WRITTEN EVIDENCE[1]

Keith Gordon[2]

Introduction

1. I write as a self-employed barrister specialising in dealing with contentious tax disputes. I have been in full-time practice since July 2006.

2. Between 1992 and 1999, I trained, qualified and was employed in accountancy practices as a Chartered Accountant (qualifying 1995) and a Chartered Tax Adviser (1997). From 1999 until 2002, I was employed by the Inland Revenue (originally Band B2 (now Grade 7) and later at Band B1 (now Grade 6)) on the Tax Law Rewrite Project. Between 2002 and 2006, I trained and subsequently qualified for the Bar. Although I am a member of a number of committees within the tax profession, the comments below are entirely my own.

3. I recognise that as someone who deals predominantly with tax disputes, I am not necessarily exposed to a representative selection of cases where taxpayers (and their advisers) encounter HMRC officers. (By analogy, one can well imagine a doctor, extrapolating from his/her patients' experiences, concluding that all humans are ill.) Nevertheless, the overriding impression I have (from my own caseload, from conversations with professional colleagues, from reading the professional press and from reading case reports) is that HMRC (as an organisation) does not deal fairly with typical taxpayers (i.e. individuals and small/medium-sized businesses).

4. In my view, this started at or shortly before the creation of HMRC in 2005, but took hold with the financial crisis. The latter has certainly made it easier for HMRC to propagate the view that taxpayers with any dispute

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with HMRC are guilty of unacceptable avoidance (or worse). One consequence is that taxpayers are now less willing to establish their rights before an independent Tribunal, for fear of adverse publicity. It does not matter what the nature of the tax dispute is, many individuals and businesses (especially those with a public profile) are unwilling to risk a story in the press where they have little control as to the approach a journalist will take. What might previously be considered to be plucky David taking on Goliath could now easily be reported as X not paying a fair share or being evasive with information.

5. Part of the difficulty is what I perceive to be a deplorable reduction in the quality of training of HMRC officers (at least compared with Inspectors of Taxes pre-2005). Individuals over the age of 50 (and perhaps a little younger) who "trained" with the Inland Revenue could be assured of having a thorough understanding of a wide range of tax issues and their qualification would be as highly respected as that of a Chartered Tax Adviser. I am pretty sure that that high quality of training has long disappeared. The perception I have now is that officers are no longer interested in ascertaining the correct tax treatment of any particular situation but are solely concerned with maximising the revenues. There is far too often no longer a frank discussion of facts and legal propositions but instead a war of attrition where HMRC officers hope and expect the taxpayer to blink first.

6. The problem is exacerbated by the fact that taxpayers do often give in. First, tax disputes cost money (professional fees). Secondly, they take an age to resolve (HMRC's concept of a prompt response, I believe, is 40 working days (i.e. 8 weeks) and that might be no more than a holding response).[1] Thirdly, taxpayers often have more important commercial matters to attend to – and these (for example, commercial transactions) could be potentially scuppered by an outstanding tax dispute. Fourthly, internal reorganisations and staff turnover will usually mean that there is at least one change of HMRC personnel in the course of any enquiry leading to a loss of any prior understanding as to what has been explained by the taxpayer meaning that the process is effectively required to start all over again. Fifthly, there is the risk of adverse publicity (i.e. in the current climate, any dispute with HMRC can lead to the press portraying an individual as a "tax cheat" etc). Consequently, irrespective of the true legal position, a partly-trained HMRC officer's belief in the correctness of his/her stance will be reinforced by the fact that taxpayers will eventually cave in.

7. It saddens me that a fundamental aspect of this country's economic well-being is no longer functioning in accordance with principle or fairness, but merely on who has the deepest pockets. I also worry that HMRC's approach risks alienating individuals who would not otherwise consider themselves as anything but compliant. I do not consider that this is a healthy situation for the future.

8. Before giving examples, I should state that I represent exclusively taxpayers. I would love the opportunity to represent the Crown in tax disputes for two reasons: one, it appeals to my sense of public duty; secondly, I am sure that, professionally, I would gain invaluable experience from the alternative perspective. However, to act as Counsel to HMRC, I would be obliged to apply to join the Attorney General's Panel of Counsel and I refuse to apply. The reason is simple. I do not approve of the way that HMRC behave in the course of enquiries and subsequent litigation and I do not wish to condone such behaviour by being a part of it.

A few examples

9. I shall try to illustrate this with a few examples. As they generally relate to my own clients, I hope that the Committee will forgive the anonymity.

Officer simply out of his depth

10. In this example, an officer was corresponding with an unrepresented and retired taxpayer in relation to the disposal of a family residence which had been owned by the taxpayer's wife. After a few exchanges of correspondence, the officer started to refer to the concepts of resulting and constructive trusts with a view to attributing some of the property's capital gain to the husband.

11. Because of the legal terminology being used, the individual sought legal advice and the solicitors referred the case to me. It was easy to refute the officer's concerns and a letter was accordingly drafted to be sent to the officer.

12. Based on my experience, I had advised the client to ensure that the response was accompanied by a formal request that the officer's enquiries be brought to a close. However (not necessarily surprisingly) the client considered that to be a little too combative and merely sent the letter with the technical arguments as drafted.

13. The officer duly responded. His response demonstrated that either he did not understand our letter or just did not care. He persisted with his arguments (clearly ignoring the points that had been carefully made to him). At this stage, the client agreed to my suggestion that he ask for the enquiry be closed.

14. The officer wrote back asking for a little more time, explaining that he was then running the case past his senior colleagues. In due course, as a result of their comments, he duly brought the enquiry to a close, accepting the points being put to him.

15. The client was grateful but bruised. He had incurred professional fees needlessly. Being "old-fashioned" he chose not to pursue a complaint against HMRC and simply wanted to forget the whole experience.

16. However, this was a clear case of an officer playing with a legal concept which (being charitable) he did not fully understand and was unwilling to check his actions with senior colleagues before wreaking havoc amongst the public. In my own professional training, it was made very clear on day 1, that no correspondence left the office without being checked by (at least) one senior colleague. The natural inference that I draw from my current experience is that that discipline is not exercised within HMRC. Consequently, taxpayers are being subjected to inaccurate assertions as to the law which many will simply believe because it comes on headed HMRC paper. The alternative interpretation is that HMRC policies actually encourage such letters to be issued (irrespective of the lack of accuracy) simply because many taxpayers will know no better but to trust HMRC.

Out of time assessments

17. The concept of "finality" is an intrinsic part of the Self Assessment code, with time limits on assessments clearly set out in the statute and well understood by tax advisers and the judiciary. As with other areas of law (Limitation Act 1980 – the "statute of limitations", time limits on claims in the Employment Tribunal etc) the law (through Parliament) has balanced legal rights with the important concept of certainty for the other side. Accordingly, this balancing act should not be controversial.

18. In the tax arena, such time limits can be extended in specific circumstances (generally, where a taxpayer/adviser has caused a prior under-assessment through carelessness or deliberate conduct).

19. However, it amazes me that HMRC will often issue assessments outside these time limits without even hinting to the taxpayer that the taxpayer will not actually need to pay the tax at stake unless HMRC can prove the requisite careless/deliberate conduct. Consequently, taxpayers are duped into thinking that they have to pay tax in relation to prior years when in truth HMRC would have great difficulty in proving the relevant conduct. HMRC should be required to make clear the conditions that need to be met if the assessment is to be valid so that taxpayers are made fully aware of their rights.

20. If the Committee agrees with me that formal assessments should include a clear statement of a taxpayer's rights, this obligation should be extended to any prior correspondence (so that it is not only taxpayers who wait until the formal assessments who are made aware of their legal rights). In this respect, I am referring (for example) to letters where HMRC advise a taxpayer of a potential liability and that, if the taxpayer does not respond within (say) 30 days, the letter will be followed by a formal assessment.

HMRC's distorted view of careless/deliberate conduct

21. When challenges are made, HMRC frequently express a wholly unrealistic view as to what is meant by careless/deliberate conduct. Indeed, it would be fair to say that HMRC will almost always say that the taxpayer (or adviser) has acted carelessly/deliberately without any real consideration of the meaning of these legal tests.

22. There will of course be cases where the allegations be more than justified. However, HMRC seem never to recognise the possibility of honest mistake (which is ironic given the number of mistakes made by HMRC themselves). One particular area of contention is where a taxpayer has relied upon a professional adviser. (When HMRC are charging penalties, then it is the taxpayer who must have been careless – carelessness by the adviser will not be sufficient to cause a penalty to be payable unless the advice was "obviously wrong".)

23. Despite the case law from the Tribunals being more or less consistent over the past ten years, HMRC still persist with the argument. My only explanation for this is that they expect most taxpayers to give up long before (or something might crop up in the Tribunal) and therefore the occasional defeat in the Tribunal is a risk worth paying. Alternatively, HMRC simply do not educate their staff properly as to the correct meaning of the legal test causing many taxpayers to be bullied into paying tax/penalties which are not strictly payable.

24. A particularly clear example is progressing through the Courts at the time of my writing this statement and I understand that the Committee cannot consider live cases. If that case does conclude before the Committee reports its findings, I shall be happy (if the Committee so wishes) to supplement my evidence in due course.

HMRC's distorted view of reasonable excuse

25. When time limits are missed by a taxpayer, a penalty can be avoided if the taxpayer has a reasonable excuse for missing the time limit. This gives rise to an allied concern.

26. HMRC's own manuals used to give a definition of this by reference to the judgment of Lord Justice Scott in *HM Customs & Excise v Steptoe* [1992] STC 757. However, what the manuals failed to mention is that Lord Justice Scott was a dissenting judge in that case and his view was expressly disapproved of by the majority. The most charitable interpretation of HMRC's approach (by advocating the Scott LJ view and ignoring the majority) is that it is disingenuous. I regrettably would use the stronger term, dishonest.

27. For changes to be made to the manuals, it took at first one eagle-eyed judge in the Tribunal to spot that HMRC were not advancing an accurate statement of the law and then further judgments to make the Tribunal's displeasure known. Yet HMRC officers are still advancing the argument.

28. The following shows extracts from some cases where HMRC have sought to rely on the judgment of Scott LJ (despite being asked not to by the Tribunals):

Perrin v HMRC [2014] UKFTT 488 (TC), First-tier Tribunal, 21 May 2014

> 105. It is true that in *Steptoe* (at page 765) Scott LJ endorsed *Salevon*, saying that to be a reasonable excuse there must be an "unforeseeable or inescapable misfortune." But this was not the view of the majority: the judgment of Scott LJ was a dissenting judgment.
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> 106. As a differently constituted tribunal has recently pointed out in *Electrical Installations v R&C Commrs* [2013] UKFTT 419 (TC) (Judge Brannan and Mr Simon) at [50]-[54]: "As regards the doctrine of precedent, a dissenting judgment of a member of the Court of Appeal has no precedent value other than as a potentially persuasive authority. Obviously, such a judgment must be treated

with considerable respect as befits any judgment delivered by a member of the Court of Appeal. However, the reasoning which led Scott LJ to his conclusion cannot be regarded as a precedent, or indeed as correct, since it contradicts the reasoning of the majority."

107. Although that case, like *Steptoe*, concerned VAT default surcharges, in our judgment the same applies to direct tax appeals: HMRC should not be applying such a narrow view of the "reasonable excuse" concept.

108. We therefore accept neither of HMRC's submissions on the meaning of "reasonable excuse."

109. We observe that it is not only the tribunal which is tasked with applying the "reasonable excuse" concept to taxpayer behaviour: in the first instance, it is for HMRC to decide whether or not a person has a reasonable excuse. It is clear from the correspondence sent to Mrs Perrin that Ms Lai's second submission –that a reasonable excuse is "an unexpected or unusual event" – is a mantra used as a matter of course by HMRC when assessing whether or not a person has met this legal test.

110. As a result, cases will come to the Tribunal when they could have been resolved by HMRC. This is a waste of time and resources, as well as causing unnecessary stress to taxpayers.

Barrett v HMRC [2015] UKFTT 329 (TC), First-tier Tribunal, 7 July 2015

151. In a case involving the non-submission of CIS returns between April 2007 and January 2009, *Turner v Revenue and Customs Commissioners* [2014] UKFTT 1124 (TC) (Judge Hacking), it was held that a contractor, who had provided details to his accountant of the monies earned by each of his subcontractors and sent a cheque each month to his accountant for the total tax payable under the CIS, did not have a reasonable excuse for the failure to submit the returns in the relevant period.

152. Two particular points must be made about the decision in *Turner*. The first is that para 23(2)(b), Sch 55 FA 2009 (where P relies on any other person to do anything, that is not a reasonable excuse unless P took reasonable care to avoid the failure) cannot be relied upon in determining cases outside those provisions. It was, in my respectful view, wrong for the tribunal to have said, at [11], that those provisions "simply restate the law as previously understood".

> 153. The second is even more fundamental. At [10], the tribunal referred, with apparent approval, to the view of HMRC that a reasonable excuse must be some circumstance which is both "unforeseen and beyond the control of the taxpayer". That reflects HMRC's own published guidance which is, as this tribunal has pointed out in a number of cases, notably in *Electrical Installation Solutions Ltd v Revenue and Customs Commissioners* [2013] UKFTT 419 (TC), wrongly places reliance on the dissenting judgment of Scott LJ in *Steptoe v Customs and Excise Commissioners* [1992] STC 757. It is inappropriate for HMRC to seek to rely on that formulation as representing the state of the law on reasonable excuse.

29. In other words, HMRC were able to get away with the inaccurate submission in the *Turner* case in 2014 (and it was not an isolated instance) despite the clear statement the previous year in *Electrical Installation Solutions* (and in other cases) that this was not acceptable.

30. In the Upper Tribunal, similar concerns have been expressed. For example:

> *ETB(2014) Ltd v HMRC* [2016] UKUT 424 (TCC) (30 September 2016)
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> 14. As an aside, we note that in July 2016 HMRC issued an updated version of factsheet CC/FS12 on penalties for VAT and excise wrongdoings. In that document, HMRC express the view that a "reasonable excuse is normally an unexpected or unusual event that's either unforeseeable or beyond your control". There are strong echoes there of Scott LJ's dissenting judgment in *Steptoe* and it certainly does not reflect the views of the majority in that case. The wording in CC/FS12 is unfortunate as it could lead a taxpayer or HMRC officer or even a tribunal into error when assessing whether particular circumstances constitute a reasonable excuse.

31. Indeed, only a few weeks ago, two Upper Tribunal judges (when the *Perrin* case was being considered by them) referred to HMRC still relying on the wrong formulation in *Steptoe*:

> 83. It is regrettably still the case that HMRC sometimes continue to argue that the law requires any reasonable excuse to be based on some "unforeseeable or inescapable" event, echoing the dissenting remarks of Scott LJ *in Commissioners for Customs and Excise v Steptoe* [1992] STC 757. It is quite clear that the concept of "reasonable excuse" is far wider than those remarks implied might

> be the case. In an appropriate case where HMRC base their argument on this unsustainable position, the FTT may well consider it appropriate to exercise their jurisdiction to award costs against HMRC for unreasonable conduct of the appeal. Similar observations apply to the HMRC "mantra" referred to at [109] of the 2014 Decision, to the effect that an "unexpected or unusual event" is required before there can be a reasonable excuse. The statutory phrase is "reasonable excuse", and those are the words that are to be applied by HMRC and the FTT, interpreted as set out above; the addition or substitution of other words beyond those used in the statute can very easily obscure rather than clarify the value judgment as to whether or not a taxpayer has a reasonable excuse, and should be avoided.
>
> (14 May 2018)

Refusing to suspend penalties

32. A similar problem exists in relation to the power to suspend penalties in cases of inaccurate tax returns. This power was a novel and most welcomed introduction into the tax code in the Finance Act 2007. Unfortunately, it coincided with the financial crisis and an apparent drive to maximise revenues. Consequently, it would appear anecdotally that HMRC officers are positively discouraged from suspending penalties.

33. The main sticking point involves cases where there is a one-off error (e.g. a capital gain is inadvertently omitted from a tax return). HMRC have taken the view that they cannot/should not suspend penalties in such cases.

34. The case law has evolved but recent cases in the First-tier now demonstrate that the one-off nature of the original error is no bar to suspension. Had HMRC disagreed with that approach, they could have and should have appealed against at least one of the First-tier's decisions to the Upper Tribunal. They did not.

35. One could interpret that as an implicit acceptance by HMRC that they now accept that one-off errors can lead to the suspension of penalties. However, they are generally still refusing to acknowledge this in practice. One suggestion that I have heard is that HMRC chose not to appeal against the First-tier decisions on suspension specifically because FTT decisions are not binding precedent and therefore HMRC are at liberty to ignore them. Had they taken one of the cases to the Upper Tribunal they would then be obliged to change their practice on suspension.

Requests for information

36. Another area of concern is HMRC's requests for information from taxpayers or third parties.

37. As one would expect, Parliament has laid down controls on the use of such powers. However, these controls are routinely sidestepped by HMRC in two ways in particular:

(a) HMRC initially make an "informal" request stating that non-compliance will lead to a formal notice and penalties will be payable for non-compliance with the latter; and

(b) neither the informal or any subsequent formal notice sets out the limits on HMRC's use of these powers, leading most recipients to assume that HMRC are entitled to the information.

38. The most frequent abuse of these powers that I see is the request for information in relation to tax year which is out of time for a formal enquiry. (Provided that HMRC "open" an enquiry within a year of the return being submitted, HMRC have more or less unfettered right to ask questions in relation to the return until such time as the enquiry is closed. If there is no such enquiry, however, HMRC must overcome additional statutory hurdles before they can insist upon the production of information.)

39. In all cases I have seen involving a late request for information (where I have been able to advise in time), a short and polite response has been sent along the following lines:

> "Thank you very much for your request. As there is no enquiry into the return, I do not believe that you are entitled to issue an information notice."

40. In virtually all cases, this has led to a similarly short and polite response similar to:

> "Thank you very much for your response. We have no further questions and are closing our file."

41. In the only exception that I have seen, the officer claimed to hold a document which would have "proven" the taxpayer's prior alleged dishonesty (and had it existed, such a document would clearly have justified an information notice outside the normal enquiry procedures). The officer, however, did not respond to any requests to share this document with the taxpayer's advisers, forcing the taxpayer to

notify a formal appeal against the information notice. The internal review process did not lead to a withdrawal of the information notice. It was only after the appeal was notified to the Tribunal (at which point the Tribunal would have required the document to be disclosed) that HMRC then withdrew the information notice.

42. In one case, about six years ago, I was advising a well-known business. They had been presented with an information notice which in my view was unjustified under the law. The advice I gave was along the following lines:

(a) You have a strong case to resist the information notice. However, there is a risk that the case will be reported in the press and, merely by disagreeing with HMRC, you could be (unfairly) described as a tax cheat – the nuances are not always understood by the public.

(b) You can respond but you will simply be sent further information requests and will be spending considerable sums on professional fees dealing with a burdensome HMRC investigation that is simply a "fishing expedition" which will last years until eventually HMRC give up or you pay some extra tax whether it is due or not. The only advantage to you is that this is all being done behind closed doors and with no risk to your public image being tarnished.

43. The business took the latter approach and indeed the response just led to further questions.

44. My natural instinct is to say that if you have nothing to hide, you should never be afraid of sharing information with HMRC. However, professional experience has shown that that is the completely wrong approach to take.

45. One particularly sad case involved an elderly couple whose retirement has been completely blighted by a naïve decision by their accountant to answer what was initially an innocuous question from the local tax office. A letter arrived in 2011 concerning the couple's 2007 business accounts – the officer was curious as to why a significant sum had been entered as "capital introduced to the business".

46. The accountant should have responded in the way I indicated above and, had he done so, I expect that the query would have gone no further. However, the accountant wrote back and explained that this represented the proceeds from the 2007 sale of the family home which

were paid into the couple's only bank account (their business account). The officer wrote back and asked for further information.

47. Again, the accountant should have considered the taxpayers' rights at this stage, but he was probably himself unaware of them and then provided HMRC with further information, concerning the house disposed of. It was at this stage that the accountant had now provided HMRC with information that did justify their further enquiries. The ensuing investigation was badly handled and drawn out and has come at a huge emotional and financial cost to the couple.

48. As to whether further tax should have been paid, that is still a matter for ongoing litigation which will continue into 2019. However, that process should have been commenced by HMRC in 2008 or 2009. By leaving it until 2011, they had actually lost the right to ask questions and it was only the accountant's ignorance/naivety that allowed HMRC a second bite of the cherry.

Insincere approach to ADR

49. That case also highlighted a complete lack of willingness on HMRC's part to try to resolve the technical parts of the dispute.

50. Although the introduction of Alternative Dispute Resolution has been a good thing, its ethos has not been universally accepted throughout HMRC.

51. The taxpayers requested that the case be resolved through ADR and, after some initial hesitation, HMRC reluctantly agreed. However, it turned principally on a question of law which to my mind was quite clear. HMRC, on the other hand, were relying on a single line from a Court of Appeal decision without considering the context of the particular case before the Court. I was of the view that a sensible discussion with an HMRC officer would allow the parties to understand better each other's view of the law and perhaps allow the case to be resolved without further costs being incurred. However:

    (a) HMRC's technical officer refused to attend the ADR session.

    (b) He also refused to address the specific legal issue over the telephone during the ADR.

    (c) Through the ADR process, it was agreed that the taxpayer would set out in writing a clear explanation as to why HMRC's reliance on the Court of Appeal decision was wrong and HMRC would then respond.

(d) In response, however, the HMRC technical officer simply repeated the line from the Court of Appeal decision and the ADR process thereby concluded in failure.

52. Even more alarmingly, at the First-tier Tribunal:

(a) HMRC's representative failed to include any arguments in his skeleton argument on the technical point in question.

(b) At the hearing, he said that he would await the taxpayers' submissions on the point and then respond.

(c) In the event, however, he decided to take an early plane home and therefore the First-tier heard no arguments from HMRC in support of the view that they were insisting upon for so long.

(d) The Tribunal subsequently agreed with the taxpayers' argument on this point.

53. It was only when seeking permission to apply to the Upper Tribunal did anyone from HMRC actually try to articulate a contrary argument. As I have noted, the case is still subject to litigation and therefore the matter is not yet concluded.

HMRC's ability to spend "other people's money"

54. Dealing with tax disputes is, for HMRC officers, a day job which they can generally forget about when not in the office. For most taxpayers, however, it is an emotionally-draining experience which has to be endured 24x7 on top of dealing with other pressing business/family issues.

55. This is not assisted by the fact that tax disputes will often last years (and usually go through at least one change of HMRC personnel).

56. Furthermore, it would usually be extremely unwise for any taxpayer to try to deal with HMRC without professional assistance and thus the experience is usually expensive as well as unpleasant. (Whilst it is easy for any professional to assert the benefits of clients engaging his/her services, I hope that some of the above examples demonstrate the dangers of taxpayers thinking that they can trust HMRC to act honourably.)

57. But HMRC's advantages are not simply limited to emotional and technical matters. To perpetuate the enquiry, HMRC officers are not spending their own money, whereas taxpayers do have to keep an eye on how much the whole dispute is costing them.

58. One acute example involved a dispute concerning the interpretation of Extra-statutory Concession A19[2], which affects mainly individuals with simpler tax affairs (typically limited to PAYE taxpayers who are outside the Self Assessment system).

59. A client was being asked to fund a £16,000 underpayment arising from a termination payment made to her by a former employer.

60. Had HMRC acted promptly, the client would have had no defence against the demand. However, HMRC failed to spot it in time and it was only a couple of years later did they alert the client to it. This was a case where the provisions of ESC A19 should have protected her. However, HMRC decided to disapply ESC A19 from PAYE cases for a few years, covering the period when they inexplicably decided to stop checking the annual returns from employers.

61. As such matters cannot be the subject of Tribunal appeals, the client commenced a judicial review in the High Court where permission was promptly given by the Judge on the papers.

62. Long before the case got anywhere near a hearing (HMRC had made repeated requests for extensions), HMRC wrote to the client and gently pointed out that they had already incurred professional costs of £38,000 which, if they were to be successful in the judicial review, they would seek from her, as well as the £16,000 tax. HMRC told the client that they would waive those costs if she paid them the £16,000 (i.e. abandoned her judicial review claim). Although the client was confident of success (and suspected that the £38,000 could be reduced on any costs assessment), she could not take any risks and eventually acceded to HMRC's requests.

63. HMRC's conduct suggests one of two scenarios. Either:

(a) They are willing to spend £38,000 of taxpayers' money in order to secure £16,000 (which does not seem like good value for money). Or

(b) They were using whatever leverage they could to prevent a judicial criticism of their approach to ESC A19 (in which case to threaten one taxpayer with the tax bill is heavy-handed to say the least).

HMRC sometimes use penalties as a cash cow

64. It is unclear to me whether this problem is a case of poor training of HMRC officers or systemic bullying (or both).

65. The tax code rightly suggests that if a taxpayer has been careless there is a risk of a penalty. Implicit within this is the concept of an innocent mistake – i.e. the taxpayer has reached a wrong decision but not due to any lack of care.

66. The problem is that may HMRC officers fail to see the distinction. The following example demonstrates how this can backfire on HMRC.

Taxpayer was a computer programmer who completed his own tax return online. Due to a programming glitch (which HMRC had been alerted to and had already corrected for the following year's tax returns), capital gains which had been reported were not factored into the automated calculation process. The taxpayer (whose true liability was £3,000) was told of a tax liability of £4.

The capital gain had arisen on the disposal of a business. Because of the annual exemption and other reliefs, the taxpayer had been told to expect a low capital gains tax bill. Consequently, the £4 liability came as no surprise.

Despite HMRC knowing of the glitch, they made no contact with the taxpayer until after the enquiry window had closed. They then wrote to him and advised him of the £3,000 underpayment which he promptly paid. HMRC then advised the taxpayer that they considered he had acted carelessly and imposed a 25% penalty (i.e. £750).

This was one step too far and the taxpayer sought the advice of an accountant who instructed me to advise. I pointed out that, in the circumstances of the case, not only was the penalty not payable but HMRC had also missed the opportunity to assess the £3,000 tax. (In fact the taxpayer had paid the £3,000 so promptly, HMRC had not even assessed it.) In both cases, HMRC were required to prove carelessness and I considered that a lay taxpayer could not be careless for trusting HMRC's computer.

HMRC decided to withdraw the threat of a penalty but they defended the right to the tax. I represented the taxpayer on a conditional fee basis and the Tribunal agreed with us.

The point is that had HMRC not been greedy (by demanding a penalty), they would also have had the benefit of the £3,000 tax. However, once I was engaged, I was able to show that HMRC were not even entitled to the tax.

67. The other consequence of HMRC's conduct in this case is that they have alienated a compliant taxpayer. That is not conducive to good relationships in the long-term.

An apparent "win at all costs" approach

68. Another issue I regularly see is HMRC willing to say whatever they need to say in order to win any argument. In many cases, this will involve arguing a particular interpretation of the law even if it goes against HMRC policy. Of course, I have no issue with HMRC changing their policy

when this is a genuine change of view. But I consider it inappropriate for such changes to be made on an *ad hoc* basis.

69. This undermines trust in the Department and professional experience dictates that I now treat utterances from HMRC officers with a healthy dose of cynicism.

70. One particular acute example involved an officer giving evidence in a Tribunal which flatly contradicted what he had sworn in an affidavit for an earlier hearing. The Tribunal gave the officer the benefit of the doubt:

Pattullo v HMRC [2014] UKFTT 841 (TC), First-tier Tribunal

> 54. … It is true that there were differences; some aspects of his evidence were not covered in his affidavit. However, we are of the view that Dr Branigan was not attempting to depart from his basic views and recollection. Rather, he was at pains to ensure that we had the complete picture. The circumstances in which his affidavit came to be prepared for the purposes of the judicial review proceedings were not before us. However, it is within the experience of the Tribunal that these documents sometimes have to be produced at short notice, and may be directed to what may seem important at the time but which become less significant subsequently, where other matters not previously thought to be of significance, assume an importance not hitherto appreciated. Dr Branigan had ample opportunity to reflect before providing and giving evidence to this Tribunal. It seems to us that his evidence before us, insofar as it is different from his affidavit, is likely to have been more comprehensive and accurate.

71. I am prepared to accept that the evidence before the Tribunal was indeed the more accurate of the two. However, I am less forgiving than the Tribunal and my suspicion (especially as it is a recurring theme with HMRC generally) is that the officer was willing to say whatever would maximise his chances of success at the earlier hearing (where the evidence would not be subject to cross-examination).

72. Even if the officer was guilty of no more than an honest mistake, this is the kind of mistake that, if made by taxpayers, would attract considerable criticism and probably penalties.

73. Whatever the actual position, I do not consider it a healthy state of affairs when HMRC officers (governed by the Civil Service Code) cannot be trusted.

The Committee's specific questions

How do HMRC governance and settlement processes affect its ability to resolve tax disputes in a proportionate and fair way?

74. I can fully accept that one side of fairness is treating all taxpayers equally.

75. However, fairness also requires disputes to be resolved in a proportionate fashion. Why should a taxpayer spend a considerable proportion of the tax at stake (often more) simply to allow HMRC establish a principle which is applicable to a wider number of taxpayers and therefore worth a lot more to them than to any one individual taxpayer?

76. Even when the matter is of more limited interest, it would make more sense for a commercial compromise to be reached rather than for disproportionate sums to be incurred on litigation. Yet, the LSS currently encourages such conduct. As HMRC officers do not suffer the costs of this approach, it is taxpayers who generally fall foul of it.

77. Another difficulty with the LSS is that it is being used as a fig-leaf to prevent HMRC from reaching a sensible view in any particular case. In one of my current cases (another instance of a taxpayer who took part in an avoidance scheme and where HMRC are alleging careless conduct), an ADR took place in which we tried to explain to HMRC (based upon the facts of the case and the case law on carelessness) that HMRC ought to abandon the case. However, the HMRC officers refused to budge relying on a generic advice from Counsel saying that they have good prospects on carelessness and saying that, in the circumstances, the LSS precludes them from settling. (In the circumstances, one therefore wonders what the point was of the ADR.) It is unclear how old that Counsel's advice was because it was certainly inconsistent with all recent case law.

Does HMRC's litigation and settlement strategy provide a rational and sound framework for resolving tax disputes?

78. It makes more sense in larger cases (and perhaps those involving avoidance – although the definition of "avoidance" is hard to pin down). But, for the reasons already expressed, it affects many taxpayers unfairly by imposing on them unnecessary and disproportionate costs.

Do HMRC's collection and management powers set out in the Commissioners for Revenue and Customs Act 2005 provide HMRC with sufficient flexibility to achieve cost-effective and fair results?

79. Absolutely. The difficulty is that HMRC have abandoned that flexibility and imposed the LSS.[3]

Does HMRC's approach to enforcing compliance with tax law, including its approach to penalties and other sanctions, result in disproportionate or unjust outcomes? If so, how can the situation be remedied?

80. The main problem is the perception by many officers that any mistake suggests carelessness (or worse) and then justifies a penalty. This attitude is not helpful and encourages a them/us approach so far as taxpayers are concerned.

81. There are many cases where taxpayers have paid HMRC sums in penalties which are simply not due. For example, the professional negligence case of *Mehjoo v Harben Barker* [2013] EWHC 1500 refers to penalties of £200,000 being levied by HMRC. (As subsequent case law in the Tribunal demonstrates, that penalty should probably not have been paid.)

82. Furthermore, there are many cases where it is cheaper for a taxpayer to pay the penalty than to fight it.

83. In some cases, however, it is the threat of penalties which encourages some taxpayers to take a more assertive stance against HMRC and is the catalyst to getting the whole case resolved properly by the Tribunal.

Is there sufficient governance over the whole of HMRC's enquiry process to ensure that HMRC's interventions are well-targeted and that taxpayers are treated fairly and professionally throughout?

84. I suspect that the concept of the "random" enquiry which was a key part of Self Assessment when it was introduced has long disappeared in practice. Accordingly, it is probably the case that interventions are

adequately targeted at those cases where HMRC consider that their efforts will be well rewarded.

85. However, this pre-selection then sometimes clouds the objectivity of the officer conducting the enquiry.

86. Furthermore, the idea of taxpayers being "treated fairly and professionally throughout" strikes me as a long way from the reality. In recent months, I have been instructed in three very different cases where enquiries have become moribund. In two cases HMRC have consented to the enquiries being formally closed (but in both cases have granted themselves a further six-month opportunity to review the paperwork before issuing their closure notices). In a third case, HMRC (who had not responded for over a year

to the taxpayer's previous information) responded to the closure notice application with a long list of more information that HMRC claimed they required, with the intention of using those unanswered questions as a reason to refuse to close the enquiry.

87. One concern is that HMRC are treating taxpayers as pawns in a much larger game. HMRC are often believed to be trying to line up "helpful" precedents in the Tribunal so as to make it more difficult or less attractive for other taxpayers to obtain a satisfactory outcome. This is particularly acute given HMRC's powers to issue Follower Notices in avoidance cases. If HMRC can identify a case which they are likely to win at the First-tier (and is unlikely to be further litigated) then that case is likely to be accelerated and other cases left to "tread water". Once HMRC get the helpful precedent, they will then promptly issue a Follower Notice to other taxpayers meaning that the other taxpayers face a 50% penalty simply for continuing with their dispute.

88. However, this seems to be a tactic being applied more widely. In one case a few years ago, HMRC were willing to take an aggressive stance until they realised that the taxpayer's case was likely to be heard by the Tribunal sooner than they had anticipated. They offered very attractive settlement terms (i.e. the additional tax payable was more or less the same as the anticipated litigation costs) which would not ordinarily be considered to be consistent with the LSS.

Do HMRC's governance processes provide sufficient scrutiny and assurance for clearances and approvals given to taxpayers outside the formal enquiry process.

89. I am not sure I can answer this.