[2024] UKUT 00242 (TCC)

Case Number: UT/2021/000192

UPPER TRIBUNAL
(Tax and Chancery Chamber)

Rolls Building, London

JUDICIAL REVIEW – challenge to HMRC's refusal to exercise s684(7A) ITEPA discretion to remove obligation on employer to account for PAYE in respect of employee's tax liability on earnings in the form of gilts – HMRC subsequently withdrew defence and sought consent to withdraw from proceedings on basis that a new HMRC officer would make new decision on exercise of discretion – whether HMRC correct to say original action rendered academic – no – whether tribunal should make mandatory, declaratory and quashing orders sought by claimant – no (apart from declaratory relief in respect of misdirections of law that were made out and mandatory order to make a new decision)

Heard on: 20 May and 10 June 2024
Judgment date: 21 August 2024

Before

UPPER TRIBUNAL JUDGE SWAMI RAGHAVAN
UPPER TRIBUNAL JUDGE JEANETTE ZAMAN

Between

THE KING (on the application of) UBS AG

Claimant

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Defendants

and

JONATHAN WOOD

Interested Party

Representation:

For the Claimant:	Sam Grodzinski KC, Marika Lemos, Counsel, instructed by Simmons & Simmons LLP
For the Defendants:	Aparna Nathan KC, Joshua Carey, Sam Way, Counsel, instructed by the General Counsel and Solicitor to His Majesty's Revenue and Customs

DECISION

INTRODUCTION

1. This decision concerns the proper disposal of a judicial review claim in relation to the decision of a public authority (HMRC) in circumstances where the Defendants, HMRC, have committed to make a new decision and sought to withdraw their defence to the original claim but where a dispute remains over whether such withdrawal and the prospect of a new decision means the original judicial review claim is academic and over what, if any, public law remedies it is appropriate for the Upper Tribunal to order.

2. On 22 September 2023, UBS AG **("UBS")** obtained permission to bring a judicial review in relation to HMRC's failure in its decision letter of 3 November 2022 ("**the November 2022 decision**") to exercise its discretion under s684(7A)(b) Income Tax (Earnings and Pensions) Act 2003 ("**ITEPA**" and "**the 7A discretion"**) to relieve UBS from its obligation to comply with the PAYE Regulations in respect of the employment income of the Interested Party, Jonathan Wood, a former senior employee of the Claimant. The amount of the tax liability in respect of the particular remuneration arrangements that were entered into depended on predictions, at a given date, of the future performance of the equity investment team led by Mr Wood. UBS's claim is brought on the grounds that HMRC's decision frustrated the relevant statutory purposes in breach of the principles in *Padfield*, contained misdirections of law, and was *Wednesbury* irrational. UBS argues that for various reasons HMRC ought to have considered it appropriate to exercise the discretion to relieve UBS of the liability to account for PAYE on the relevant income. In particular, UBS argues it would be more efficient to litigate the tax liability in an appeal by Mr Wood against a closure notice into his self-assessment return rather than proceed against UBS: the tax liability ultimately fell on Mr Wood as employee and in the particular circumstances of this case he was best placed to address the relevant valuation question which would determine the amount of the tax liability. Mr Wood supports UBS's position that HMRC should exercise the 7A discretion.

3. The substantive hearing of the judicial review was listed for late May 2024. On 21 March 2024 HMRC sought the Upper Tribunal's consent to withdraw from the case and later also sought a stay of proceedings on the basis a new HMRC officer would make a new decision on whether to exercise the 7A discretion. HMRC argue that meant UBS's existing claim for judicial review became academic. By contrast, UBS argues a live issue remains in respect of which the Upper Tribunal should now grant the public law orders they seek of declaring HMRC's decision not to exercise the 7A discretion unlawful, mandating that HMRC exercise the discretion in its favour and quashing the PAYE determinations HMRC had made in respect of UBS's PAYE liability. For the reasons we explain below, we consider the existing claim is not academic and that it *does* therefore need to be resolved. However, with the exception of some limited relief we disagree with UBS that the public law remedies sought should be ordered.

BACKGROUND

4. Mr Wood was formerly employed as head of UBS's Senior Risk Management ("**SRM**") Equity Investment Team. His remuneration arrangements involved the entering into, in October 2002, of three gilt option agreements between UBS, a UBS EBT and the trustees of a settlement of which Mr Wood was the principal beneficiary. There were three separate agreements for the three calendar years 2003 to 2005. The agreements were intended to reflect the performance of the SRM equity investment team in each immediately preceding calendar year. The performance would determine the amount of a basket of notional investments and the value of that basket would then determine what was delivered to Mr Wood's trust in the form of treasury

gilts when the options came to be exercised. The options were exercised in February 2012, some years after Mr Wood had left his employment with UBS. The gilts which are the subject of this dispute were received in 2016/17 (UBS explained the length of time between exercise and delivery arose because of the time UBS and Mr Wood's trustees took to resolve the valuation of certain notional investments which included illiquid private equity-type investments). Under the employment-related securities provisions of ITEPA, the delivery of gilts would, in broad terms, result in taxable employment income to the extent the market value of the gilts when delivered exceeded the money's worth value of the option when granted back in 2002 and the consideration paid on exercise (in this case £1,000). According to UBS, valuing that money's worth at the time of grant (to inform what amount if any of tax was payable) involves a hypothetical exercise of predicting, as at October 2002 when the agreements were entered into, the future performance of the SRM equity investment team which was managed by Mr Wood.

5. Liability to tax on employment income under ITEPA is ultimately that of the employee. Under PAYE the employee's liability is collected from the employer by imposing obligations on the employer to make deductions from sums paid or else to account for the tax. The delivery of gilts constituted "notional payments" under ITEPA and were accordingly dealt with under Regulation 62 of the Income Tax (Pay As You Earn) Regulations 2003 ("**PAYE Regulations**"). That obliged UBS to deduct tax so far as possible from any other payments made at the same time, or else payments made later in the same tax period. However where, as here – because by the time the gilts were delivered Mr Wood had long since left UBS – the employer was unable to deduct tax from an actual payment, UBS was under an obligation pursuant to Regulation 62(5) to "account [to HMRC] for any amount which the employer is unable to deduct".

6. The 7A discretion which is central to the dispute before us enables HMRC to relieve the employer from its obligation to comply with the PAYE Regulations (which may include removing the obligation from the employer to deduct or, as in this case, account for tax) where an HMRC officer "is satisfied that it is unnecessary or not appropriate for the payer to do so".

7. As regards the amount to which UBS's PAYE obligations applied, the gilts delivered came within the definition of "readily convertible assets" under s696 ITEPA. Section 696 stipulated the amount UBS was required to account for under Regulation 62(5) as the:

> "amount which, on the basis of the best estimate that can reasonably be made, is the amount of income likely to be PAYE income in respect of the provision of the asset".

8. The terms "best estimate" and the reference to the amount of income "likely to be" PAYE income foreshadow the fact it is possible that the amount the employer is liable to account for will not necessarily correspond to the correct amount of tax for which Mr Wood would be liable. There may therefore be a mismatch between UBS's best estimate of Mr Wood's income and the correct amount of income on which Mr Wood is liable to pay tax in respect of the delivery of the gilts. As will be seen, UBS contrasts this with the usual situation where wages or salary are paid and the amount the employer is liable to deduct or account for will be the same as the amount the employee is liable for. If there is a shortfall due to the mismatch HMRC can still collect the correct amount from the employee by issuing a closure notice at the end of an enquiry into the employee's Self-Assessment ("**SA**") tax return for the relevant year. In this case, HMRC have opened an enquiry into Mr Wood's SA return for 2016/17.

9. In October 2018, HMRC informed UBS that they had concluded that the value of the option agreement was considerably less than the value of gilts delivered but did not specify a particular figure. After exchanges of correspondence HMRC arrived at a figure of £22.5

million, subsequently issuing a determination under Regulation 80 of the PAYE Regulations ("**Regulation 80 determination**") to UBS in the amount of £13,439,600.51. (HMRC's cover letter explained they would continue to work with UBS on the valuation but that HMRC had to take action within time limits to protect their recovery position.) UBS has appealed to HMRC against that Regulation 80 determination. HMRC have not produced a view of the matter and the appeal has therefore not been notified to the First-tier Tribunal ("**FTT**").

10. In May 2021 UBS then asked HMRC to make a direction under Regulation 72 of the PAYE Regulations that tax be collected from Mr Wood, not UBS. (Under Regulation 72 HMRC may make a "redirection" to recover amounts (which the employer ought to have deducted but did not) from the employee in circumstances which include those where the employer took reasonable care to comply with the PAYE Regulations and failed to deduct due to an error in good faith.) UBS did not receive a response and issued a judicial review claim challenging HMRC's failure to make the Regulation 72 direction and the lawfulness of the Regulation 80 determination. UBS also appealed HMRC's refusal to make a Regulation 72 direction which resulted in proceedings before the FTT. Those proceedings have been stayed by the FTT by consent pending the outcome of this judicial review (because if UBS were successful in obtaining the exercise of the 7A discretion then the Regulation 72 redirection would become unnecessary). HMRC do not accept Regulation 72 can apply as on its terms it only applies where the employer is obliged to *deduct* tax from a payment made whereas here the relevant PAYE obligation was to *account* for tax.

11. In May 2022 the Court of Appeal gave judgment in *Stephen Hoey & Others v HMRC* [2022] EWCA Civ 656, a case which we will address in more detail later. The issues it dealt with included a judicial review by an employee who objected to HMRC's exercise of the 7A discretion. In rejecting that claim the Court of Appeal set out various propositions regarding the scope of the 7A discretion emphasising its wide nature. On 1 June 2022, UBS asked HMRC to exercise the 7A discretion to relieve UBS of its obligation to account for the best estimate amount under s696 ITEPA. The relevant tax would accordingly then be recovered from Mr Wood instead of UBS.

12. The 7A discretion is provided for as follows:

> "Nothing in PAYE regulations may be read -
>
> […]
>
> (b) as requiring the payer to comply with the regulations in circumstances in which the Inland Revenue is satisfied that it is unnecessary or not appropriate for the payer to do so."

13. The 7A discretion accordingly would, if exercised, have enabled HMRC to relieve UBS from UBS's obligation to account for the best estimate of tax amount if the HMRC officer was "satisfied that it [was] unnecessary or not appropriate" for UBS to do so.

14. On 27 September 2022 Mr Wood wrote to HMRC supporting the exercise of the 7A discretion in UBS's favour and indicating he understood the consequences.

15. On 3 November 2022 HMRC Officer Sue Harper responded to UBS's request as follows:

> "On the basis of the information currently available, I am not satisfied that it is appropriate for HMRC to make a decision in respect of its discretionary power found in section 684(7A)(b) at this time. HMRC would be able to consider the application of this legislation once we have confirmed what liabilities are due.
>
> Your letter seems to base the request on:

> • your view that HMRC's analysis of Regulation 72(5) Income Tax (Pay As You Earn Regulations) 2003 is incorrect and unfair (with which we disagree), and,
>
> • the idea that if HMRC agree UBS AG do not have to comply with their PAYE obligations that that would absolve UBS of any obligation to assist with our enquiries to understand the valuation, and to establish the correct amount of employment income delivered to Mr Wood through the 2005 gilt option agreement, which Mr Wood participated in by reason of his employment with UBS AG.
>
> HMRC's view is, in this case, we still need to agree the valuation and how much tax needs to be paid before we consider collection. We will write to you separately on the information we require to move this matter towards conclusion.
>
> While I note your view that the amount for which Mr Wood is ultimately liable could be recovered more efficiently though an amendment to his self-assessment tax return, this would not be the case for National Insurance Contributions (NICs).
>
> …
>
> HMRC considers that any decision about the application of s684(7A)(b) at this time would not assist the parties in bringing these matters towards conclusion."

16. Whether the above letter, the November 2022 decision, is properly characterised as a refusal *to consider* or as a substantive *refusal to exercise* a discretion is a matter of dispute. However either way the position following the letter remains, as it does now, that HMRC have not exercised their 7A discretion as requested by UBS.

17. With the Upper Tribunal's permission, the parties subsequently amended the original judicial review pleadings. A permission hearing took place in September 2023 following which the Upper Tribunal (Judge Raghavan) granted permission to bring a claim for judicial review on two grounds (set out below) relating to the refusal of the 7A discretion (the Claimant having explained in its skeleton argument for that hearing that it was no longer pursuing its original grounds concerning the unlawfulness of HMRC's decision not to issue a Regulation 72 direction and the issue of the Regulation 80 determination).

18. HMRC later filed detailed grounds of resistance on 3 November 2023 and a substantive judicial review hearing was listed to take place in late May 2024. On 21 March 2024 HMRC filed a Notice of Withdrawal. This sought consent to withdraw stating that HMRC:

> "…intend to give further consideration to the [Claimant's] request to use its discretion under s684(7A)(b) ITEPA 2003 and will issue a new decision once they have done so."

19. The Notice suggested that where a new decision was yet to be made it was inappropriate for the present proceedings to continue. In the further rounds of representations to the Upper Tribunal that ensued HMRC's position was disputed by UBS and the current hearing was duly listed.

UBS'S JUDICIAL REVIEW GROUNDS

20. UBS's judicial review claim, as it now stands, raises the following two grounds detailed below.

Ground 1 – Breach of *Padfield* principle

21. UBS argues that "By declining, in substance, to exercise the power under [7A] to relieve UBS of the obligation to comply with the PAYE Regulations in "appropriate" circumstances HMRC have frustrated the purpose of Part 11 ITEPA" thereby breaching the administrative law principle in *Padfield v Minister of Agriculture, Fisheries and Food* [1968] UKHL 1 that a discretionary power must not be used to frustrate the object of the Act which conferred it.

22. The ground highlights the following matters as relevant:

(1) *Promotion of efficient collection and recovery and Mr Wood's agreement to exercise:* UBS explains the usual position that the employer is in a good, if not better, position to calculate and pay an employee's tax does not apply here and that even if HMRC (referring to the redirection criteria in Regulation 72) were not satisfied UBS took reasonable care and/or made the "best estimate than can reasonably be made" then any discrepancy could be recovered from Mr Wood through HMRC amending his SA return given HMRC's open enquiry into tax year 2016/17. There is, UBS submits, no obvious purpose either in the public interest or in UBS's or Mr Wood's interest by HMRC investigating / litigating on two fronts against UBS and Mr Wood on the same issue in relation to income tax for which Mr Wood is liable. Exercising the discretion would mean the burden of the central dispute would revert to Mr Wood. Given it is he who would owe the tax liability in question, UBS could withdraw the Regulation 80 appeal, HMRC could conclude their s9A enquiry against which Mr Wood could, if advised, appeal. That is particularly so given (i) there are no concerns about Mr Wood's solvency and ability to pay, and (ii) he is in a good position to address the central issues concerning quantification of the tax payable (the hypothetical exercise mentioned above of valuing, as at 2002, the future performance of his equity investment team). The case for exercising the discretion is made even stronger as Mr Wood supports its exercise.

(2) *Gap in scope of Regulation 72* - As mentioned above, Regulation 72 enables HMRC to redirect the liability from the employer to the employee – see [10] above. UBS argues it is inconsistent, anomalous and unfair that the Regulation 72 redirection provisions do not apply where, as here, the obligation is to *account* for tax rather than *deduct* tax, it being happenstance that the payment here, a "notional" payment, is made at a time when no actual payment was made from which UBS could make a deduction.

(3) *Exercising power would be entirely consistent with the purpose of the 7A discretion* As made clear by the Court of Appeal in *Hoey*, HMRC are able to use the 7A discretion as a separate and free-standing tool provided the criteria for its exercise are met. The question is simply whether HMRC are satisfied it would be unnecessary or inappropriate for the payer to comply with the PAYE Regulations.

Ground 2 - Misdirections of law and *Wednesbury* irrationality

23. Under this ground UBS argues the refusal to exercise the 7A discretion contained misdirections in law and/or was *Wednesbury* irrational:

(1) It was a misdirection of law to say HMRC had not confirmed the liabilities were due given the Regulation 80 determination it had made. The quantum of liability was in any case irrelevant to whether the 7A discretion should be exercised (except to the extent there were concerns about collection but that was not identified by HMRC as an issue here).

(2) It was a misdirection of law and/or irrelevant consideration for HMRC to rely on UBS's potential liability to Class 1 Primary or Secondary NICs to decline to exercise the

7A discretion given the NICs liability would ultimately be determined by the amount on which Mr Wood was taxed as employment income.

(3) HMRC were mistaken in their premise that UBS would not have any obligation to assist HMRC with their enquiries in relation to Mr Wood and the 2005 gilt option agreement. HMRC could not reasonably expect UBS to provide assistance beyond explaining how it fulfilled its best estimate obligation, but in any case, HMRC could still compel UBS to provide information in its possession under HMRC's statutory information gathering powers and would not lose the ability to do that by exercising the 7A discretion.

Remedy sought

24. UBS's claim accordingly seeks the following relief:

(1) an order declaring HMRC's decision not to exercise the 7A discretion to have been unlawful;

(2) a mandatory order requiring HMRC within 14 days to exercise the 7A discretion to relieve UBS from its obligation to comply with the PAYE Regulations in respect of the delivery of the gilts to Mr Wood referred to above;

(3) an order quashing the Regulation 80 determination issued to UBS on 24 March 2021; and

(4) costs.

PARTIES' SUBMISSIONS IN SUMMARY

25. HMRC submit that given their commitment to make a new decision by 23 August 2024, the claim has become academic and there is no purpose in continuing the judicial review. They argue the mandatory order the Claimant seeks of requiring HMRC to exercise the 7A discretion in UBS's favour is not something the tribunal has jurisdiction to order (whilst the tribunal could order HMRC to make a decision, it could not compel a specified outcome - the sole authority for making the decision lies with the statutory decision-maker, the HMRC officer). In any case, HMRC say that even if the claim is not academic, public law remedies in a judicial review are a matter of discretion rather than entitlement. The question of whether to grant a remedy usually follows from findings of unlawfulness of the impugned decision, but where the facts have changed in that there is no decision whose lawfulness falls to be determined, it is inappropriate for a remedy to be granted.

26. UBS disagrees that the claim has become academic in that UBS's challenge was not simply that HMRC had failed to consider the discretion but was a challenge to HMRC's refusal to exercise the 7A discretion in UBS's favour. UBS has not obtained the relief it seeks since HMRC have still not exercised the 7A discretion so as to relieve UBS from its PAYE obligations. UBS argues that given HMRC seek to withdraw their defence, the central plank of which was that it was premature for HMRC to exercise their discretion, that must mean HMRC have conceded that point. The appropriate relief is that sought by UBS in its claim form**.** In respect of declaratory relief, HMRC have not advanced any defence. As regards the mandatory order, the fact that it is an officer of HMRC that has been given the statutory discretion is no bar to a mandatory order. It follows that if the 7A discretion is exercised pursuant to the mandatory order sought then UBS would be relieved of PAYE liability and that the Regulation 80 determination should be quashed.

ISSUES:

27. Our discussion section will follow the broad outline below. We will consider whether:

(1) UBS's claim has become academic.

(2) HMRC's application to stay should be granted.

(3) If UBS's claim is *not* academic, the consequences and i) whether UBS's Ground 1 (*Padfield)* and ii) Ground 2 (misdirections of law/ *Wednesbury*) succeed.

(4) What if any public law remedy should be ordered.

(1) Is the claim academic?

28. The general proposition that courts and tribunals should not hear disputes which have become academic is not in dispute. It is illustrated by the facts of *R v Secretary of State for the Home Department Ex p Salem* [1999] 1 AC 450 which concerned the validity of an adverse asylum determination which had in turn led to the applicant's social security benefits being withdrawn. However by the time the matter reached the House of Lords the applicant had been awarded refugee status. His benefits were reinstated and back-paid, and a housing benefit claim (that was contingent on his immigration status) was resolved. The parties agreed no live issue remained relating to the claimant. Lord Slynn described the situation in terms of:

> "…there .. no longer [being] a lis to be determined which will directly affect the rights and obligations of the parties inter se."

29. (In that case, the parties were agreed the dispute had become academic and the issue for the House of Lords was the court's discretion to hear a matter despite it being academic where there was a good public interest reason for so doing. UBS's argument is that its claim is not academic in the first place; it does not seek to argue that the proceedings are academic but nevertheless should be heard because it is in the public interest.)

30. A more recent illustration of a matter that was viewed as academic appears in *R (Raja and another) v Redbridge London Borough Council* [2020] EWHC 1456 (Admin), a case which both parties relied on for various propositions. The issue there was a local authority's ongoing failure to provide interim night-time care of the claimant's two disabled brothers. Fordham J considered (at [63]) that had the defendant decided to continue the interim care provision he had no doubt the substantive hearing would then have become unnecessary: As he put it:

> "It would have been "academic", because of a decision to give the claimants what they were asking for."

31. In line with that Mr Grodzinski KC, who appeared for UBS, is right to say that a claim for judicial review becomes academic when the defendant has in substance done something (whether that involves taking an action or making a decision) giving the claimant in substance the remedies to which it would have been entitled had the claim succeeded. The question ultimately therefore is whether HMRC's action, in withdrawing their defence and committing to make a new decision, means that UBS has "got what it was asking for".

32. The essence of HMRC's case is that UBS's claim only ever concerned HMRC's refusal *to consider* the exercise of the 7A discretion. HMRC argue the challenged decision (the November 2022 decision) did not decide substantively whether or not the 7A discretion should be exercised. Even if it were substantive, it would be a qualified refusal (HMRC highlight the use of the words "at this time" in the first sentence, and that the officer considered it would be appropriate to move on to consider whether or not to exercise once it was "confirmed what liabilities are due"- see extract at [15] above). As Ms Nathan KC, who appeared for HMRC, put it, the decision was not giving a final answer but saying "right now is not the time because we do not have enough information". With HMRC having effectively withdrawn that refusal to consider, by now committing to consider the 7A discretion, UBS's claim, argues Ms Nathan, becomes academic.

33. Thus, it can be seen that the contested issue of whether the proceedings have become academic turns on the parties having a different view on what the claim was asking for. HMRC have construed the claim as if it were a claim that HMRC *consider* exercising the discretion whereas the Claimant says its claim is that in the particular circumstances relied on in its grounds the public law principles require *the exercise of discretion in UBS's favour*.

34. In seeking to answer a criticism by UBS that HMRC, by taking the approach they were of committing to make a new decision, were simply "kicking the can down the road" and avoiding scrutiny of the original decision, HMRC submitted that the open-mindedness shown in their change of approach was a virtue not a subject for criticism. In support HMRC referred us to the following extract from Fordham J's judgment at [19] of *Raja*. The passage is also instructive however in noting the variations on the classic model of judicial review concerning a challenge to a specific public authority decision. Fordham J explained*:*

> "The conventional approach to judicial review, reflected in the design of Form N461, identifies and impugns a specific "decision", with a specific date. This brings focus and discipline, including on the question of whether the claim is sufficiently prompt. Often, the claimant says there is an error of approach in a reasoned decision and seeks a quashing order. But there are lots of variations from this model. A claimant may impugn inaction or a failure or refusal, and seek a mandatory remedy. The conduct under challenge, and the alleged default, may be of a continuing nature. Sometimes a defendant authority is "functus" once a decision has been made and lacks jurisdiction to reconsider. More usually, the defendant public authority is able to review, reconsider and react. It is important that they should. Open-mindedness is a virtue. At the letter before claim stage, and after proceedings are commenced, a defendant may reflect and reconsider. Court proceedings and court hearings, and the costs associated with them, should be avoided if possible. Circumstances can change. There may be further exchanges of information and representations. New requests may be made and new responses written. If a new decision is adverse to the claimant, questions can arise as to whether a claimant needs to, and should be permitted to, amend the claim and grounds to challenge it. The case, for which the court gave permission for judicial review, may be reshaped, narrowed or expanded. Issues can become "water under the bridge" and there can be a lack of practical utility in analysing the past."

35. Although HMRC's depiction of UBS's claim focuses on the November 2022 decision, there can, as set out by Fordham J above, be judicial review claims which go beyond a challenge to a specific decision. While HMRC's submissions have focussed on the interpretation of the November 2022 decision it is important to see that letter in the context of the claim and in particular the grounds upon which permission was granted. We have set out the detail of the grounds above. Permission to apply for judicial review was granted on these grounds without any reservation. Standing back, it can be seen the claim contains elements which capture not only the November 2022 decision but which, as referred to below, go beyond the decision itself.

36. Two broad elements emerge from the grounds setting out UBS's claim: first that HMRC made a "no" decision in respect of the 7A discretion (including a decision not to consider for lack of final liability quantification) that was contrary to the purpose of the statute and for reasons for which were flawed and contained misdirections. The second element is that HMRC ought to have made and are under a continuing obligation to make a "yes" decision given the particular circumstances (litigation efficiency, including Mr Wood's insight into the key valuation question and his support for exercising the 7A discretion, and to make good the gap in the scope of Regulation 72). Thus, as well as challenging what is said to be the flawed basis of the November 2022 decision, UBS is also submitting, in essence, that the *only* permissible

answer in the circumstances here is for HMRC to exercise the 7A discretion in UBS's favour. Plainly UBS's grounds are not simply that HMRC failed to make a decision on the 7A discretion but extend to arguing that their failure to make a decision *in UBS's favour* was unlawful in public law terms too.

37. We therefore agree with Mr Grodzinski's submissions that the claim is not academic. To the extent UBS's claim amounts to saying HMRC should have said "yes" to exercising the 7A discretion – that claim only becomes academic when UBS obtains the decision it seeks. That will only happen when HMRC do say "yes", not when there is simply a possibility HMRC might say "yes". The way in which the November 2022 decision was expressed, it is true, was qualified and not the final word on the matter. It envisaged further consideration being given by HMRC in the future when the liabilities were known. But that is beside the point in so far as UBS's claim concerns HMRC's ongoing failure to exercise the discretion in UBS's favour.

38. There is in any case a good argument, even if the claim were to be restricted to the November 2022 decision, for treating that decision as a substantive "no" decision. The very thing UBS was seeking to prevent by shifting the dispute about the amount of Mr Wood's tax liability – in its eyes a pointless debate in relation to the accuracy of UBS's "best estimate" of the amount of the PAYE income - was the thing HMRC were maintaining needed to be resolved *before* the 7A discretion could be considered. As far as UBS was concerned, the decision in substance amounted to a refusal when it should, according to their view of the public law principles, have been granted and moreover granted at that point in time. And although not the final word, some thought was clearly given by HMRC in Ms Harper's letter to the substance of whether the 7A discretion should be exercised given the various points that were mentioned that indicated that HMRC would not be exercising the 7A discretion in UBS's favour. Ms Harper's letter (understandably) did not simply stop and decline to address any of the matters UBS had raised, as it could have done if it was a refusal to consider.

39. Characterising the decision as amounting to a substantive refusal would also fit with the chronology of events leading up to the November 2022 decision. The Regulation 72 proceedings were stayed in the FTT. Permission in the judicial review proceedings concerning Regulation 72 and Regulation 80 was given for the pleadings to be amended. Those actions contemplated that HMRC would give a substantive response on whether they would *exercise* a 7A discretion not simply decide whether or not to *consider* the discretion.

40. The above analysis (that the claim encompasses HMRC's ongoing refusal to exercise their 7A discretion in favour of UBS) also explains why HMRC's submission that the November 2022 decision must be regarded as having been withdrawn by HMRC is not one that takes the issue of whether the claim is academic any further. That might have been an answer if the decision was simply that HMRC were not going to *consider* the 7A discretion and that refusal to consider was the only decision challenged by UBS, but for all the reasons explained above UBS's claim is a more general and ongoing challenge to HMRC's stance of refusal. Moreover, even if the challenge were to be viewed as centred on the November 2022 decision, that decision, as we have explained, is capable of being construed as a substantive refusal rather than just a refusal to consider. We therefore disagree with Ms Nathan's submission that if we were to consider that the claim remained live then that would create an "unnatural situation" because the proceedings were against a particular decision and that decision no longer existed.

41. The breadth of the claim and that it encompasses a challenge to the failure to exercise the 7A discretion also explains why HMRC's reliance on various authorities does not help.

42. HMRC rely on *TUI UK Ltd v Griffiths* [2023] UKSC 48 (at [41]) for the proposition that courts and tribunals only determine matters in dispute between parties but that does not assist

here because there is a matter still in dispute: whether HMRC must exercise the 7A discretion in UBS's favour. Similarly while HMRC referred to the Administrative Court's analysis in *R(Purnell) v Essex Magistrates' Court* [2015] EWHC 333 (Admin) that a magistrates' court's failure to assess a defendant's means for sentencing purposes had become academic by the time the claim came to be heard (because the magistrates had by that point carried out the means assessment) that is not a good analogy with HMRC's commitment to reconsider the exercise of the 7A discretion. That was a case where the thing the public authority was criticised for failing to do was carried out and the claimant achieved what they sought (the consideration of the claimant's financial means) whereas here HMRC have still failed to exercise the 7A discretion in UBS's favour.

43. Ms Nathan also submitted there was no substantive dispute because all that was achievable was HMRC agreeing to reconsider and HMRC had already agreed to that. She relied on the observations of the Court of Appeal in *R (oao Tesfay) v Secretary of State for the Home Department* [2016] EWCA Civ 415 (which concerned a contested costs issue following settlement of an immigration law judicial review) where (at [57]) Lloyd Jones LJ said:

> "…the courts are not the decision-makers and often in public law the most that can be achieved is an order that the decision maker reconsider on a correct legal basis. That may not lead to ultimate victory for the claimant because the new decision may be a lawful decision against the interests of the claimant. Nevertheless, to achieve an order for reconsideration will often be a substantial achievement. Success in public law proceedings must be assessed not only by what is sought and on which it was opposed but also by reference to what was achievable".

44. At best that is true only in respect of the dispute as to HMRC's refusal to consider the 7A discretion without finalisation of the liabilities. That part of the dispute is arguably academic as now HMRC are to consider the discretion. But in so far as HMRC engaged with the substance of UBS's points there remains a dispute as to whether HMRC's responses contained misdirections and also over whether HMRC were bound in public law terms, in the particular circumstances, to exercise the discretion in UBS's favour. While HMRC maintain the position that this tribunal would not in any case be able to order all of what the Claimant seeks, that assumes (as Mr Grodzinski rightly pointed out) that UBS has already failed in its *Padfield* argument when no determination had yet been made on that point. The reference in the above extract to "<u>often</u> in public law" also indicates that the Court of Appeal's observation was not advanced as an all-encompassing rule. The extract recognises that a court or tribunal could "order that the decision maker reconsider on a correct legal basis". Even if HMRC were correct and the Upper Tribunal were incapable of ordering HMRC to make a "yes" decision, a dispute still remains around the lawfulness of HMRC's continuing refusal of the 7A discretion given the various misdirections of law alleged.

45. HMRC also relied on extracts from the Administrative Court Guide to Judicial Review which at 24.4.3 provides:

> "Where the claim is withdrawn, this leaves the challenged decision in place (unless the defendant has voluntarily withdrawn the decision, thus removing the claimant's need to obtain the relief of the Court).Where the decision is quashed, it will be of no legal effect."

46. HMRC rely on the words in parentheses which suggest that when a decision is withdrawn that removes the need to obtain the relief of the court. However, as Mr Grodzinski explained in UBS's reply, 24.4.3 must be read in the context of 24.4 as a whole which concerns the situation where parties have agreed to end the claim and have agreed a consent order. Here the parties have not agreed to end the claim. 24.4.3 simply recognises that where the underlying

challenged decision is withdrawn that may, but not always will, obviate the need to obtain relief from the court and that in such circumstances the claimant can then voluntarily withdraw the claim. The Guide is not saying that withdrawal of the underlying decision will inevitably obviate the need for relief. Also, where UBS's complaint is the lack of a decision *exercising* the 7A discretion in UBS's favour, even if the decision is to be regarded as having been withdrawn that does not deliver the outcome the Claimant seeks.

47. HMRC cautions against a "rolling judicial review" approach. In *oao Tesfay* at [83] the Court of Appeal, quoting the Court of Appeal in *R(A) v Chief Constable of Kent Constabulary* [2013] EWCA Civ 1706 explained that approach as where the:

> "[court] will not only be adjudicating on the dispute between the parties as to the legality of the original decision made. It will become part of a rolling administrative decision-making process in which a decision by the Secretary of State is followed by challenge, which is followed by new material which in turn is followed by a further decision, with the possible interposition of the court at any or all of these states. Such "rolling judicial review" appears unprincipled. It is also liable to lead to confusion and to sideline the administrative process laid down by the legislature."

48. The context for the Court of Appeal's voiced concern, as explained in its preface to the above extract, was of a "a court becoming too entangled in post-decision material and the later legality of later decisions". That is not the situation which arises here. UBS does not appear to take issue with HMRC's stance that challenging a new decision would need a new claim. Nor is there is any issue regarding "post-decision material". No substantive new information has been sought or raised since the November 2022 decision.

49. HMRC, as mentioned above, say they should not be criticised for being open-minded per *Raja* [19] (see [34] above). Our reasoning should not be seen as deprecating or discouraging the virtue of a public authority being open to reconsidering its position. But it should be recognised that there are also some points of distinction here to the position mentioned in *Raja.* First, the reconsideration envisaged there is predicated on circumstances changing, further exchanges of information and representations. As we have said there is no suggestion that has happened here. The only change here is that HMRC no longer regard as fatal that the liabilities have not been finally determined. In other words the virtue is only in respect of HMRC's point that the 7A discretion could only be exercised once the liabilities were quantified. That no longer presents the roadblock it did. Second, HMRC's approach does not avoid court proceedings but contemplates the possibility, if UBS is not content with the outcome of the new decision, that there might have to be fresh proceedings against a new decision.

50. In conclusion, UBS's claim sought the exercise of the 7A discretion removing its obligation to comply with the PAYE Regulations, and in particular removing the PAYE liability on it – it continues not to have what it seeks. That HMRC have committed to make a new decision does not change that position. The Claimant still has not got what it wanted and the claim would only be academic, as UBS accepts, if HMRC's decision was that the 7A discretion should be exercised.

(2) HMRC's application to stay the current proceedings

51. HMRC had also applied to stay the judicial review proceedings. We raised with Ms Nathan our difficulty in reconciling that application with HMRC's case that the proceedings sought to be stayed were academic. In other words, why allow the proceedings to continue if HMRC were right and they were of no effect? Also, as Mr Grodzinski pointed out, seeking a stay was inconsistent with HMRC's position that if UBS were dissatisfied with the new decision (when made) then it would be open for UBS to challenge that decision by way of a new judicial review. Ms Nathan explained the purpose of the stay as seeking to put the

proceedings into abeyance because they were of no real effect; it was just "a procedurally elegant way of putting [the proceedings] on the shelf". She explained that once the new decision was made it might mean it could be possible to determine the proceedings by consent (for instance if the 7A discretion were granted). HMRC thus confirmed their application for a stay was predicated on their view that the current proceedings were academic and of no real effect. As we have rejected that argument, the application to stay the proceedings falls away and must therefore be rejected.

(3) Consequences if claim is not academic

52. Mr Grodzinski accepted that HMRC's withdrawal of their defence did not mean UBS should automatically be granted the orders for which it had applied, or that they should be "rubber stamped" by the Upper Tribunal. He accepts the burden lies on UBS to make out its claim. (That is consistent with 24.4.1 of Administrative Court Judicial Review Guide where, in relation to consent orders, the Guide indicates that the court "will only approve the order if it is satisfied that the order should be made" and "if not so satisfied" that a hearing date may be set. Parties have to file "a short statement of the matters relied on as justifying the proposed agreed order".) Mr Grodzinski thus accepts the Upper Tribunal must turn its mind to the substance of the grounds. He also argued the withdrawal of defence by HMRC (and failure to provide any justification) is a point towards UBS's case when it comes to assessing the merits (we return to this below).

53. HMRC's position was that the Upper Tribunal did not need to address the substance of UBS's grounds because the November 2022 decision must be regarded as withdrawn by the commitment given to make a new decision. That, HMRC explain, is why they withdrew their defence. In line with what we have said above however, the only aspect of the decision which can arguably be considered to be superseded is HMRC's decision that no decision on the exercise of the 7A discretion could be made until the PAYE liability was quantified. We probed with HMRC what their case was in the alternative if we disagreed the decision had been withdrawn and their analysis that the proceedings were academic but that case concerned the issue of what remedy should be ordered (which we note only falls to be considered once it is established UBS's claim has succeeded). In other words HMRC did not seek to resurrect their defence if they were wrong on the proceedings being academic.

54. We will approach the matter as follows: the November 2022 decision, apart from arguably the prematurity point (i.e. that HMRC could not consider the 7A discretion before the tax liability was finalised), remains amenable to judicial review. We will first consider UBS's case that the only answer in the circumstances regarding exercise of the 7A discretion is that HMRC should say "yes" to it (Ground 1) and then consider the alleged misdirections made in the decision (Ground 2).

55. Although at the outset of these applications there was some dispute around whether the Upper Tribunal should grant consent for HMRC to withdraw their defence (pursuant to Rule 17 of The Tribunal Procedure (Upper Tribunal) Rules 2008) by the end of the hearing we understood the issue of our consent not to have any significance. As mentioned, there was no suggestion that simply by giving consent to HMRC to withdraw its case that meant UBS's case automatically succeeded. We saw no reason in the circumstances to deny HMRC the consent it sought.

i) Ground 1 - UBS's positive reasons for why the only answer could be "yes" to 7A / saying "no" would breach Padfield

56. UBS's case is that HMRC's refusal to exercise the 7A discretion breaches the principle in *Padfield* because it runs counter to the purpose of the statute. In *R (oao Palestine Solidarity Campaign Ltd and another) v Secretary of State for Housing, Communities and Local*

Government [2020] UKSC 16 – at [20] the Supreme Court (Lord Wilson) helpfully summarised the House of Lords decision in *Padfield* as arising:

> "… out of the statutory requirement in England and Wales that producers of milk should sell it only to the Milk Marketing Board. Producers in the south east of England complained to the minister about the price paid to them by the board. Statute provided that, 'if the Minister … so directs', a committee had to consider their complaint. The minister declined to direct the committee to do so. The House of Lords upheld the claim of the producers that he had acted unlawfully in declining to give the direction."

57. Lord Wilson went on to quote Lord Reid's speech in *Padfield* (which was supported by Lord Pearce and Lord Upjohn):

> "Parliament must have conferred the discretion with the intention that it should be used to promote the policy and objects of the Act [which] must be determined by construing the Act as a whole … [I]f the Minister … so uses his discretion as to thwart or run counter to the policy and objects of the Act, then our law would be very defective if persons aggrieved were not entitled to the protection of the court."

58. In relation to the scheme of the legislation, all three of their Lordships in *Padfield* considered the relevant provision was to offer a safeguard mechanism. Lord Reid explained this as "determining whether the scheme is operating or the board is acting in a manner contrary of the public interest". (The factual background was that the South-East region milk producers could not secure the milk purchase pricing change they sought for the prices that applied to their region - but which, because of the restrictions on the total global purchasing budget would have implied corresponding reductions in pricing in other regions - because they could not get a majority on the decision making board and board members would vote in line with their constituent region's interests). Lord Pearce similarly reasoned the investigation process provided for in the legislation was there to "correct the normal democratic machinery of the scheme". The minister's refusal to investigate accordingly frustrated the purpose for which the discretion was conferred rendering, as Lord Reid put it "…nugatory the safeguard" and depriving "…complainers of the remedy Parliament intended them to have."

59. The question of whether HMRC's failure to exercise the 7A discretion breaches the principle in *Padfield* will therefore require an examination of the purpose of the relevant scheme of legislation. The statutory context for the 7A discretion relevant to this case was considered in some detail by the Court of Appeal in *Hoey*. That concerned a situation where client companies ("end-users") had engaged IT contractors who, as part of a tax scheme, were employed by offshore employers. Because the employer was offshore, under the PAYE Regulations the obligation to deduct in respect of employment income fell on the end-user. HMRC took the view the 7A discretion *should* be exercised (with the result the employee was to pay the tax) considering that it was inappropriate for the end-users to comply with their PAYE obligation to account for the tax. Amongst the considerations was that the end-users did not, and could not have been expected to, know of the employment arrangements with offshore employers which the IT contractors had entered into. In considering the IT contractors' claim that HMRC's decision to exercise was unlawful in public law terms the Court of Appeal (Simler LJ as she then was with whom the other LJJs agreed) addressed a number of propositions concerning the scope of the 7A discretion. Addressing the challenges that HMRC ought to have used the specific redirection regulations in the PAYE Regulations (including Regulation 72) rather than the general 7A discretion, and by not doing so this subverted the taxpayer protections those offered, Simler LJ explained at [70]:

> "These provisions have overlapping aims and overlapping applications. The redirection regulations are plainly not exclusive; nor are the PAYE Regulations the exclusive machinery for assessment and collection of tax in respect of an employee's self-employment income. This is not a case of specific legislation displacing a general provision. The scheme of this legislation enables HMRC to use the7A power granted in primary legislation as a separate and free-standing tool provided the criteria for its exercise are met."

60. Simler LJ went on to explain the breadth of the power:

> "[72] Returning to the language of the 7A power, it could not have been expressed more plainly and clearly. There is no expressed limit to the circumstances in which an HMRC officer can decide that it is inappropriate for the payer to comply with obligations under the PAYE Regulations. The provision recognises that, despite the detail of the PAYE Regulations, HMRC may form the view in the circumstances of a particular case, that it is not appropriate to expect an end user (or other employer) to comply with the deduction and/or accounting obligations in the PAYE Regulations."
>
> [73] As Mr Grodzinski [*counsel for HMRC*] submitted, sections 684 (7A)(a) and (b) are dealing with different aspects of the same problem – a situation where for whatever reason the payer ought to be relieved of its obligations under the PAYE machinery. Certain outlier situations, such as short-term or casual employment, are likely to fall within subsection (a). Since subsection (b) was also enacted, this provision must have an additional purpose and cater for different situations. Given its broad terms, it was clearly intended to apply whenever it is considered appropriate to relieve an employer from PAYE requirements and is not limited to outlier situations as Mr Mullan [*counsel for the applicant*] contended. Its focus is inevitably on the payer, and neither subsection makes any reference to the payee. This is unsurprising in circumstances where exercise of the 7A power has no impact whatever on the underlying liability to tax of the payee recipient of the PAYE income, which remains undisturbed.
>
> [74] The question for the officer in a subsection (7A)(b) case is simply whether, in the circumstances of the case, he or she is satisfied that it would be unnecessary or inappropriate for the payer to comply with the PAYE Regulations. Two points follow from the plain words of the provision. First, because the words "unnecessary" and "not appropriate" are used in the alternative by the drafter, it is clearly contemplated that an officer may be satisfied that it would be inappropriate to expect compliance with the PAYE Regulations, even where compliance is otherwise necessary. Secondly, by empowering the officer to decide what is appropriate, Parliament has decided that it should be within the discretion of the officer to decide when compliance with the PAYE Regulations is not appropriate. Nonetheless, this is not an untrammelled power. It must be exercised in accordance with well-established principles of public law, including the obligation to act *Wednesbury* rationally and the *Padfield* obligation not to act inconsistently with the purpose of the legislation.

61. From the above extracts it is thus clear that the 7A discretion is*:*

(1) broad and not limited to outlier situations; and

(2) must be exercised in accordance with public law principles including *Wednesbury* rationality and the *Padfield* principle.

62. In addition, other propositions Mr Grodzinski highlights are that liability to tax on employment income is always that of the employee (at [67]), that Parliament has given HMRC freestanding power to decide to disapply the PAYE Regulations whenever they consider the employer's compliance is either unnecessary or inappropriate (at [70]), and that the power may be exercised prospectively and retrospectively (at [82]).

63. Of particular relevance to UBS's case is the Court of Appeal's explanation that there is no policy that tax always falls to be collected first or at all from the employer. That proposition appears in the following passage at [68] rejecting various submissions of the claimant employee there, including that the core purpose of the PAYE code was to ensure the primary obligation to pay for and account for PAYE lay with the person paying and not the employee:

> "Nor is there anything in ITEPA suggesting that the purpose of the PAYE Regulations is to forgive the employee in respect of his or her own income tax liability when PAYE has not in fact been deducted or accounted for by an employer or deemed employer. There is no policy discernible in the PAYE Regulations by which the tax in relation to an employee's PAYEincome always falls to be collected from the employer. To the contrary, the availability of directions under the redirection regulations (including regulations 72F and 81) show this to be incorrect."

64. The cornerstone of UBS's case is that HMRC were wrong not to have concluded that it was inappropriate to subject UBS to the obligation to account for PAYE and to have to agree the relevant valuation issues with HMRC given the inefficiency that led to litigating against UBS in respect of tax for which Mr Wood was liable. Any discrepancy between the "best estimate [of tax] than can reasonably be made" and the amount of tax for which Mr Wood was liable could be recovered from Mr Wood through HMRC amending his SA return given HMRC had an open enquiry into his SA return for the relevant tax year. The case for exercising the 7A discretion was even stronger as Mr Wood supported its exercise and, being a person of substantial means, no concerns had been raised by HMRC over his solvency and ability to pay. Exercising the 7A discretion would not, as HMRC suggested, open the floodgates to employers more generally simply electing not to apply PAYE. In the general case, there would not be any potential mismatch between the amount due from the employer under the PAYE Regulations and the employee's tax liability and even in respect of "mismatch" cases the facts of this case were unique in that the employee rather than the employer was best placed to debate the right amount of tax under s476 ITEPA.

65. We consider that the breadth of the 7A discretion, as explained in *Hoey*, means it is relatively straightforward for UBS to establish that the features it relies on can at least be potentially relevant to a consideration of the 7A discretion. If a decision-maker were to accede to exercising its discretion on the basis of them, it would, we think, be difficult to say that such decision was contrary to the purpose of the legislation. That does not, however, take UBS's case as far as it needs to go which is to establish that the *only* decision open to HMRC in the circumstances is to exercise the discretion in UBS's favour. Just as the breadth of the discretion available to HMRC helps explain how a wide range of factors might be relevant to the necessity or appropriateness of an employer's compliance with the PAYE Regulations, so too the breadth makes it correspondingly difficult to argue HMRC effectively had no discretion but to grant the exercise sought by UBS. The factors relied upon by UBS, either alone or together, would need to be elevated to ones which are determinative of a single potential outcome.

66. As made clear in *Hoey* (at [73]), the focus of consideration is on the payer, here the employer, and the question of whether it is unnecessary or inappropriate for UBS to comply with the PAYE Regulations. PAYE is a mechanism to collect tax due from the employee.

Against that backdrop the purpose of the 7A discretion is to enable HMRC to relieve compliance from such obligations where they consider it is unnecessary or inappropriate.

67. As Mr Grodzinski's submissions pointed out, it is plain from *Hoey* that there is no policy that the employer is always liable (see [63] above) however the key word in that proposition that should not be overlooked is "always". The fact there is no policy that tax always falls to be collected from employer is not inconsistent with a general policy that is made subject to exceptions through the operation of the 7A discretion or, where the relevant conditions are met, the redirection regulations. It is not impermissible, nor inconsistent with the breadth of the 7A discretion, to start from the position that the payer is the person liable to pay or account for the employee's tax as long as HMRC remains open to exercising the discretion in those circumstances when it is not necessary or inappropriate to expect compliance with the PAYE regulations. It is inherent in the analysis in *Hoey* that the focus should be on the necessity or appropriateness of the payer's compliance that it contemplates a starting point (which may of course be departed from) of the payer being expected to comply with the PAYE Regulations.

68. The efficiency of avoiding litigation on multiple fronts by exercising the 7A discretion is advanced in this case as one such significant reason why compliance is inappropriate. Mr Grodzinski points to [80] of *Hoey* for support for the proposition that avoiding litigation on multiple fronts against employer and employee was a relevant concern. In that paragraph the Court of Appeal noted HMRC's witness' evidence as to why a route of pursuing a Regulation 80 determination against the end-user was not taken. The evidence explained that HMRC would have been forced to engage in potentially costly and lengthy litigation against end-users and that if unsuccessful HMRC could then pursue the tax from the claimant employee through a direction under Regulation 81 of the PAYE Regulations. If successful the evidence mentions the end-user could pursue claimants for restitution of tax paid. Similarly UBS argues it is not necessary or appropriate to prolong the debate with UBS over the PAYE liability through an appeal by UBS against the Regulation 80 determination when HMRC will still ultimately need to decide the correct amount of tax owed by Mr Wood.

69. We agree this is at least a relevant factor but it appears to us from the treatment of the point in *Hoey* that its relevance should not be overstated and does not point to the factor being determinative. The Court of Appeal's analysis at [80] was part of a general explanation dealing with the claimant's argument there regarding the redirection tools at HMRC's disposal and why it was permissible, in the Court of Appeal's view, for HMRC not to use such tools. Part of that explanation was that the end-users were not and could not have been expected to have known of the offshore employment arrangements which rendered the end-user subject to PAYE. The end-users would thus effectively have had a reasonable basis for saying they did not know and could not have been expected to know that the PAYE obligation applied to them. The Court of Appeal's implicit endorsement of HMRC's evidence was not based exclusively on efficiency. It simply shows costs / efficiency factors may be reasons why the *redirection* tools HMRC had at its disposal (which have certain criteria and appeal rights which the claimant was arguing would be short circuited by the exercise of 7A discretion) did not have to be used. However that does not necessarily mean such factors are reasons why the 7A power *must* be exercised.

70. Central to the point on inefficiency was that, unlike the usual situation that arises when wages and salary are paid subject to PAYE and match the employee's ultimate liability, here there was a mismatch. In response to our observations that such mismatch was a structural feature of the regime pursuant to the reference to "best estimate" in s696 that arose in relation to the sorts of assets in issue here ("readily convertible assets"), Mr Grodzinski pointed out it would not always be the case that the two amounts would be different. He also emphasised Mr Wood's unique position to answer key questions given Mr Wood's role as head of the SRM

equity investment team as predictions as to that team's performance would underlie the valuation of the gilt option at the time it was granted. That would not always be true in a s696 "best estimate" case. The current case, Mr Grodzinski submitted, was an outlier situation (which thus clearly justified the exercise of the 7A discretion given the Court of Appeal in *Hoey* had made clear there did not even need to be an outlier situation in order for the relevant 7A conditions to be considered met).

71. On reflection we can see that the fact that even if a mismatch is in some sense "hard-baked" into the regime, that would not necessarily preclude the exercise of the discretion. In *Hoey* it could equally be said the end-users had an obligation under the PAYE regime to account despite them not knowing of the offshore employment arrangements but the Court of Appeal nevertheless held the exercise of the 7A discretion to be lawful. However the fact a reason, here the possibility of a mismatch, could sustain the exercise of 7A does not establish that reason would compel HMRC to exercise the 7A discretion in the employer's favour. If anything the fact primary legislation has seen fit to acknowledge that an employer paying a readily convertible asset will be accounting for a "best estimate" of the amount "likely to be" payable and the insertion of a standard of "reasonable care" points to some concessions already being made to what is expected as regards the obligations on the employer which stand in contrast to a bare obligation to pay the amount of tax due. The way in which the obligation has been designed, with protections built in, does not suggest one should be too quick to consider compliance as unnecessary or inappropriate.

72. As regards Mr Wood's unique position to give evidence on the valuation question which will inform the relevant tax liability, we do not know enough about what evidence would be potentially available in any appeal against the Regulation 80 determination regarding the "best estimate" amount or the tax liability in any appeal against a closure notice, to accept that it is correct that Mr Wood would be the "best person" to speak on it, rather than simply a witness able to give relevant evidence. The valuation question is not subjective but an objective question of what the likely investment performance of the SRM equity investment team was when viewed at 2002. However even on the assumption he was, we cannot see why, as a matter of principle, the fact that evidence is given by him should determine that his litigation should take precedence – in other words if his evidence is the best evidence on the issue that will be true irrespective of the witness's role as a party in their own case as opposed to in another's case. His ability to give evidence on the valuation issue is in our view a neutral factor. Although we would not rule out that HMRC could as a matter of their own strategic preference consider Mr Wood's insights would best be addressed in a closure notice appeal they would not be compelled to do so. The fact Mr Wood has particular insight into the issue also does not mean UBS is any less able to comply with its best estimate obligation and it is certainly not a factor which compels the exercise of the 7A discretion.

73. Mr Wood's own support for the exercise of the 7A discretion and his ability to pay are similarly, in our view, factors which could be taken account of but which do not compel the exercise of the discretion. As regards the relevance of Mr Wood's views, Mr Grodzinski took us to [71] of *Hoey* submitting the views of the employee are relevant hence the reason why HMRC must give the employee a right to make representations. However we are not sure that necessarily follows from the reasoning and risks overstating the relevance of the employee's views (when the focus as stated above is on the payer's compliance). The Court of Appeal was merely highlighting that the employee is not in a worse position than following a redirection regulation in terms of notice because they would get *notice* via a request to them for representations. While that indicated the employee's views may potentially be relevant and we can see how the employee's support might well give HMRC comfort if it decided to exercise the discretion, the employee's support would not compel such exercise.

74. UBS also argue that, if it is correct that the power of redirection under Regulation 72 (which may apply where the employer has taken reasonable care to comply with the PAYE Regulations and the error in not deducting is made in good faith) is not available to redirect liability to the employee (because it only applies where there is a failure to *deduct* the correct amount as opposed to a failure to *account* for the correct amount) then that gives rise to an inconsistent, anomalous and unfair result given "the happenstance of a payment being a "notional" payment made at a time when no actual payment was made". (It will be recalled that the employer can only make a *deduction* where an actual payment is made either at the same time or in the same tax period as the notional payment).

75. We do not rule out that HMRC could choose to use the 7A discretion in such circumstances, but it does not follow that the 7A discretion *must* be used as a matter of course where the Regulation 72 criteria would otherwise be met still less that it should be exercised in UBS's case. The focus, as explained in *Hoey*, is on the necessity or appropriateness of the employer's compliance which will depend on the particular circumstances of the case. The limitations of Regulation 72 to deduction scenarios does not explain why it is unnecessary or inappropriate for UBS to comply with its obligation to account. It should be noted that the Court of Appeal in *Hoey*, where the facts involved notional payments too, made a point of distinguishing the duty to deduct and account and highlighted the limitation of the redirection regulations to deduction scenarios. If it were thought such limitation of scope was so anomalous or unfair or inconsistent that it *required* exercise of the 7A discretion one might have thought that that would have elicited comment. The gap in Regulation 72's scope would have presented reason enough to justify HMRC's exercise of the 7A discretion in that case such that the Court would not have needed to engage with the disputed issues regarding the relevance of the end-user's lack of knowledge of the offshore employment arrangements.

76. UBS also argues that exercising the 7A discretion would be entirely consistent with the purpose of the discretion. Again we do not rule that out but the point is insufficient to make out UBS's ground of claim by establishing that refusal of the discretion would be inconsistent with the object of the statute.

77. We address whether the cumulative effect of the factors which can be taken into account would nevertheless mandate the exercise of 7A below at [87].

ii) Ground 2: Misdirection of law / *Wednesbury* irrationality

Misdirection that exercise of 7A premature because quantum of liability not established

78. UBS's case is that HMRC misdirected themselves by regarding exercise of the 7A discretion as premature because it could not be addressed until UBS's PAYE liability had been confirmed. First the Regulation 80 determination HMRC made was final and second quantum was in any case irrelevant (except to the extent there were collection concerns but that was not apparent here).

79. While HMRC's skeleton says compliance with the s696(2) obligation is a matter which may be taken into account, a proposition with which we agree, we note the November 2022 decision went further by in effect saying that HMRC were not even going to consider the 7A discretion without knowing the s696(2) figure. That refusal to consider was wrong in our view. The crux of the issue here is *who* to have the debate over quantification of tax liability with – will it be UBS and Mr Wood in potentially two sets of proceedings or would it just be the employee, Mr Wood? In agreement with UBS, in principle there is no reason why one needs to know the amount of the best estimate liability before the issue of the 7A discretion can be considered because that then begs the question by assuming the debate over quantification is to be had first with the employer. We also agree that to the extent finality was sought then there was sufficient finality for HMRC's purposes that arose in the Regulation 80 determination

which they issued. Barring alteration by agreement or on appeal that determination would specify the final figure.

80. However none of this should be taken as suggesting that the quantum of tax at issue is not at least a relevant factor. It will obviously be so for instance when it is zero and there is nothing which then turns on the exercise of 7A but its amount might also be relevant to the extent there were concerns around differing prospects of recoverability as between the employer and employee. There is no indication that is a concern in this case but it could be in others.

81. We would therefore agree this aspect of HMRC's decision was a misdirection and accordingly to that extent unlawful.

Misdirection and/or irrelevant consideration as to interaction between NICS and 7A

82. This point concerns the way HMRC responded to UBS's point that it would be more efficient for HMRC to deal with Mr Wood rather than UBS in relation to Mr Wood's tax liability. HMRC's response was that exercising the 7A discretion would not be able to remove UBS's liability for NICs. In other words HMRC were saying exercising the 7A discretion would not realise the benefits they understood UBS hoped for namely extricating itself from the dispute. The November 2022 decision explained this as follows:

> "To date we have not discussed NICs directly, however where there is a chargeable event under section 476 ITEPA 2003 this would also be remuneration derived from employment under section 4(4)(a) Social Security Contributions and Benefits Act 1992 (SSCBA 1992). It therefore attracts a liability to Class 1 National Insurance Contributions. Where, as in this case, the securities are also 'readily convertible assets' both the income tax and the NIC are accountable via PAYE.
>
> UBS AG, as the secondary contributor, is liable for the Class 1 Secondary NICs arising from any gain on the securities option, and is also liable in the first instance to pay any Class 1 Primary NICs under paragraph 3(1) of Schedule 1 to SSCBA 1992. Unlike for tax, neither Regulation 72(5) of the PAYE regulations 2003 nor section 684(7A)(b) ITEPA 2003 can apply to remove the liability to pay National Insurance Contributions from the secondary contributor.
>
> For the avoidance of doubt, on the basis of the information seen to date I do not consider that the conditions of Regulation 86 SSCR 2001 would apply here either. Therefore, we consider UBS AG and Mr Wood need to work with HMRC to agree the valuation and apportionments affecting the amount of tax and NICs due, in particular as UBS AG will be liable to pay any NICs due. HMRC considers that any decision about the application of s684(7A)(b) at this time would not assist the parties in bringing these matters towards conclusion."

83. UBS argues HMRC's response that UBS remained liable was a misdirection in that UBS's NICs liability would, because of the relevant legislation, be dependent on Mr Wood's ultimate employment tax liability. It would thus, contrary to HMRC's assumption, realise the efficiency UBS sought. (UBS explains that the NICs charge in relation to securities options arises under s4(4)(a) of the Social Security Contributions and Benefits Act 1992 ("SSCBA"). This provides that "there shall be treated as remuneration derived from an employed earner's employment" for the purposes of s3 of the SSCBA, the amount of any gain calculated under s479 ITEPA that counts as the employment income of the earner under s476 ITEPA, reduced by any amounts deductible under ss480(1) to (6) ITEPA in arriving at that amount). There is no equivalent to the s696 "best estimate" amount.

84. We agree with UBS that HMRC's analysis proceeded on a misdirection. To the extent the efficiency arguments pointed in favour of exercising the 7A discretion then the fact the 7A discretion would not remove the NICs liability from UBS did not detract from the efficiency savings advanced. UBS's NICs liability will therefore be determined by the amount on which Mr Wood is ultimately taxed as employment income, irrespective of the amount of income tax that UBS accounted for, or should have accounted for, on the basis of the best estimate which could reasonably be made.

Mistaken premise that UBS would not and/or could not be compelled to provide information relating to HMRC's enquiries.

85. UBS's claim maintains that HMRC's assertion in its November 2022 decision that UBS would not have any obligation to assist HMRC with the enquiries in relation to Mr Wood and the 2005 gilt option agreement is incorrect. Our first observation is that it is not clear to us that the letter discloses the assertion advanced. Read in the round the point being made is that HMRC understood UBS's position to be that if the 7A discretion were to be exercised UBS would then bow out but we do not read the letter as agreeing with that position. On the contrary, the point the letter goes on to make is that even if the 7A discretion were exercised UBS would still need to be involved because of UBS's NICs liability. We do not therefore consider HMRC were making the assertion said to be a misdirection (and there is no suggestion it was doing so from Ms Harper's witness statement). We note however that HMRC's position at the permission hearing was to defend this point on the basis the assertion was made but that HMRC were right to be concerned about UBS's lack of engagement if the 7A discretion were exercised. If we are wrong on this (i.e. there was an assertion by HMRC that they were concerned exercising the 7A discretion would mean UBS no longer being involved) or if the view is taken that despite withdrawal of their defence HMRC are to be held to what is effectively a concession on their part that the assertion was made), then we would agree with the Claimant that HMRC's assertion would be incorrect and a misdirection. As UBS points out, if UBS had relevant information in relation to the liability issue, there would be a mechanism through Schedule 36 Finance Act 2008 to get UBS to provide that in Mr Wood's closure notice proceedings if need be. It would not be a factor which pointed against exercising the 7A discretion.

86. To the extent we have found there to be misdirections of law it follows that those misdirections were also points that were reached which were irrational in *Wednesbury* terms i.e. they were points which no reasonable decision maker could have reached.

Does the combination of above factors mean that HMRC are bound to exercise the 7A discretion?

87. The above misdirections indicate HMRC should reconsider the issue of whether to exercise the 7A discretion. However none, in our view, whether taken individually or together *require* that HMRC's decision must be to exercise the 7A discretion in UBS's favour.

88. The prematurity misdirection explains why HMRC were wrong to proceed on the basis that they ought not even consider exercising the discretion. The NICs liability and UBS information misdirections ought not to have detracted in the way they did from HMRC's analysis of the positive reasons why UBS was arguing the 7A discretion should be exercised, but they were not reasons in themselves for *exercising* the 7A discretion.

89. In our judgment the positive reasons (efficiency and the Regulation 72 anomaly) advanced, while capable of sustaining an exercise of the 7A discretion do not individually or together compel its exercise in UBS's favour. In summary going back to *Padfield* and *Hoey* we remind ourselves what this power is for. Parliament means to allow HMRC broad discretion to relieve compliance from the PAYE Regulations where an HMRC officer considers it

unnecessary or inappropriate. The backdrop is the collection machinery of the employee's tax liability. While there is no policy of *always* collecting from the employer, that does not rule out a starting point of collecting from the employer. The focus is on employer's compliance. While we recognise it would be open for the officer to decide that it was appropriate in the circumstances to exercise the discretion, we are not persuaded they would be bound to exercise the discretion and that HMRC would thereby breach the principle in *Padfield* or be *Wednesbury* irrational if they did not.

90. Accordingly, despite having identified various misdirections, which will necessitate a new exercise of discretion, we are not satisfied that UBS has met the burden on it to show that HMRC's refusal was unlawful in the sense that the *only* decision it could lawfully have reached was to grant the discretion.

91. Mr Grodzinski sought to persuade us of the significance of HMRC not advancing the factors and reasons that would justify saying "no" to the 7A exercise (as a consequence of HMRC withdrawing its defence to the claim) but we do not think this changes the above analysis in circumstances where we are not satisfied UBS has met the burden on it to show HMRC were bound to grant the 7A discretion. Similarly we do not draw anything of significance from HMRC's omission to plead in defence to the argument that the claim should fail because the outcome of any decision is highly likely to not have been substantially different (under s16(3C) onwards of the Tribunal Courts and Enforcement Act 2007 being the analogous provisions to those set out in s31(3C) Senior Courts Act 1981). That is consistent with HMRC's view that no assumptions can be made about what the new decision-making officer will decide when the matter is reconsidered. Although we have concluded HMRC would not be bound to exercise it in UBS's favour as a matter of public law, given our view that it would in principle be open to the decision-maker to grant the exercise of the 7A discretion, we consider HMRC are right not to suggest the new decision will inevitably be the same.

(4) Remedies

92. As both parties acknowledge, the question of what remedies, if any, the tribunal should order is a matter of discretion.

93. We have identified misdirections of law were made in respect of prematurity and as regards the relevance of NICs to UBS's case on litigation efficiency.

94. We see no reason not to declare that HMRC's decision was unlawful in those identified respects.

95. As regards mandatory relief, given the misdirections, we consider HMRC ought to consider the matter afresh. Although HMRC have already committed to making a new decision we consider it is appropriate to mandate that HMRC do so, to make clear that the new decision takes account of the misdirections identified by our declaration. We therefore make a mandatory order requiring HMRC *to consider* whether to exercise the 7A discretion to relieve UBS from its obligation to comply with PAYE Regulations in respect of the delivery of the gilts to Mr Wood referred to. We anticipate that HMRC's decision maker will also want to reflect on the contents of this decision and recognise that the decision is being issued in the summer leave period but consider that a deadline of two months from the release date will be ample and so order. The issue of whether to make an order mandating HMRC to grant the 7A discretion does not arise as UBS has not met the burden on it of showing that the circumstances advanced compelled a positive 7A decision under the principles of public law it relied on. Neither, for the same reason, does the issue of quashing HMRC's Regulation 80 determination arise. That determination remains in place. Similarly although it was a matter of dispute as to whether we would in any case have had jurisdiction to mandate the exercise of 7A if UBS had

been successful on its *Padfield* ground we do not need to and accordingly do not express a view on that issue.

CONCLUSION

96. The Upper Tribunal consents to HMRC's application to withdraw.

97. HMRC's application to stay the proceedings on the basis the proceedings are academic is refused.

98. UBS's claim against HMRC's refusal to exercise the 7A discretion succeeds in the following respects:

(1) HMRC misdirected themselves in regarding the lack of quantification of liability as a bar to considering the 7A discretion.

(2) HMRC misdirected themselves in assuming the fact UBS remained liable for NICs detracted from UBS's argument that exercising the 7A discretion would be more efficient.

99. UBS's claim, that HMRC's failure to exercise 7A in its favour was in the circumstances unlawful under *Padfield* / *Wednesbury* irrationality, is dismissed.

100. The remedy ordered is:

(1) a **declaration** that the November 2022 decision was unlawful insofar as it made the misdirections of law in [98] above.

(2) a **mandatory order** that HMRC, within two months of the release date of this decision, make a new decision on whether to exercise the 7A discretion which takes account of the misdirections of law identified above.

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UPPER TRIBUNAL JUDGE SWAMI RAGHAVAN
UPPER TRIBUNAL JUDGE JEANETTE ZAMAN

Release date: 21 August 2024