[2020] UKFTT 246 (TC)

TC07730

Appeal number: TC/2017/06127
TC/2017/06128

INCOME TAX – follower notice – penalty for failure to take corrective action – whether reasonable in all the circumstances – no – whether appropriate mitigation given – no – appeal upheld in part as to mitigation

FIRST-TIER TRIBUNAL
TAX CHAMBER

JOHN UNSWORTH **NICKY UNSWORTH**	**Appellants**
- and -	
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS	**Respondents**

TRIBUNAL: JUDGE ANNE FAIRPO
MS SHAMEEM AKHTAR

Sitting in public at Manchester on 11 February 2019

Mr Cummings, accountant for the Appellant

Ms Poulter, presenting officer for the Respondents

DECISION

1. These are two appeals against penalties issued under s208 Finance Act 2014 for failure to take corrective action in response to a follower notice. The appellants are husband and wife and the appeals were heard together because the relevant facts were essentially the same. The only distinction between them is that Mrs Unsworth had received a repayment of tax from HMRC, which was subsequently repaid to HMRC, whereas Mr Unsworth had had no repayment.

Background

2. There was no dispute between the parties as to the background to the appeals which was, in summary:

> (1) The appellants (Mr and Mrs Unsworth) filed tax returns for the tax year ending 5 April 2005 which disclosed that they had participated in a gilt strips scheme. The respondents (HMRC) subsequently opened enquiries into their returns.
>
> (2) In February 2011, HMRC formed the view that the gilt strips scheme was very similar to the scheme involved in the decision of *Berry* [2011] UKUT 81 (TCC) such that the decision in Berry was "relevant" for the purposes of s205(3) Finance Act 2014.
>
> (3) In December 2015, HMRC issued Follower Notices and Advance Payment Notices to Mr and Mrs Unsworth. Forms CADAcc36 for amendment of their returns were also provided. The date by which the necessary corrective action was required was 21 March 2016.
>
> (4) On 4 April 2016, Mr and Mrs Unsworth's agent wrote to HMRC and in the letter stated that "my clients have formally instructed me to notify you that they no longer wish to pursue any argument with HMRC as to the merit of the arrangement and to accept the formal amendment of their respective tax returns for the year ended 5 April 2005. Please … forward the revised tax assessments for the year".

Appellants case

3. Mr and Mrs Unsworth accepted that they had not met the deadline for taking corrective action but argued that they had a reasonable excuse for doing so and that the delay was – taking into account the Easter holiday in 2016 – only eight working days. They submitted that the severity of the penalty was unjust and unfair in the circumstances.

4. They had instructed an agent (Mr Cummings, their representative at the hearing) when the Follower Notices were issued. As they had no information from the promoter of the scheme, Mr Cummings sought this from HMRC in order to be able to advise Mr and Mrs Unsworth.

5. HMRC responded with the information on 16 March 2016. Mr Cummings wrote to Mr and Mrs Unsworth on 20 March 2016 to pass on the information and ask them what they wanted to do.

6. Mr and Mrs Unsworth were on holiday at the time. They replied to Mr Cummings on 2 April 2016 when they returned from holiday and instructed him to comply with HMRC's requests.

7. On 4 April 2016, Mr Cummings wrote to HMRC as set out in the background above. The forms CADAcc36 provided by HMRC were not used because Mr and Mrs Unsworth were not available to sign the forms at that time.

8. Mr Cummings also argued that the returns could not be amended because they had been "stayed" and HMRC had already amended them to deny the relief.

9. It was submitted that the letter of 4 April 2016 contained enough information for HMRC to close the matter for each of Mr and Mrs Unsworth and that it should be regarded as being the necessary corrective action. No tax was due to HMRC, as the repayment received by Mrs Unsworth had been repaid. HMRC's subsequent letter of 27 April 2016, which stated that closure notices would be issued, did not indicate that these could be challenged. Mr and Mrs Unsworth were not aware at this stage that HMRC did not accept that the necessary corrective action had been taken. It was not until issued the penalties on 8 July 2016 that they realised this.

10. It was submitted that there was a clear trail of cooperation with HMRC and that the penalties charged did not take this into account.

11. It was submitted that this was supported by the cases of *Onillon* [2018] UKFTT 33 (TC) and *Hutchinson* [2018] UKFTT 290 (TC). In *Onillon*, the tribunal concluded that the case did not merit a penalty as the appellant in that case had taken reasonable action and so, in the circumstances, the failure was reasonable. In *Hutchinson*, the tribunal concluded that HMRC's assessment of the penalty was not a fair assessment as it did not properly reflect the actions of the appellant even though the necessary corrective action was taken some eight months late with no good explanation as to why it was so late. The tribunal concluded that as it seemed to be easy for HMRC to close the enquiry on the basis of information in their possession, the taxpayer's failure did not appear to create much work for HMRC.

12. In addition, it was submitted that HMRC were treating Mr and Mrs Unsworth unfairly as they were aware that there were other users of the scheme who had not had Follower Notices or penalties. This was one of the reasons for delays, as they were double checking with HMRC as to what was correct because these other users had not had any correspondence from HMRC. It was unfair that Mr and Mrs Unsworth should have to pay a penalty in circumstances where others are not being treated in the same way.

HMRC's case

13. HMRC submitted that there was no dispute that the due date for the necessary corrective action was 21 March 2016 nor that the necessary corrective action had not been taken by that date, and so the questions for this Tribunal were:

(1) Whether there was a reasonable excuse for the failure to take corrective action on time; and

(2) Whether the penalty should be reduced from that assessed by HMRC.

14. HMRC made a number of submissions, as follows.

15. The delay was considerably more than eight days as submitted by Mr and Mrs Unsworth and that, in fact, no corrective action has been taken by Mr and Mrs Unsworth. The matter was resolved by HMRC issuing a closure notice in respect of the enquiry.

16. s208 Finance Act 2014 sets out as relevant that:

> (4) The necessary corrective action is taken in respect of the denied advantage if (and only if) P takes the steps set out in subsections (5) and (6).
>
> (5) The first step is that—
>
> (a) in the case of a follower notice given by virtue of section 204(2)(a), P amends a return or claim to counteract the denied advantage;
>
> …
>
> (6) The second step is that P notifies HMRC—
>
> (a) that P has taken the first step, and
>
> (b) of the denied advantage and (where different) the additional amount which has or will become due and payable in respect of tax by reason of the first step being taken.

17. Mr and Mrs Unsworth had received detailed information as to the necessary corrective action in various documents:

(1) The advance notification letters dated 9 December 2015;

(2) The Follower Notices dated 17 December 2015;

(3) The corrective action forms; and

(4) The covering letters sent with the Follower Notices.

18. The corrective action forms were not required to be used but were provided to make it easier for a taxpayer to provide the required information as it was prepopulated.

19. Mr and Mrs Unsworth had not amended their tax returns by 21 March 2016. The letter from Mr Cummings of 4 April 2016, which they submitted amounted to the

necessary corrective action, did not amend their returns, nor did it inform HMRC that the returns had been amended, and it did not information HMRC as to the denied advantage. The letter stated only that they did not want to pursue any argument with HMRC and asked for HMRC to provide a revised assessment of their tax liabilities. The letter did not therefore comply with the necessary steps 1 and 2 set out in the legislation.

20. The legislation requires that the taxpayer takes the necessary corrective action themselves in order to create finality as to the taxpayer's return. Where a taxpayer amends a return, there is no appeal against that amendment. If HMRC amend the return on behalf of the taxpayer, that amendment could be appealed.

21. Mr and Mrs Unsworth's belief that the letter of 4 April 2016 amounts to the necessary corrective action does not provide a reasonable excuse for the failure to take the necessary action by the due date. The necessary corrective action is that set out in the legislation, not that which is believed to be necessary by the taxpayer.

22. HMRC submitted that the case of *Onillon* was a First-tier Tribunal decision and so is not binding on this Tribunal. In addition, the facts in this case are not the same as those in *Onillon*. For example, Mr and Mrs Unsworth had not instructed their agents to take corrective action before the deadline. Further, the ambiguity and contradictory information in the covering letter sent in *Onillion* was not present in the covering letters sent to Mr and Mrs Unsworth which made it clear that a penalty would be charged if corrective action was not taken by the due date.

23. HMRC also submitted that the fact that no tax advantage was obtained by Mr Unsworth, as no repayment was made to him, nor maintained by Mrs Unsworth as the repayment made to her was repaid to HMRC, was relevant. As was made clear in *Hutchinson*, the necessary corrective action was required by the legislation even if the advantage was not obtained.

24. HMRC noted that Mr and Mrs Unsworth's tax returns had not been amended by HMRC before the date by which the necessary corrective action was required. Mr Unsworth's repayment had been denied, and the relevant amounts held in suspense, but the returns had not been amended.

25. As the necessary corrective action was not taken by the due date and Mr and Mrs Unsworth had not established that they had a reasonable excuse for the failure to take the action by that date, HMRC submitted that they were correct to issue a penalty.

26. HMRC calculated the penalty pursuant to s209 Finance Act 2014, which provides that the penalty is 50% of the value of the denied advantage. The denied advantage is defined by paragraph 2, Schedule 30 of Finance Act 2014 as (in this case) the amount which would be repayable by HMRC if the denied advantage were not counteracted.

27. The penalty was reduced under s210 Finance Act 2014 to reflect the quality of the cooperation of Mr and Mrs Unsworth. The minimum penalty which may be

imposed is 10% of the denied advantage. In calculating the reduction, no credit was given for taking corrective action, as no corrective action had been taken by either Mr or Mrs Unsworth. It was submitted that this was reasonable, as they had not given up their rights to pursue the matter further. A reduction of 50% was therefore given, bringing the penalty to 30% of the denied advantage.

28. HMRC submitted that the penalty was reasonable in all the circumstances. The submissions that the penalty was not fair because others in the same scheme had not been subject to penalties was not relevant.

Decision

29. It was not disputed that:

(1) the Follower Notices were correctly issued;

(2) the specified time for the necessary corrective action was 21 March 2016;

(3) no corrective action was taken by the specified time.

30. Under s208(2) Finance Act 2014 Mr and Mrs Unsworth are each therefore liable to pay a penalty. The questions for this Tribunal are:

(1) was it was reasonable in all the circumstances for them not to have taken the necessary corrective action by the specified time, so that the penalty is not payable; or

(2) is the reduction in the penalty given by HMRC appropriate?

31. In respect of the first question, s214(8) Finance Act 2014 provides that this Tribunal may affirm or cancel HMRC's decision. In respect of the second question, s214(9) Finance Act 2014 provides that we may affirm HMRC's decision or substitute another decision that HMRC had power to make.

32. It was also submitted for Mr and Mrs Unsworth that the penalty was disproportionate because there was a delay of only eight working days before the letter of 4 April 2016 was sent and because other people who had used the same scheme had not been penalised. It was submitted that even there had been a breach in the law, it did not justify a penalty of 30%. We have considered the question of whether the reduction given was appropriate below but deal here with the wider question of whether the penalty regime as a whole is disproportionate.

33. We have has jurisdiction to consider the proportionality of a penalty because the European Convention of Human Rights confers a right to property, and a person cannot be deprived of his property (such as by the imposition of a penalty) unless in exercise of the right of the government to levy tax and enforce laws. In doing so, the Government must act proportionately. Case law has established that, to lack proportionality, a penalty must be 'not merely harsh but plainly unfair' (*International Transport Roth* [2002] EWCA Civ 158).

34. With regard to the penalty regime relating to follower notices as a whole, we do not consider that it is disproportionate that the penalty regime be related to the amount of tax in question. The purpose of the follower notice regime is to require taxpayers to end a dispute over tax arrangements which have been found by a court to be ineffective because the obtaining of a tax advantage was at least one of the main purposes of the arrangements. The penalty regime is to provide consequences for failure to act in accordance with the rules of the regime without good reason. The prejudice to HMRC of a failure by a taxpayer to comply with the regime will depend on the amount of tax in dispute and so it is not disproportionate for the penalty to be related to that amount.

35. The penalty is set initially at 50% but can be mitigated by behaviour down to 10%. Overall, whilst the higher level may be considered to be harsh, it does not seem to us that the regime as a whole can be considered to be 'plainly unfair' given the purpose of the follower notice regime.

Was it reasonable for Mr and Mrs Unsworth not to have taken the necessary corrective action by the specified time?

36. There were no clear submissions made during the hearing as to why it was reasonable for Mr and Mrs Unsworth not to have taken the necessary corrective action although it was submitted that we should find that we should follow the decision in *Onillion* and find that, in all the circumstances, it was reasonable for Mr and Mrs Unsworth not to have taken corrective action by the due date.

37. It was suggested in correspondence that it was reasonable for them not to have taken the necessary corrective action because they were on holiday at the relevant time, although this was not repeated in the hearing.

38. For the avoidance of doubt, we do not consider that it is reasonable for a taxpayer to fail to take action because they are on holiday on a particular date. The due date for compliance, 21 March 2016, had been notified to Mr and Mrs Unsworth in December 2015. They had plenty of time to make arrangements to comply. Mr Cummings also accepted that waiting for information from HMRC did not amount to a reasonable excuse for the delay.

39. We have considered the submissions made with regard to the decision in *Onillon* although we note that, as a First-tier Tribunal decision, it is not binding upon us in this case.

40. We consider that the facts in *Onillon* were materially different: there were substantial errors in that case that are not present in this case. We do note that the covering letters sent to Mr and Mrs Unsworth are not free from error. In particular, the section headed "If you want to settle your tax affairs" in each letter ends with the half-sentence "However, as we have now given you a follower notice, you will be liable to pay a penalty if." Nevertheless, we consider that it is clear from information earlier in the letters that a penalty will be payable if the necessary corrective action is not taken by the date shown in the notice. This is in contrast to *Omillon*, where there

appears to have been some ambiguity as to whether the necessary corrective action was needed.

41. In addition, it is clear that in *Onillon* the taxpayer did follow certain of HMRC's instructions in the covering letter in an attempt to comply before the specified time. There was no suggestion that Mr and Mrs Unsworth, or their agent, took actions that could be regarded as an attempt to comply with the requirement to provide the necessary corrective action by the specified date, although we note that they were engaging with HMRC.

42. There were also other circumstances, including an incorrectly issued Accelerated Payment Notice, which added to the confusing circumstances in *Onillon* which meant that the court concluded that the taxpayer's failure as reasonable in those circumstances. We do not consider that there are any similar circumstances which would apply in this case.

43. Accordingly, considering all of the circumstances of the case, we do not consider that it was reasonable for Mr and Mrs Unsworth not to have taken the necessary corrective action by the specified date.

44. Accordingly, we find that Mr and Mrs Unsworth were liable to pay a penalty under s208(2) Finance Act 2014.

Whether the reduction given by HMRC is appropriate

45. The amount of a penalty under s208(2) Finance Act 2014 is set by s209 Finance Act 2014 as 50% of the denied advantage.

46. s210 Finance Act 2014 provides that a penalty may be reduced by HMRC where the taxpayer has cooperated. Cooperation is defined in s210(3) as having:

> (a) provided reasonable assistance to HMRC in quantifying the tax advantage;
>
> (b) counteracted the denied advantage;
>
> (c) provided HMRC with information enabling corrective action to be taken by HMRC;
>
> (d) provided HMRC with information enabling HMRC to enter an agreement with [the taxpayer] for the purpose of counteracting the denied advantage;
>
> (e) allowed HMRC to access tax records for the purpose of ensuring that the denied advantage is fully counteracted.

47. We consider that (b) must refer to counteraction taken by the taxpayer after the specified time, as no penalty could arise if the counteraction is taken by the specified time.

48. s210(4) sets the minimum penalty which may be imposed as 10% of the denied advantage.

49. The penalty notice provided by HMRC to each of Mr and Mrs Unsworth explained that the penalty had been reduced as follows:

(1) For providing assistance, HMRC will normally reduce the penalty range by up to 20%, In this case, all the necessary information had been given in the tax return and during the compliance check, so HMRC had given the full 20%;

(2) For counteracting the denied advantage, HMRC will normally reduce the penalty range by up to 50% but had given no reduction as no corrective action had been taken;

(3) For providing information that enables HMRC to take corrective action, HMRC will normally reduce the penalty range by up to 10%. As HMRC did not need any information from Mr or Mrs Unsworth, the full 10% was given;

(4) For providing information that enables HMRC to enter into an agreement to counteract the denied advantage, HMRC will normally reduce the penalty range by up to 10%. As HMRC did not need any information from Mr or Mrs Unsworth, the full 10% was given;

(5) For providing access to tax records to make sure that the denied advantage is fully counteracted, HMRC will normally reduce the penalty range by up to 10%. As HMRC did not need any information from Mr or Mrs Unsworth, the full 10% was given;

50. We noted the parties' submissions with regard to *Hutchinson*. As with *Onillon*, this is a First-tier Tribunal and is not binding upon us. However, we agree with a number of points made in that decision. Firstly, as set out in §101 to 103, HMRC's guidance as to mitigation (the same guidance was given in *Hutchinson* as in this case) is not set out in law and so is not binding on this Tribunal. s210 Finance Act 2014 does not include any provisions as to how a reduction is to be calculated, other than to set out what constitutes cooperation.

51. The definition of cooperation (s210(3)) states that a taxpayer has cooperated if they have done "one or more" of the actions set out.

52. HMRC's method of calculating the reduction, as set out above, assumes that all three circumstances must be present for a full reduction in the penalty to be possible. This would seem to mean that the full reduction can only be available where:

(1) A taxpayer has counteracted the denied advantage; *and*

(2) The taxpayer has provided HMRC with information enabling corrective action to be taken by HMRC; *and*

(3) The taxpayer has provided HMRC with information enabling HMRC to enter into an agreement with the taxpayer for the purpose of counteracting the denied advantage.

53. It is not clear, and was not explained, how all three of these circumstances can exist at the same time.

54. We note from HMRC's penalty explanation schedule that HMRC did not in fact require any assistance or information from Mr and Mrs Unsworth in relation to the Follower Notices to comply with factors (a), (c), (d) and (e). All such information had been provided by them before the Follower Notices were issued.

55. In practice, it also seems that HMRC in fact give full credit for factors which cannot apply in a particular case. In this case, for example, HMRC have given full credit for factor (e) even though they state in their analysis that no such information was required.

56. We note also that HMRC's explanation of the penalty indicates that they can "reduce the penalty range by up to 50%" for factor (b). We consider that this clearly indicates that HMRC anticipate that there is a range of possible behaviours which can fall within factor (b).

57. Accordingly, we consider that HMRC have treated Mr and Mrs Unsworth as if they had been completely uncooperative with regard to the Follower Notices as they have given no credit for any actions taken by Mr and Mrs Unsworth in relation to the Follower Notices. The overall assessment in this case puts Mr and Mrs Unsworth on the same basis as a taxpayer who has previously engaged with an enquiry but then completely ignored the Follower Notice.

58. Considering all the circumstances, we do not consider that this is appropriate. Mr and Mrs Unsworth did not completely ignore the Follower Notices or their requirements. They failed to take the necessary corrective action by the specified time, but we consider that the evidence shows that they attempted to take corrective action shortly after the specified time and that they were in correspondence with HMRC to obtain information before the specified time. We find that they (and their agent) were mistaken as to what was required for such corrective action to be effective, but they were not being uncooperative.

59. In these circumstances, we do not consider that it is appropriate to give no reduction for this factor. Mr and Mrs Unsworth have attempted to cooperate, and the attempt should, we consider, be reflected in the reduction of the penalty.

60. We note that it is open to us under s214(9) that we may substitute for HMRC's decision as to the amount of the penalty another decision that HMRC had power to make.

61. We do not consider that we can give a full reduction for factor (b) as Mr and Mrs Unsworth did not actually undertake the actions required in the legislation to counteract the denied advantage and so did not irrevocably amend their returns.

62. We consider that it is appropriate to give a reduction in the penalty range of 25% for factor (b) to reflect the fact that an attempt was made at compliance, but that Mr and Mrs Unsworth did not (directly or via their agent) establish what was actually required to counteract the denied advantage. It was not submitted that any check had been made to confirm whether the letter of 4 April 2016 in fact met the requirements of the legislation, although previous correspondence had made it clear what was

required. They did not use the form provided by HMRC. In contrast, in the case of *Hutchinson*, the form provided by HMRC was (eventually) used by the taxpayer before the penalty was issued.

63. Giving an additional reduction of 25% for attempting to counteract the denied advantage means that that the total reduction in the penalty range is 75%. The penalty range is 40% (being the difference between the maximum penalty of 50% and the minimum penalty of 10%). We find that each penalty should therefore be 20%, being 50% less 75% of 40%.

64. The penalty charged to Mr Unsworth is therefore reduced from £32,579.40 to £21,719.60. The penalty charged to Mrs Unsworth is reduced from £9,297.17 to £6,198.11.

65. We considered the proportionality of the penalties in this particular case, as reduced, and consider that it is not plainly unfair given that the reason why the deadline was not met in the first place was that Mr and Mrs Unsworth were on holiday at the relevant time, despite having been aware of that deadline, and that it was not indicated that any check had been made to confirm whether the correct action had been taken to meet the relevant requirements of the legislation.

Decision

66. The appeal is allowed in part: the penalties are upheld but reduced to £21,719.60 for Mr Unsworth and £6,198.11 for Mrs Unsworth.

67. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

68. Amended and reissued on 2 April 2020 pursuant to Rule 37 of the Tribunal's Procedure Rules to correct the mistake, slip and/or omission of the original decision dated 17 February 2020.

ANNE FAIRPO

TRIBUNAL JUDGE

RELEASE DATE: 17 FEBRUARY 2020