for tax purposes.

In Revenue and Customs Commissioners v Collins [2009] EWHC 284 it was necessary for Henderson J to consider the effects of a closure notice issued after the conduct of such an inquiry. None of the cases discussed above were mentioned by name in the Collins judgment, but the Collins case involved a similar issue to those cases because the taxpayer belatedly sought to argue, in an appeal from a decision of a tax tribunal, that the tribunal had had no jurisdiction to entertain the appeal, since HMRC’s preferred line of defence bore no relation to the content of the closure notice against which the taxpayer had appealed.

(Strictly speaking, no final decision was ever reached on the jurisdictional issues. This was because Henderson J concluded that the taxpayer’s underlying claim for tax repayment was fundamentally misconceived and that the appeal could never have succeeded on purely procedural grounds if the taxpayer had been permitted to advance new arguments about the original tribunal’s alleged lack of jurisdiction.)

In substantive terms, the Collins case was fairly straightforward. A taxpayer had sold some shares in a private company on terms that provided for both immediate and deferred tranches of cash consideration, together with the making of a special contribution to the taxpayer’s pension fund (albeit paid over to a third party). The original point of dispute concerned the characterisation of the pension contribution as part of the taxable consideration for the disposal of the shares. That issue was initially decided in favour of the taxpayer at tribunal level and HMRC appealed.

As well as (unsuccessfully) defending his position on the merits, the taxpayer also sought to argue before the High Court – presumably because his advisers first became aware of the Tower jurisprudence not long before the case was due to be heard by that court – that there was nothing in relation to which the original tribunal could have given a meaningful decision. This was because an inquiry into the taxpayer's claim for repayment of excess tax had resulted in the issue of a closure notice containing a single ground for refusal of the claim and HMRC had then abandoned that line of argument. According to the taxpayer, this meant that there was nothing over which a tax tribunal could legitimately have exercised any jurisdiction, so that the proceedings were a nullity.

If it had been appropriate to view the matter in isolation, the taxpayer would presumably have succeeded on that basis (assuming – and this was a point which Henderson J felt that it was not ultimately necessary for him to decide - that the taxpayer was entitled to raise a fundamental jurisdictional issue before the High Court after having failed to do so before the original tribunal). However, Henderson J regarded the tax inspector's sole explicit conclusion as embodying a broader implicit conclusion.

The explicit conclusion was to the effect that the disputed pension contribution did not qualify as tax-deductible expenditure under the general capital gains tax ('CGT') computational provisions by virtue of its being otherwise chargeable to income tax. However, Henderson J took the view that it was appropriate to read the closure notice in the context of the preceding general correspondence between the parties.
On that basis, the explicit conclusion about lack of specific statutory tax-deductibility could be seen to be buttressed by a broader implicit conclusion to the effect that the pension contribution was itself part of the taxable consideration for the disposal of the taxpayer's shareholding. After all, there would be no need to seek specific reasons for excluding the pension contribution from the charge to CGT unless it was chargeable to CGT as a matter of general principle. This meant that the tribunal had in fact had jurisdiction to consider whether the pension contribution was part of the taxable consideration and had not simply had jurisdiction to decide whether it was tax-deductible expenditure on the basis mentioned in the original closure notice.

This decision appears to be in line with the earlier cases discussed above, because although HMRC were permitted to rely upon matters not stated in the closure notice, these matters were not (unlike the novel capital allowances argument advanced in the Tower case) inconsistent in any way with the conclusions so stated, and indeed they flowed naturally from the single conclusion actually stated in the closure notice. Although it is not strictly relevant to the subject of defining the scope of appeals against closure notices, it is notable that HMRC attempted, during the course of argument in the Collins case, to arbitrarily broaden another of the statutory mechanisms relating to direct tax, but they were prevented by the judge from doing so. HMRC argued that the making by a taxpayer of a CGT repayment claim under section 48 TCGA 1992 entitled them to re-open the whole of any past CGT computation to which such a claim related.

However, Henderson J endorsed the view of the taxpayer's advocate to the effect that section 48 was only concerned with possible failure to obtain elements of deferred consideration in respect of a capital disposal. If, for some reason, the taxpayer had previously under-reported any part of the consideration which was payable *immediately*, a section 48 repayment claim could not be used by HMRC as an excuse to offset any past underpayments of tax which could have been the subject of an earlier assessment, but which had now become incapable of such assessment by reason of the expiry of the limitation periods for inquiring into a past tax return and/or making a discovery assessment.

Conclusion

It appears from the first handful of judicial decisions on the scope of self-assessment appeals that the courts and tribunals have sought to strike a fair balance between, on the one hand, the protection of taxpayers from unduly broad and speculative re-examination of their tax affairs during tax-based litigation and, on the other hand, the maintenance of HMRC's right to ensure that taxpayers' assertions of their rights are tested rigorously during appeal proceedings against the full range of potentially relevant technical arguments in support of HMRC's own view of the law on any particular matter.

It is suggested that this makes sense in terms of both public policy and legislative content. It would be pointlessly debilitating to require HMRC, at the precise moment when they proposed to issue a closure notice, to marshal all possible arguments they might wish to deploy in a subsequent appeal that might never actually take place. However, it is incumbent on HMRC to make clear to a taxpayer exactly which aspects of the taxpayer's affairs are in dispute.

However, early evidence suggests that the tax tribunals are not necessarily entirely consistent in their approach to the screening of new arguments raised by the tax authorities after the issue of a formal closure notice. Since it is the constitutional function of the legislature, not the courts, to cure any general defect (such as the lack of a statutory power to amend or re-issue a closure notice) in the administrative processes that enable HMRC to challenge a taxpayer's own view of his tax liabilities under the self-assessment regime, it is submitted that the tax tribunals should not permit new arguments to be raised by HMRC to the extent that any such arguments fundamentally alter the conceptual scope of an appeal after it has already commenced. A taxpayer who appeals to the tax tribunals should not be put to the trouble and expense of attempting to hit a moving target unless the relevant appeals legislation clearly requires this. At present, it does not.