

Analysis

Getting closure: the FTT's approach in *Hitchins*

Speed read

In the recent case of *Hitchins*, the FTT directed HMRC to issue a closure notice on the basis that outstanding information requests were not sufficiently relevant and therefore did not form a reasonable basis for keeping the enquiry open. In particular, there was no evidence that HMRC reasonably believed the query would actually yield relevant information. Advisers should consider this approach when analysing the merits of HMRC's information requests and considering whether there is evidence that such requests will yield relevant information. Refusing to provide the information requested by HMRC will not be fatal to an application for a closure notice where there is no reasonable basis upon which the information has been requested.



Sophie Rhind
Macfarlanes

Sophie Rhind is a senior associate at Macfarlanes. She acts on a broad range of contentious tax issues for a variety of clients from high net-worth individuals to multinationals. She has experience litigating appeals before the FTT up to the Court of Appeal, as well as judicial reviews in the High Court and Court of Appeal. Email: sophie.rhind@macfarlanes.com; tel: 020 7791 4079.



Victoria Braid
Macfarlanes

Victoria Braid is an associate at Macfarlanes. Victoria advises on a range of contentious matters, with a particular focus on tax disputes. Email: victoria.braid@macfarlanes.com; tel: 020 7849 2600.

Where a tax return addresses complex issues and facts, a lengthy enquiry may be inevitable. Frequently, however, enquiries can seem never-ending. Where discussions between the taxpayer and HMRC cannot progress matters, there are limited options open to the taxpayer, but the taxpayer can apply to the First-tier Tribunal (FTT) to direct HMRC to close their enquiries. Taxpayers are often reluctant to take this step, but the recent case of *Hitchins v HMRC* [2023] UKFTT 127 (TC) illustrates how the FTT will approach matters and demonstrates the value of being more assertive in managing HMRC enquiries in the right circumstances.

Applying for a closure notice

HMRC has one year from when a tax return is filed to open an enquiry. Once the enquiry is open, it will only come to an end when HMRC issue a closure notice. Unlike the strict timeframes in place for issuing assessments, there is no statutory deadline for the issuing of a closure notice. Until a closure notice is issued, the taxpayer will not know for sure whether there is an issue. With interest rates having risen significantly, a delayed enquiry is not only frustrating, but it carries with it potentially high costs if it is concluded that tax

is owed (at the time of writing, the interest rate on unpaid tax is 6.5%).

Involving the FTT is a last resort and asking HMRC informally for a closure notice should always be the first step, but the ability to apply to the FTT under TMA 1970 s 28A(4) for a closure notice to be issued within a specified period is an important protection for taxpayers. There are similar provisions in relation to enquiries into partnership returns (TMA 1970 s 28B(5)), claims not included in returns (TMA 1970 Sch 1A para 7(5)) and company tax returns (FA 1998 Sch 18 para 33(1)).

Once an application is made, the burden is then on HMRC to show that there are reasonable grounds for keeping the enquiry open. The FTT must direct a closure notice if it is not satisfied of this.

Reasonable grounds for keeping an enquiry open

Whether there are 'reasonable grounds' for HMRC not to give a closure notice will depend on the facts and will involve the FTT making a value judgment in order to determine what is reasonable in the circumstances (*Frosh and others v HMRC* [2017] UKUT 320 (TCC) at para 43).

HMRC will invariably argue that there are outstanding requests for information, or information has been provided, but it needs further time to consider the information and determine if further requests need to be made.

The case law is clear that simply identifying outstanding information requests is insufficient. HMRC must show that the information sought is reasonable and relevant (*Gulliver v HMRC* [2017] UKFTT 222 (TC) at para 14).

HMRC will not be forced to issue closure notices without sufficient facts. The Supreme Court in *HMRC v Tower MCashback LLP* [2011] UKSC 19 noted (at para 85) that, although a closure notice can be issued in broad terms, wherever possible it should set out conclusions on each aspect of the enquiry. HMRC may have difficulties in raising a new issue that was not identified in its closure notice, and the FTT will take this into account when determining if a closure notice should be directed.

Such arguments are not, however, always as effective for HMRC as it might hope. A closure notice may still be appropriate even if every line of enquiry has not been pursued to the end, as long as the officer can make an informed judgment of the matter (*Eclipse Film Partners No 35 LLP v HMRC* [2009] STC (SCD) 293 at para 19). HMRC may even be prevented from seeking more substantial information if it unreasonably protracted the enquiry (*Price v HMRC* [2011] UKFTT 264 (TC) at para 40).

The timing of any closure notice application is, therefore, important. It will be most effective where the taxpayer can show it has taken considerable steps to provide HMRC with all the relevant information. In those circumstances, the FTT will challenge HMRC to explain why its enquiries cannot be closed. *Hitchins* is an instructive example of just such an issue.

The background to *Hitchins*

HMRC's enquiries in *Hitchins* focused on the potential application of the transfer of assets abroad (ToAA) legislation.

As a reminder, the ToAA legislation (as contained in ITA 2007 Part 13 Chapter 2) can operate to treat income that arises to a person abroad as belonging to any UK resident individual who:

- is responsible for the original transfer of assets overseas and has a power to enjoy that income; or
- receives a benefit as a result of such a transfer of assets by another person.

In *Hitchins*, the main transactions took place nearly 20 years ago in 2003 and involved the transfer of shares in a UK company to various offshore entities along with the payment of a £40m dividend. HMRC did not open enquiries into the year the dividend was paid and were, instead, focused on how that sum was used and what enjoyment or benefit the taxpayers received in the years under enquiry.

For one applicant, HMRC's enquiries dated back ten years to the tax year ended 5 April 2013. In addition, there had been earlier enquiries between 2006 and 2008 which were closed without amendment, and during which it was submitted by the applicant that the same underlying events had been fully disclosed to HMRC.

As part of its enquiries, HMRC had issued numerous information notices and, while information was provided, various requests were disputed and were either withdrawn or successfully appealed. As a result, HMRC issued a notice under ITA 2007 s 748, which is a wide-ranging information power specific to the ToAA provisions that cannot be appealed. Further information was provided as a result of the notice.

Despite this, HMRC maintained that it still needed further details. In particular, the 'crucial missing information' was the ultimate destination of the £40m distribution.

It is particularly welcome to see this approach taken in relation to the ToAA provisions

The decision

When determining whether there were reasonable grounds for HMRC not to provide a closure notice, the FTT in *Hitchins* considered both:

- the extent to which HMRC's queries were relevant to their enquiries; and
- the extent to which the taxpayers had answered those queries,

in line with the approach taken in *Gulliver*.

The FTT noted that the parties disagreed as to the interpretation of some aspects of the ToAA legislation, but it was not for them to rule on such matters. For the purpose of this exercise, it proceeded on the basis that HMRC's interpretation was arguable.

In relation to the details of the ultimate recipients of the £40m distribution, the applicants explained that they had received no such distribution. The details of who may have received such distributions was therefore irrelevant to the determination of the open enquiries and so they refused to provide the information. HMRC contended that the query justified keeping the enquiry open because if the taxpayers had received a benefit from the £40m distribution as a result of further transactions, the ToAA legislation would apply.

When weighing up the merits of this outstanding query, the FTT found it significant that there was no evidence at all to indicate that the funds had been transferred for the benefit of the taxpayers. This lack of evidence undermined HMRC's argument that there was a reasonable basis for believing that there could be transactions which would satisfy the requirements of the ToAA legislation.

The FTT held that an outstanding query from HMRC cannot form reasonable grounds for delaying the closure of an enquiry when there is no reasonable basis for that query. When determining whether there is a reasonable basis for

the query, the FTT will consider whether there is evidence that HMRC reasonably believed the query would actually yield relevant information (in this case, the existence of subsequent transactions involving the £40m funds from which the taxpayers received a benefit). If there is no such evidence, the outstanding query amounts to a fishing expedition and will not justify keeping the enquiry open.

Following the approach taken in *Eclipse*, the FTT found that it was appropriate to direct that a closure notice should be issued even though the officer had not pursued every line of enquiry to the end. The enquiry had been conducted to a point where it was reasonable for the officer to make an 'informed judgment' of the matter.

There was a degree of frustration at HMRC's approach, which many taxpayers will share. The FTT concluded that HMRC had misinterpreted the information that it held (so that some of its assertions as to why its queries were relevant were factually incorrect), refused to acknowledge any errors or mistakes and rigidly adhered to its initial view of the matter. All of this undermined HMRC's position.

Relevance going forward

Although as previously noted, decisions in relation to applications for closure notices are fact specific, the FTT's view that HMRC's enquiries entailed a fishing expedition is helpful. The FTT did not duck the challenge of engaging with the complex rules in question in order to decide the application. HMRC's arguments that it needed to understand whether beneficiaries of the distribution in 2003 had 'passed it onwards, invested it on behalf of, or in any other way acted to direct that value to one or more of [the applicants]' might have been superficially compelling but the FTT considered what the potential charges actually were, looked at whether the information sought was relevant to that charge, and determined that HMRC's requests did not have a reasonable basis.

This case will, therefore, be of interest to any taxpayer facing a long running enquiry and it encourages taxpayers to engage with the merits of HMRC's information requests. Refusing to provide the information requested by HMRC will not be fatal to an application for a closure notice where there is no reasonable basis upon which the information has been requested.

It is particularly welcome to see this approach taken in relation to the ToAA provisions. The legislation is wide ranging, and it is common for HMRC to ask detailed questions about transfers that have taken place many years previously. As a result of the broad nature of the anti-avoidance provisions, it is frequently the case that HMRC cast a very wide net with its queries and the information sought in the hope that something will be caught. While the ToAA provisions have an important function in preventing offshore avoidance, many taxpayers will likely agree that HMRC's enquiries in this area are similar to the type of fishing expedition faced in *Hitchins*. It is reassuring that, in the right circumstances, the FTT will be prepared to step in and direct closure notices.

As a result of the finding in *Hitchins* as to the relevance of the requests, the FTT did not need to consider whether the enquiries were unreasonably protracted and how that would affect HMRC's ability to sustain their enquiries. This is an issue that many taxpayers face and it seems likely that the FTT will consider it further at some point. ■

For related reading visit taxjournal.com

Cases: *J Hitchins and others v HMRC* (7.3.23)