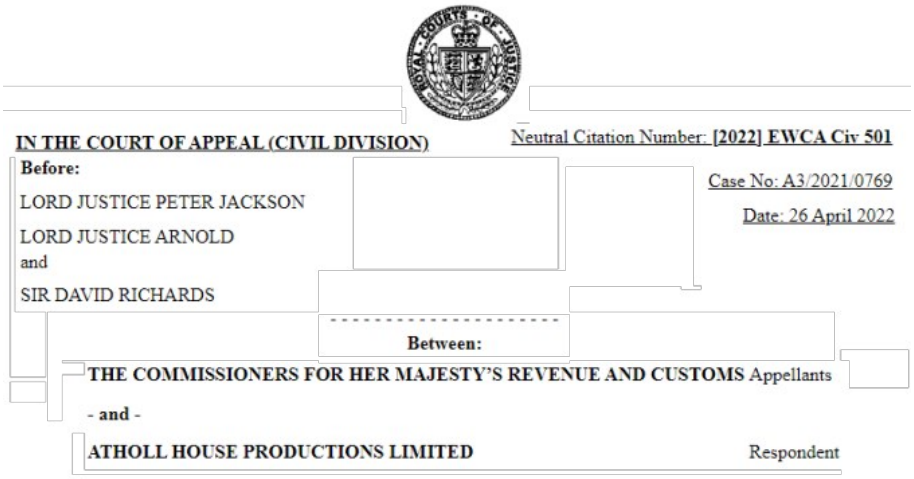
BREAKING NEWS: Major loss for HMRC after Atholl House Court of Appeal ruling



IN THE COURT OF APPEAL (CIVIL DIVISION)

Neutral Citation Number: [2022] EWCA Civ 501

Before:

LORD JUSTICE PETER JACKSON

LORD JUSTICE ARNOLD

and

SIR DAVID RICHARDS

Case No: A3/2021/0769

Date: 26 April 2022

Between:

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS Appellants

- and -

ATHOLL HOUSE PRODUCTIONS LIMITED Respondent

The Court of Appeal has published its decision for the IR35 case of HMRC v Atholl House Productions Limited, involving presenter Kaye Adams. Whilst the case will be remitted to a lower tribunal for the final decision, HMRC lost on their primary ground of appeal, signalling a major blow to their longstanding view of how they and others should determine IR35 status.

This clarification by the Court of Appeal is a significant victory for freelancers who are in business on their own account. HMRC will now need to update their IR35 guidance and revisit all their existing IR35 litigation against freelancers, especially in the media.

Dave Chaplin, who attended all of the tribunals in this case, said: "HMRC's primary ground of appeal, in this case, sought to radically change the law around employment status and force IR35 status determinations away from the written statute and down a narrow path. Their now-rejected view would have inadvertently resulted in many freelancers being considered 'employed for tax purposes' despite clear evidence of being in business on their own account."

A statement released exclusively to ContractorCalculator by Kaye Adams stated: "I am very encouraged that the Court of Appeal has confirmed that a freelancer's career should be considered in its entirety when considering its status under the IR35 legislation. Many of my fellow freelancers will be enormously cheered by this conclusion."

What did the Court of Appeal say in Atholl House?

The Atholl House hearing was based on two grounds of appeal by HMRC, the first one of which took up the vast majority of the time at the court.

HMRC had claimed that the Upper-tribunal had erred in law in its interpretation and/or application of the third stage of the Ready Mixed Concrete status test. Ready Mixed Concrete (South East) Ltd v Minister for Pensions and National Insurance [1968] ("RMC") is the bedrock common law which describes a much-used framework for assessing employment status.

RMC describes key areas to be considered, including personal service, mutuality of obligation, control and then 'other factors'. Other factors sit in what's referred to as the "third limb", which is to be used to establish whether there are any factors that might differ from the conclusion drawn after personal service, mutuality, and control are considered. One such factor in this stage is being "in business on own account" ("IBOOA").

Chaplin says: "In many cases for freelancers, the stages of personal service and control could fail to reach any meaningful conclusion, especially where someone is hired to do a specific task and only paid for work done. The 'sufficient framework of control' argument can often be irrelevant because there is always some element of control present in many cases, but that doesn't mean the relationship is one of master/servant. Therefore the 3rd limb is of paramount importance and should not be discounted."

At the hearing, HMRC tried to argue that RMC and Hall v Lorimer ("HvL") were different tests, that HvL should not be considered, and that IBOOA should only be given little weight when considering whether a prima facie conclusion of employment could be displaced. The Court of Appeal unanimously rejected HMRC's view. The four paragraphs [168 to 171] by Lord Justice Arnold perfectly summarise the correct principles:

> - *"Firstly, …, it cannot be right to treat RMC and Hall v Lorimer as representing two separate tests which may be applied by the court or tribunal potentially leading to different results. Both approaches have a common core: mutuality of obligation and a right of control are necessary, but not sufficient, conditions for a contract of employment, and if those conditions are satisfied it is necessary to go on to consider a range of other factors."* [Para 168]
> - *"Secondly, …, if mutuality of obligation and a right of control are present, then there will inevitably have to be one or more factors pointing the other way if the court or tribunal is to conclude that the contract is not one of employment; but that does not mean that the court or tribunal should divorce its evaluation of the other factors from its assessment of the first two conditions. In particular, it may well be relevant to take into account the extent of the control exercisable by the alleged employer."* [Para 169]
> - *"Thirdly, …, the answer to the question as to what limit there is on the factors to be taken into account is supplied by basic principles of contract law. In a case like the present, the issue is one of interpretation of a written contract (or, to be more precise, a hypothetical contract derived from a written contract with the alteration of the identity of one of the contracting parties). That contract, like any other agreement in writing, should not be construed in a vacuum, but in the light of the admissible factual matrix. It follows that a factual circumstance known to both parties at the date of the contract (such as, for example, the fact that the person providing the work has an established career as a freelance) should be taken into account. It also follows that a factual circumstance not known or reasonably available to one party (such as, for example, the precise terms on which the person doing the work has performed work for other parties if those terms have not been disclosed to the alleged employer) cannot be taken into account."* [Para 170]
> - *"Fourthly, …, the enquiry concerns the relevant contract(s), interpreted in the light of the admissible factual matrix. In the present context, that means the contract(s) relevant to the tax year(s) in question. The position under earlier contracts between the same parties is admissible as part of the factual matrix, since it will be known to both parties at the date(s) of the relevant contract(s), but not the position under later contracts between the same parties. It is necessary to bear in mind, however, that an individual may move from being an independent contractor to being an employee, and vice-versa, while working for the same contractual counterparty. It is also necessary to bear in mind that an individual may simultaneously be engaged under a contract of employment with one counterparty and under contracts for the provision of services with one or more other counterparties."* [Para 171]

In layman's terms, status determinations need to look at the full factual matrix, including whether the putative taxpayer is in business on their own account. The analysis must include other work done outside of the specific engagement which is being categorised.

Chaplin says: "This is neither ground-breaking, nor new, but HMRC have sought to shape the common law in another radical direction entirely, by seeking to fight the case against a single taxpayer in court. That tactic has now spectacularly backfired."

HMRC's "onerous argument" fails to work for HMRC

It is to be noted In HMRC's grounds of appeal, shared with ContractorCalculator, that HMRC sought to advance arguments as to why IBOOA should not be considered:

"Treating someone's status over their entire career as a relevant factor in the analysis of their status under a particular engagement, places an unduly onerous compliance burden on HMRC.

"It places an onerous burden on organisations or businesses engaging others to provide work if they are not able to determine the worker's employment status by considering only the terms of the contracts that they have entered into (either actual direct contracts or hypothetical direct contracts under the Intermediaries Legislation), but instead are required to take into account the status of the work done by the worker for other engagers, in previous tax years, and potentially over their whole careers."

Chaplin says: "The Lordships did an excellent job unpicking all the nuanced arguments made by both parties, as demonstrated by their incisiveness at the hearing, where the debates were highly nuanced. Unfortunately for HMRC, the statements saying that IBOOA should not be considered because it makes things too hard from a policy point of view did not convince the court.

"HMRC now have total clarity on how they must consider IR35 status decisions during their reviews. Whilst HMRC admit the burden on them on how they must conduct status enquiries is onerous, it is still something they must do to follow the law and ensure they adhere to the Civil service code.

The Civil Service code is unambiguous on how Civil servants are expected to carry out their roles with dedication and a commitment to the Civil Service and its core values: integrity, honesty, objectivity and impartiality. The section on objectivity clearly states, "You must not ignore inconvenient facts or relevant considerations when providing advice or making decisions."

Chaplin says: "The Court of Appeal has now laid down clear legal principles that must be followed by HMRC when considering cases. No longer can they dismiss arguments that a taxpayer is in business on their own account, nor can they solely consider each engagement in isolation where there is clear evidence of concurrent portfolio of work."

HMRC must review guidance and exiting litigation

This binding decision by the Court of Appeal is a significant blow to HMRC's longstanding and contentious interpretation of employment status law, which will now need to be revised, along with their various guidance products, including their Check Employment Status for Tax (CEST) tool.

The ruling also has wider implications, especially with those who are portfolio earners. HMRC will also need to reconsider their approach in current compliance action and litigation around cases involving these workers, particularly in the media sector.

Chaplin says: "None of these necessary actions by HMRC will surprise them because they are their ideas, confirmed in oral evidence to the Public Accounts Committee on 21st February 2022. That session was attended by senior officials of HMRC's Off-payroll working team and the CEO of HMRC, Jim Harra."

With HMRC already promising they would need to revisit their guidance and existing litigation, many taxpayers in the media sector who have also been under the spotlight for years can hopefully get some relief. HMRC inspectors will undoubtedly need to reconsider any "Inside IR35" opinion letters where engagements have been considered in isolation instead of a more holistic view of the complete portfolio.

Will HMRC apologise to Adrian Chiles?

This ruling by the Court of Appeal further highlights the punitive injustice suffered by Adrian Chiles (see Basic Broadcasting Limited case) as a result of HMRC's inspectors. Chiles spent seven years and undoubtedly considerable sums of money defending his position of being in business on his own account – which was also the primary reason the First-tier upheld his appeal.

Chaplin says: "Both the Atholl House and Basic Broadcasting cases were never about the people involved. They were about HMRC seeking to narrow the law on status matters to suit their now-disproven view and force the self-employed to pay taxes as if they were employed, despite not receiving any rights.

"The courts have roundly rejected their view. They should revisit the IR35 status opinions they have been handing out to taxpayers in the media in a cut-and-paste confetti fashion over the past few years."

Yet more expense for Atholl House?

The Court of Appeal did uphold the secondary ground related to how the in business on own account test should be considered alongside the hypothetical contracts.

Chaplin says: "This is a very complex argument, but boils down to comparing whether the hypothetical contracts fit in with the other work within the contractors' portfolio, or whether they are individual contracts of employment."

As Sir David Richards pointed out in the decision (paragraph 165), the Court of Appeal's power to re-make a decision should be used sparingly and only if the court feels no real doubt about how the FTT or the UT, properly directed, would have decided the case. Therefore, the case is being remitted back to a lower tribunal, which will be the fourth tribunal for Atholl House.

The costs involved in defending this case have been considerable. HMRC have the power to form an opinion tax is owed, which is binding in law unless proven otherwise by the taxpayer. Compare that to the taxpayer, who has the onus of discharging their burden of proof against the Goliath of HMRC, who has access to unlimited taxpayer funds to hire expensive Counsel.

Adams draws attention to this in her statement: "My greatest concern is that the financial and emotional cost of this flawed IR35 legislation falls on the private citizen. Two tribunals have already found in my favour and yet I am being placed back on the punitively expensive legal merry-go-round. The costs of defending myself now far outweigh the amount of tax that HMRC claim is at stake. Unlike HMRC, the hundreds of other freelancers under HMRC's spotlight do not have the bottomless pit of the public purse to dig into, and this inequality of arms is one reason many choose not to appeal.

Will more evidence be allowed?

One particular hurdle to overcome for Atholl House is that the Court of Appeal has stated that activity relating to earlier years than those under investigation is material and that it may need to be considered when the case is readmitted back to either the UT or FTT. The decision [paragraph 166] refers to this:

"I would, however, give the parties the opportunity to argue, if either wishes to do so, that further facts should be found and, if so, whether the parties should be confined to the existing evidence or (and, if so, on what basis) either party should be permitted to adduce further evidence. If any further fact-finding or evidence were permitted, it would then be necessary to decide whether the case should be remitted to the UT or the FTT."

It may be sensible for both parties to agree to more evidence being heard, notably because HMRC dropped two tax years at the last minute before the first hearing at FTT. These were years when Atholl House's income from the BBC was a fraction of its earnings. Therefore, material evidence strongly supporting her position that she was in business on her own account was not, due to HMRCs manoeuvre, fully presented and cross-examined in court. To ensure there is no impediment to natural justice, it seems fair that this evidence should be considered.

Chris Leslie from Tax Networks, a tax disputes and resolution business specialising in IR35 and employment status matters, says: "It is essential for taxpayers when constructing a defence that compelling corroborated facts are collated and presented to the tribunal. Without expert corroboration, the taxpayer faces an uphill battle at the tax tribunal, where the onus is on them to discharge their burden of proof.

"It is curious that HMRC chose to dispense with the two earlier years before the FTT Hearing, particularly as they were aware of the degree of outside work 'in business on own account'. It seems fair, and aligns with the tribunals objective of delivering justice, that the evidence pertaining to those earlier years is to be considered."

Adams also expresses hope that she will get tax finality and closure at the next tribunal on this matter, stating: "This dispute has already been the source of considerable anxiety in my life for eight years, and I sincerely hope the fourth tribunal will be the final one."

Whilst the saga continues for Atholl House, for many in the media sector with multiple streams of income and clear signs of being in business on their own account, they should hopefully see, subject to HMRC revisiting their position in line with the clarified law, that some cases will finally be dropped.

Published: 26 April 2022