Project Blue Ltd v HMRC: An Arbitrary Decision (Part 2)

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An analysis of the Upper Tribunal's decision on the substantive issue in the case *Project Blue Limited v HMRC*[1] can be found in the last issue of *Private Client Business*.[2] The case also raised a number of other interesting issues, including a fascinating administrative argument (the "Administrative Issue") advanced by Project Blue Limited (PBL), which is considered in this article. Readers will remember that the case concerned whether the Finance Act 2003 (FA 2003) s.75A applied to treat PBL as the purchaser in a notional transaction. The text of s.75A as it was at the time of the case, along with a summary of the relevant transactions, is reproduced in boxes at the end of this article. The Upper Tribunal had found that, for the purposes of s.75A(1), the Qatari Bank Masraf al Rayan (MAR) was the vendor (V),[3] PBL was the purchaser (P),[4] the Scheme Transactions were Steps 1–7[5] and the notional transaction was a transfer of the Freehold from the Secretary of State for Defence (SSD) to PBL for a consideration of £1.25bn.[6]

The original appeal to the First-tier Tribunal[7] was against HMRC's amendment of PBL's return, (LTR1), which the FtT had found was in respect of Step 5,[8] the transfer of the freehold from the SSD to PBL under the contract that was entered into under Step 1. In respect of the Administrative Issue, PBL argued that if a liability arose under s.75A, it arose not in relation to the actual transaction under Step 5, but in respect of a notional transaction deemed to take place under s.75A(4) which, it will be seen from Box A, provides that:

> "(4) Where this section applies—
>
> (a) any of the scheme transactions which is a land transaction shall be disregarded for the purposes of this Part, but

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[1] *Project Blue Limited v The Commissioners for Her Majesty's Revenue & Customs* [2014] UKUT 0564 (TCC) (hereinafter referred to in this article as the "Upper Tribunal Decision").

[2] [2015] 4 PCB 182-200.

[3] Within s.75A(1)(a).

[4] Within s.75A(1)(a).

[5] Within s.75A(1)(b).

[6] Within s.75A(1)(c).

[7] *Project Blue Limited v The Commissioners for Inland Revenue* [2013] UK FTT 378 (TC) (hereinafter referred to in this article as the "FtT decision").

[8] FtT decision at [76].

(b) there shall be a notional land transaction for the purposes of this Part effecting the acquisition of 'V's chargeable interest by 'P' on its disposal by 'V'."

PBL argued that:

"It was clear from the details contained in … ['LTR1'] … that the return related to [a] disregarded transaction. It did not relate to the notional transaction for which HMRC argued under section 75A. HMRC could not, in [the Appellant's] submission, take one land transaction return and amend it to apply to a completely different (ie notional) transaction."[9]

The Administrative Issue: the FtT's decision

In respect of this argument, the FtT first referred to enquiries into land transaction returns explaining that:

"Paragraph 13 of Schedule 10 defines the scope of an enquiry under Part 3. So far as material, paragraph 13 (1) provides as follows: [10]

'An enquiry extends to anything contained in the return, or required to be contained in the return, that relates—

(a) to the question whether tax is chargeable in respect of the transaction, or to the amount of tax so chargeable…'"

It went on to state that:

"In our view, the fact that HMRC amended the return in respect of the actual transfer of the freehold by the MoD to the Appellant rather than a return in respect of a notional transfer of the same freehold between the same parties, does not invalidate the closure notice or the amendment.

There is nothing in paragraph 23 of Schedule 10 that precludes an amendment to a return in respect of the actual transfer in accordance with the provisions of section 75A which applies to a notional transfer. The conclusion of HMRC was that the tax due was £38.36 million (and by the amendment to HMRC's Statement of Case the Tribunal is asked to increase the amendment to the self-assessment under paragraph 42 (3) Schedule 10 FA 2003 to show tax due of £50m).

We do not consider that the terms of paragraph 13 of Schedule 10 contradict this conclusion. The enquiry can extend to anything contained in the return. The return related to a 'scheme transaction' for the purposes of section 75A. We do not read the reference in paragraph 13 (1) (a) to 'the transaction' as precluding an enquiry into whether the actual transfer of the freehold from the MoD to the Appellant (which by virtue of section 45 (3) was not, in fact, a land transaction) can be re-characterised as a notional transaction under section 75A.

In this case, the return amended by the closure notice was a return in respect of the same parties to the notional land transaction (i.e. the MoD and the Appellant) and related to the same interest in the Property. The closure notice of 13 July 2011 made the amendments necessary to give effect to HMRC's conclusions in respect of their enquiry. The only amendment made was to adjust the tax payable by the Appellant."[11]

The FtT does not seem to have given due weight to the fact that Sch.10 para.13(1) restricts the enquiry to:

"… anything contained in the return, or required to be contained in the return, that relates—

(a) to the question whether tax is chargeable in respect of the transaction, or

[9] FtT decision at [109].
[10] FtT decision at [300].
[11] FtT decision at [301]–[304].

(b) to the amount of tax so chargeable…"

Accordingly, the enquiry cannot extend beyond anything that is contained in the return that relates to the transaction referred to in Sch.10 para.13(1)(a), which must be the transaction that is the subject of the return.

HMRC can amend a taxpayer's return under Sch.10 para.23, but only in respect of the conclusions of its enquiry. If its enquiry can only be in relation to the transaction which is the subject of the return, and the return it amends is in respect of an actual transaction and not a notional transaction under s.75A(4), any conclusion that is not in respect of the actual transaction cannot be a conclusion of the enquiry and therefore HMRC cannot make any amendment in respect of a notional transaction. It is clear that a notional land transaction under s.75A(4) must be a different transaction to any of the Scheme Transactions which actually take place, yet the FtT said:

> "We do not read the reference in paragraph 13(1)(a) to 'the transaction' as precluding an enquiry into whether the actual transfer of the freehold from the MoD to the Appellant … can be recharacterised as a notional transaction under section 75A."[12]

In this, the Tribunal asked itself the wrong question; it should have asked whether there is anything in ss.75A–75C to allow one to identify the notional transaction under s.75A(4) with any of the Scheme Transactions under s.75A(1)(b)? The answer must surely be that there is not. The Scheme Transactions are between various parties and in respect of various interests. It is true that In choosing to amend LTR1, HMRC amended the return in respect of the scheme transaction that most nearly corresponded to the notional transaction, but it was not exactly the same and the similarities were to some extent accidental. The terms of the notional transaction are determined under s.75A(1), (5) and (6). In this case, it happened that the notional transaction was between the same parties, related to the same interest in the Property and was deemed to take place on the same date as the actual transaction that was the subject of the amended return, LTR1, but the consideration for the two transactions differed. In any event, it was an accident of the facts of the case that the parties and dates of the two transactions were the same. If the lease to the appellant had been granted by MAR on February 1, 2008 and not on January 31, the dates of the notional and actual transactions would have differed. If other PBGHL Group[13] companies had been involved in the transactions, there might have been no actual transactions at all between the parties to the notional land transaction.

The FtT gave no reason why one should identify the notional land transaction with one out of several actual scheme transactions or why one should do so even where the terms of the notional and comparative transactions differ.

On an appeal, the Tribunal may only amend a self-assessment if it appears to the Tribunal that PBL is overcharged by a self-assessment or is undercharged by it (Sch.10 para.42). Thus, the Tribunal's decision is confined to the subject matter of the self-assessment. The self-assessment which is the subject of the appeal was the self-assessment in respect of the actual land transaction and not in respect of the notional land transaction under s.75A(4).

Because it is clear that HMRC's amendment could not have been in accordance with the conclusions of its enquiry into that return, for it is clear that no liability arose in respect of the actual land transaction that was its subject, one might have thought it obvious that the FtT was under a duty to restore the taxpayer's self-assessment.

[12] FtT decision at [303].
[13] PBL was a member of the PBGHL Group.

The Administrative Issue: the Upper Tribunal's decision

In the Upper Tribunal, however, Morgan J, with whom Judge Nowlan agreed, said:

> "The first question is how to interpret the return numbered 307388936MC [the LTR1]. Should that return be read as a return in relation to the actual transfer from SSD to PBL or as a return in relation to the notional land transaction whereby, pursuant to section 75A, SSD disposed of its freehold and PBL acquired that freehold for a consideration of £959 million? The principal, and perhaps the only, point in favour of reading it as a return of the actual transfer is that the return referred to a contract of 5 April 2007; a reference to that contract had no part to play in a return of the notional land transaction."[14]

Morgan J's decision that the LTR1 which the FtT had found was in respect of Step 5 (the transfer of the property from the SSD to PBL in completion of the contract under Step 1), should indeed be regarded as a return of the notional land transaction was based on the following argument:

> "Against this background, I return to the question whether the return delivered by PBL in relation to a transfer of the freehold by SSD to PBL should be considered to be a return of the actual transfer or a return of the notional land transaction. If the return related to the actual transfer, then it was an unnecessary return. Further, if the return related to the actual transfer, the result was that PBL failed to perform its statutory duty to deliver a return in relation to the notional land transaction.
>
> With some hesitation, I consider that the return in question can be considered to be a necessary return, rather than an unnecessary return, and a return which performed PBL's obligation under section 76 to deliver a return. On this basis, it was a return in relation to the notional land transaction in accordance with section 75A."[15]

With all due respect to Morgan J, one has to say that this suggestion that a taxpayer who did not consider that s.75A applied to impose a charge to tax on a notional transaction, made a return of that notional transaction claiming that the SDLT liability arising on it was reduced to nil by an unspecified relief, a thing which was impossible because, if the SDLT on the notional transaction had been nil, the condition in s.75A(1)(c) could not have been satisfied is startling. Morgan J cited[16] *Pollen Estate Trustee Co v RCC*[17] in summarising the principles to be applied to the construction of statutes. That summary in turn referred to the seminal House of Lords' decision in *Barclays Mercantile Business Finance Ltd v Mawson (Inspector of Taxes)*[18] which in turn quoted with approval[19] the remark of Ribeiro PJ in *Collector of Stamp Revenue v Arrowtown Assets Limited*[20] that:

> "The driving principle in the *Ramsay* line of cases continues to involve a general rule of statutory construction and an unblinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically."[21]

Was it "realistic" of Morgan J to conclude that PBL's return actually related to a notional transaction arising under s.71A even though the FtT had found as a fact that it "related to the completion on January 31, 2008 of the contract between the SSD and PBL dated 5th April 2007" and even though PBL, who

[14] Upper Tribunal decision at [117].
[15] Upper Tribunal decision at [123] and [124].
[16] FtT decision at [51].
[17] *Pollen Estate Trustee Co v RCC* [2013] 3 All ER 742.
[18] *Barclays Mercantile Business Finance Ltd v Mawson (Inspector of Taxes)* [2004] UKHL 51.
[19] *Barclays Mercantile Business Finance Ltd v Mawson (Inspector of Taxes)* [2004] UKHL 51.
[20] *Collector of Stamp Revenue v Arrowtown Assets Limited* [2003] 6 ITLR 454.
[21] *Collector of Stamp Revenue v Arrowtown Assets Limited* [2003] 6 ITLR 454 at [35].

made the return, did not consider that the notional transaction, of which it was supposed to have made a return arose at all? It is suggested that this is an unrealistic view of the matter.

One would not dissent from Morgan J's conclusion that the notional land transaction was notifiable under ss.76 and 77 (which concern notifiable transactions) in spite of the fact that, at that time, s.77(1) did not provide specifically that a notional land transaction under s.75A was a notifiable transaction, although it was later amended to do so. The authors did consider that, as the completion of PBL's acquisition of the Freehold from the SSD was to be disregarded under s.45(3), either Morgan J was correct to say that the return was unnecessary or it was not a return at all. It is also true, as Morgan J said, that PBL failed to perform its statutory duty to deliver a return in relation to the notional land transaction. None of that, however, would seem to lead to the conclusion that PBL must be presumed to have made a return which it did not think was required.

As PBL argued, where a taxpayer fails to make a return of a land transaction, HMRC's remedy is to make a determination under FA 2003 Sch.10 para.25.

Could HMRC Issue a Determination in respect of PBL's Failure to make a Return of the Notional Transaction?

If:

> "… the Inland Revenue discover as regards a chargeable transaction that:—
> (a) an amount of tax that ought to have been assessed has not been assessed; or
> (b) an assessment to tax is or has become insufficient; or
> (c) relief has been given that is or has become excessive,
> they may make an assessment (a 'discovery assessment') in the amount or further amount that ought in their opinion to be charged in order to make good to the Crown the loss of tax.
>
> The power to make a discovery assessment in respect of a transaction for which the purchaser has delivered a return is subject to the restrictions specified in paragraph 30."

Paragraph 31(2A) provides that:

> "An assessment of a person to tax in a case involving a loss of tax—
> …
> (b) attributable to a failure by the person to comply with an obligation under section 76(1) …[22]
> … may be made at any time not more than 20 years after the effective date of the transaction to which it relates."

Paragraph 31(2A) was inserted into FA 2003 by FA 2009,[23] which received the Royal Assent on July 21, 2009, and came into effect on April 1, 2011.[24] If, as the Upper Tribunal found, s.75A applied, PBL was required to make a return of its notional land transaction by February 29, 2008. Does para.31(2A) permit HMRC to make an assessment now on that notional land transaction, even though para.31(2A) was enacted almost a year and a half later? It does because, as of the time of writing, para.31(2A) is in force, PBL has failed to make a return of the notional land transaction under s.76(1)[25] and less than 20 years have passed since the effective date of the notional land transaction, namely January 31, 2008.

If HMRC were to make a determination in respect of a notional land transaction under para.25(1), it appears that it could also charge a penalty equal, and in addition, to the tax charged.[26]

[22] Which imposes an obligation on the purchaser in respect of a notifiable transaction to deliver a return.
[23] Sch.51 para.15.
[24] FA 2003, FA 2009 s.99(2) and SI 2010/867 reg.2(2).
[25] Sch.10 para.31(2A)(b).
[26] FA 2003 Sch.10 para.4 and Sch.14 para.8(3).

Therefore, even if PBL had been successful on the Administrative Issue, it is possible that it would have won only a pyrrhic victory.

A deeply flawed decision

Although that may be so, it does not affect the fact that the Upper Tribunal's reasoning on this issue is deeply flawed.

The courts seem to be reluctant to allow taxpayers to escape taxation by reason of HMRC's administrative defaults, although recently there have been some notable examples of taxpayers being successful on such grounds.[27] One cannot help thinking that Morgan J's "instinctive reaction" that the taxpayer ought to be assessed resulted in his ignoring the relevant statutory provisions in the most arbitrary way.

Box A

"75A Anti-avoidance

(1) This section applies where—

(a) one person ('V') disposes of a chargeable interest and another person ('P') acquires either it or a chargeable interest deriving from it,

(b) a number of transactions (including the disposal and acquisition) are involved in connection with the disposal and acquisition ('the scheme transactions'), and

(c) the sum of the amounts of stamp duty land tax payable in respect of the scheme transactions is less than the amount that would be payable on a notional land transaction effecting the acquisition of 'V's chargeable interest by 'P' on its disposal by 'V'.

(2) In subsection (1) 'transaction' includes, in particular—

(a) a non-land transaction,

(b) an agreement, offer or undertaking not to take specified action,

(c) any kind of arrangement whether or not it could otherwise be described as a transaction, and

(d) a transaction which takes place after the acquisition by 'P' of the chargeable interest.

(3) The scheme transactions may include, for example—

(a) the acquisition by 'P' of a lease deriving from a freehold owned or formerly owned by 'V';

(b) a sub-sale to a third person;

(c) the grant of a lease to a third person subject to a right to terminate;

(d) the exercise of a right to terminate a lease or to take some other action;

(e) an agreement not to exercise a right to terminate a lease or to take some other action;

(f) the variation of a right to terminate a lease or to take some other action.

(4) Where this section applies—

(a) any of the scheme transactions which is a land transaction shall be disregarded for the purposes of this Part, but

(b) there shall be a notional land transaction for the purposes of this Part effecting the acquisition of 'V's chargeable interest by 'P' on its disposal by 'V'.

(5) The chargeable consideration on the notional transaction mentioned in subsections (1)(c) and (4)(b) is the largest amount (or aggregate amount)—

(a) given by or on behalf of any one person by way of consideration for the scheme transactions, or

[27] *Bristol v West plc v HMRC* [2014] UKUT 0073 TCC, *HMRC v McCarthy & Stone (Developments) Ltd and Anor* [2014] UK UT 0196 (TCC).

(b) received by or on behalf of 'V' (or a person connected with 'V' within the meaning of section 839 of the Taxes Act 1988) by way of consideration for the scheme transactions.

(6) The effective date of the notional transaction is—

(a) the last date of completion for the scheme transactions, or

(b) if earlier, the last date on which a contract in respect of the scheme transactions is substantially performed.

(7) This section does not apply where subsection (1)(c) is satisfied only by reason of—

(a) sections 71A to 73, or

(b) a provision of Schedule 9."

Box B

The facts

Project Blue concerned the acquisition for development of Chelsea Barracks in London (the "Property"), a £1bn transaction which was financed by Sharia compliant arrangements known as "Ijara financing".[28]

The parties

The parties to the transactions in the case were:

1. the Secretary of State for Defence (the "SSD")[29] which was the vendor of the Property;
2. the appellant company, Project Blue Limited (PBL), which was part of a group (the "PBGHL Group") indirectly owned by the Qatari Ruling Family;
3. Qatari Bank Masraf al Rayan (MAR), a Qatari financial institution specialising in Islamic finance;[30] and
4. Project Blue Developments Ltd (PBDL), another member of the PBGHL Group which undertook the actual development of the site and sold the resulting residential units in the property to the Public.

The Seven Steps

It was common ground that PBL was not subject to SDLT on its acquisition of the Freehold from the SSD because of s.45(3) (sub-sale relief) subject to the application of s.75A.[31]

April 5, 2007: Step 1

PBL contracted to purchase the freehold (the "Freehold") of the Property from the SSD for a total price of £959m payable by instalments (Step 1).

January 29, 2008: Steps 2 and 3

Step 2

PBL sub-sold the Freehold to MAR (Step 2). The consideration for this sale was:

1. US $1,893,353,700 payable in four tranches;
2. the amount of any SDLT liability arising on PBL subject to a maximum of US $75,813,120;
3. an additional amount quantified by reference to the rent payable under the lease to be granted by MAR to PBL under Steps 3 and 7. That amount was US $498,708,180.

The total consideration was US $2,467,875,000. It was accepted by both parties that the sterling equivalent of this amount, presumably on the date of the grant of the lease by MAR to PBL, was £1.25bn.

Step 3

[28] FtT decision at [63].
[29] Referred to in the FtT decision as the Ministry of Defence or "MOD"; FtT decision at [3].
[30] FtT decision at [7] and [8].
[31] FtT decision at [2] and [29].

MAR agreed to grant a lease (the "Superior Lease") of the Property back to PBL for the finance period, which was 999 years and two days. The rent was calculated to give MAR an appropriate return on its ownership of the Freehold (Step 3).

January 31, 2008: Steps 4–7

On January 31, 2008, the following steps took place.

Step 4

MAR and PBL entered into put and call options respectively requiring and entitling PBL to repurchase the Freehold at the end of the finance period (Step 4).

Step 5

The SSD conveyed the Freehold to PBL (Step 5).

Step 6

At the same time as, and in connection with Step 5, PBL conveyed the Freehold to MAR (Step 6).[32]

Step 7

Immediately after Step 6, MAR granted the Superior Lease to PBL (Step 7).

The land transaction returns

On February 22, 2008, five land transaction returns were submitted to HMRC, three in respect of Steps 5, 6 and 7, being the completion of Steps 1, 2 and 3, and two in respect of the two options granted under Step 4. All five of these returns showed no SDLT payable.[33]

Box 9 of the return (LTR1) made by PBL in respect of Step 5, the transfer of the Property from the SSD to PBL in completion of the contract made under Step 1, included a claim for "other relief". The return stated that no SDLT was payable. HMRC amended this return increasing the amount of SDLT payable to £38.4m on chargeable consideration of £959m on the basis that this was the effect of s.75A. Subsequently, the FtT allowed HMRC to amend its statement of case to assert that SDLT of £50m was due on chargeable consideration of £1,250bn.[34]

[32] FtT decision at [14] and [61].
[33] FtT decision at [76].
[34] On the basis that the consideration deemed by s.75A(5) to be given under the notional land transaction arising under s.75A(4) was to be determined by reference to the consideration under the contract under Step 2 that was completed by Step 6.