[2017] UKFTT 460 (TC)

TC05923

Appeal number: TC/2013/04664

INCOME TAX – partnership tax return - penalties for late filing – whether properly imposed – yes – whether HMRC's statement on a partnership tax return that indicates to a taxpayer that he "may" have to buy commercial software to file online is misleading - yes - whether reasonable excuse – no – whether special circumstances – no –whether penalties proportionate – yes - appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

RAYMOND QUESTED T/A EYELEVEL DESIGN CONSULTANTS **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE NIGEL POPPLEWELL

The Tribunal determined the appeal on 27 May 2017 without a hearing under the provisions of Rule 26 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (default paper cases) having first read the Notice of Appeal dated 25 June 2013 (with enclosures), HMRC's Statement of Case (with enclosures) prepared by the Respondents on 2 February 2017 and the responses to directions given by this Tribunal on 18 April 2017

DECISION

Background

1. This is an appeal against a late filing penalty of £100 ("**late filing penalty**"), and daily penalties amounting in total to £50 ("**daily penalties**") for failure to submit a partnership tax return for the tax year 2011 – 2012 on time.

Evidence and findings of fact

2. From the papers before me I find the following facts:

(1) In 2004 Mr Quested went into partnership with his daughter. The partnership traded under the name of Eyelevel Design Consultants.

(2) Mr Quested is the representative member of the partnership. He welcomed the opportunity to file partnership tax returns online as he thought it would make things easier for both himself and the respondents.

(3) The partnership tax return for the year ended 2012 was issued, in paper form, to Mr Quested, on behalf of the appellant partnership on 6 April 2012.

(4) On the first page of that return there is the following text:

"*You can file the tax return using:*

- *this form and any supplementary pages you need;* ***OR***

- *the internet (****you will need to use commercial software which you may have to buy.)*** *If you file on line you will receive an instant online acknowledgement telling you that we have received your tax return safely. To file online, go to* ***www.hmrc.gov.uk/online***

Make sure that your tax return, and any documents asked for, reach us by:

31 October 2012 *if you complete a paper tax return;* ***OR***

31 January 2013 *if you file online."*

(5) The filing date for the partnership tax return was 31 October 2012 for a non-electronic return or 31 January 2013 for an electronic return.

(6) The appellants paper return was received by HMRC on 5 February 2013 and was processed on 15 February 2013.

(7) As the return was not received by 31 October 2012, HMRC issued a notice of penalty assessment on or around 12 February 2013 in the amount of £100.

(8) I find that the form of this Notice was AS328D which clearly indicates that if the partnership tax return is more than 3 months late HMRC will charge each partner a penalty of £10 for each day it remains outstanding.

(9) As the return had still not been received three months after the penalty date, HMRC issued a notice of daily penalty assessment on or around 19 February 2013 in the amount of £50.

(10) On 6 March 2013 Mr Quested appealed against the penalties and on 22 April 2013 requested a review of HMRC's decision. HMRC carried out a review and issued their review conclusion on 4 June 2013. The outcome of that review was that HMRC's decision should be upheld.

(11) On 25 June 2013 Mr Quested notified the appeal to the Tribunal.

The Law

Legislation

3. A summary of the relevant legislation is set out below:

Obligation to file a return and penalties

(1) Under Section 12AA of the Taxes Management Act 1970 ("**TMA**") the representative member of a partnership, who is required by HMRC to submit a tax return for a year of assessment, must submit that return by 31 October immediately following the year of assessment (if filed by paper) and 31 January immediately following the year of assessment (if filed on line).

(2) Failure to file the return on time engages the penalty regime in Schedule 55 Finance Act 2009 (and references below to paragraphs are to paragraphs in that Schedule).

(3) Penalties are calculated on the following basis:

(a) failure to file on time - £100 (paragraph 3) (i.e. the late filing penalty).

(b) failure to file for 3 months (i.e. the daily penalties) - £10 per day for the next 90 days (paragraph 4).

(c) failure to file for 6 months – 5% of payment due, or £300 (whichever is the greater) (paragraph 5).

(d) failure to file for 12 months – 5% of payment due or £300 (which is the greater) (paragraph 6).

(4) In order to visit a penalty on a taxpayer pursuant to paragraph 4, HMRC must decide if such a penalty is due and notify the taxpayer, specifying the date from which the penalty is payable (paragraph 4).

(5) If HMRC considers a taxpayer is liable to a penalty, it must assess the penalty and notify it to the taxpayer (paragraph 18).

(6) A taxpayer can appeal against any decision of HMRC that a penalty is payable, and against any such decision as to the amount of the penalty (paragraph 20).

(7) On an appeal, this tribunal can either affirm HMRC's decision or substitute for it another decision that HMRC had the power to make (paragraph 22).

Special circumstances

(8) If HMRC think it is right to reduce a penalty because of special circumstances, they can do so. Special circumstances do not include (amongst other things) an ability to pay (paragraph 16).

(9) On an appeal under paragraph 20, I can either give effect to the same percentage reduction as HMRC have given for special circumstances. I can only change that reduction if I think HMRC's original percentage reduction was flawed in the judicial review sense (paragraph 22(3) and (4)).

Reasonable excuse

(10) A taxpayer is not liable to pay a penalty if he can satisfy HMRC, or this Tribunal (on appeal) that he has a reasonable excuse for the failure to make the return (paragraph 23(1)).

(11) However, an insufficiency of funds, or reliance on another, are statutorily prohibited from being a reasonable excuse. Furthermore, where a person has a reasonable excuse, but the excuse has ceased, the taxpayer is still deemed to have that excuse if the failure is remedied without unreasonable delay after the excuse has ceased (paragraph 23(2)).

Case law

(12) A summary of the relevant case law is set out below

Notification of penalty

(13) As can be seen from [3(4)] above, in order to visit a daily £10 penalty on a taxpayer under paragraph 4, HMRC must make a decision that such a penalty should be payable, and give an appropriate notice to the taxpayer.

(14) These issues were considered by the Court of Appeal in *Donaldson v HMRC* [2016] EWCA Civ 761.

(15) The Court of Appeal decided that:

> (a) The high level policy decision taken by HMRC that all taxpayers who are more than three months late in filing a return will receive daily penalties constituted a valid decision for the purposes of paragraph 4.

(b) A notice given before the deadline (i.e. before the end of the three month period (and so issued prospectively) was a good notice. In Mr Donaldson's case, his self-assessment reminder and the SA326 notice both stated that Mr Donaldson would be liable to a £10 daily penalty if his return was more than three month's late and specified the date from which the penalties were payable. This was in compliance with the statute.

(c) HMRC's notice of assessment did not specify, however, the period for which the daily penalties had been assessed. On this it agreed with Mr Donaldson. However, there is a saving provision in Section 114(1) of the Taxes Management Act 1970 which the Court of Appeal held applied to the notice. And so they concluded that the failure to specify the period for which the daily penalties had been assessed did not invalidate the notice.

Reasonable excuse

(16) The test I adopt in determining whether the appellant has a reasonable excuse is that set out in *the Clean Car Co Ltd v C&E Commissions* [1991] VATTR 234, in which Judge Medd QC said:

> "The test of whether or not there is a reasonable excuse is an objective one. In my judgment it is an objective test in this sense. One must ask oneself: was what the taxpayer did a reasonable thing for a responsible trader conscious of and intending to comply with his obligations regarding tax, but having the experience and other relevant attributes of the taxpayer and placed in the situation that the taxpayer found himself at the relevant time, a reasonable thing to do?"

(17) Although the Clean Car case was a VAT case, it is generally accepted that the same principles apply to a claim of reasonable excuse in direct tax cases.

(18) Indeed, in the First-tier Tribunal case of *Nigel Barrett* [2015] UKFTT0329 (a case on late filing penalties under the CIS) Judge Berner said:

> "The test of reasonable excuse involves the application of an impersonal, and objective, legal standard to a particular set of facts and circumstances. The test is to determine what a reasonable taxpayer in the position of the taxpayer would have done in those circumstances, and by reference to that test to determine whether the conduct of the taxpayer can be regarded as conforming to that standard."

(19) HMRC's Compliance Manual recognises that reasonable care cannot be identified without consideration of a particular person's abilities and circumstances, and HMRC recognises the wide range of abilities and circumstances of persons completing returns or claims.

> "So whilst each person has a responsibility to take reasonable care, what is necessary for each person to discharge that responsibility has to be viewed in the light of that person's abilities and circumstances".

"In HMRC's review it is reasonable to expect a person who encounters a transaction or other event with which they are not familiar to take care to find out about the correct tax treatment or to seek appropriate advice".

Special Circumstances

(20) There have been a number of cases on special circumstances from which I derive the following principles (see *Bluu Solutions Ltd v Commissioners for Her Majesty's Revenue & Customs* [2015] UKFTT 0095 and the cases cited therein):

(a) While "special circumstances" are not defined, the courts accept that for circumstances to be special they must be "exceptional, abnormal or unusual" (*Crabtree v Hinchcliffe* [1971], 3 All ER 967) or "something out of the ordinary run of events" (*Clarks of Hove Ltd v Bakers Union* [1979], 1 All ER 152).

(b) HMRC's failure to consider special circumstances (or to have reached a flawed decision that special circumstances do not apply to a taxpayer) does not mean the decision to impose the penalty, in the first place, is flawed.

(c) Special circumstances do not have to be considered before the imposition of the penalty. HMRC can consider whether special circumstances apply at any time up to, and during, the hearing of the appeal before the tribunal.

(d) The tribunal may assess whether a special circumstances decision (if any) is flawed if it is considering an appeal against the amount of a penalty assessed on a taxpayer.

(e) The tribunal should assess any decision (or failure to make one) in light of the principles applicable to judicial review.

(f) Failure to have considered the exercise of its discretion to reduce a penalty by virtue of special circumstances, in the first place, or failure to give reasons as to why, (if HMRC has made a decision), special circumstances do not apply, can render the "decision" flawed.

(g) I can allow the taxpayer's appeal if I find that HMRC's decision is unreasonable unless it is inevitable that HMRC would have come to the same decision on the evidence before him (as per Lord Justice Neill in John Dee) *John Dee Limited v Commissioners of Customs and Excise* 1995 STC 941.

"I turn therefore to the second matter raised in the appeal, I can deal with this very shortly.

It was conceded by Mr Engelhart, in my view rightly, that where it is shown that, had the additional material been taken into account, the decision would inevitably have been the same, a Tribunal can dismiss an appeal. In the present case, however, though in the final summary the Tribunal's decision was more emphatic, the crucial words in the Decision were:

> "I find that it is most likely that, if the Commissioners had had regard to paragraph (iii) of the conclusion to Mr Ross' report, their concern for the protection of the revenue would probably have been fortified."

I cannot equate a finding "that it is most likely" with a finding of inevitability.

On this narrow ground I would dismiss the appeal."

(h) In deciding whether HMRC's decision was unreasonable, I should follow the approach summarised by Lord Greene MR in *Associated Provisional Picture Houses Limited v Wednesbury Corporation* [1948] 1 KB 223:

> "The court is entitled to investigate the action of the local authority with a view to seeing whether they have taken into account matters which they ought not to take into account, or, conversely, have refused to take into account or neglected to take into account matters which they ought to take into account. Once that question is answered in favour of the local authority, it may be still possible to say that, although the local authority have kept within the four corners of the matters which they ought to consider, they have nevertheless come to a conclusion so unreasonable that no reasonable authority could ever have come to it."

(i) As Lady Hale has recently said, in *Braganza v BP Shipping* [2015] UKSC 17 at [24], this test has two limbs:

> "The first limb focuses on the decision-making process - whether the right matters have been taken into account in reaching the decision. The second focusses upon its outcome – whether even though the right things have been taken into account, the result is so outrageous that no reasonable decision-maker could have reached it. The latter is often used as a shorthand for the Wednesbury principle, but without necessarily excluding the former."

(j) Having undertaken that assessment:

> (i) if the tribunal considers the decision is flawed, it may itself consider whether there are special circumstances which could justify substituting it's decision for that of HMRC unless

it considers that HMRC would inevitably have come to the same decision on the evidence before them.

(ii) if the tribunal considers that HMRC have properly exercised its discretion in relation to special circumstances, it cannot substitute its own decision for that of HMRC when considering by what amount, if any, it should reduce a penalty.

Proportionality

(21) In relation to the doctrine of proportionality and its application to the issues in this case, I have considered the following cases:

(a) Paraskevas Louloudakis v Elliniko Dimosio (Case C-262/99) [2001] ECR I-5547 ("*Louloudakis*")

(b) International Transport Roth GmbH v Secretary of State for the Home Dept [2003] QB 728 ("*Roth*")

(c) James v UK (Application 8793/79) (1986) 8 EHRR 123 ("*James*")

(d) Wilson v SoS for Trade and Industry [2003] UKHL 40 [2004] 1AC816 ("*Wilson*")

(e) R(on the application of Lumsden and others) (Appellants) v Legal Services Board (Respondent) [2015] UKSC 41 ("*Lumsden"*)

(22) A summary of the principles relating to proportionality are set out below:

(a) Proportionality as a general principle of EU law involves a consideration of two questions: first, whether the measure in question is suitable or appropriate to achieve the objective pursued; and secondly, whether the measure is necessary to achieve that objective, or whether it could be attained by a less onerous method (Lumsden at [33])

(b) As is the case for other principles of public law, the way in which the principle of proportionality is applied in EU law depends to a significant extent upon the context (Lumsden at [23].

(c) In the context of its application to penalties, the principle of proportionality is that:

(i) penalties may not go beyond what is strictly necessary for the objective pursued; and

(ii) a penalty must not be so disproportionate to the gravity of the infringement that it becomes an obstacle to the freedoms enshrined in the Treaty (Louloudakis at [67]).

(d) In deciding whether the measures or their application is appropriate and not disproportionate, the court must exercise a value judgment by

reference to the circumstances prevailing when the issue is to be decided. It is the current effect and impact of the legislation which matters, not the position when the legislation was enacted or came into force (Wilson at [62]).

(e) The margin of appreciation given to law makers in implementing social and economic policy should be a wide one and the courts will respect the law makers judgment as to what is in the public interest unless that judgment is manifestly "without reasonable foundation" (James at [46]) or "not merely harsh but plainly unfair" (Roth at [26]).

Burden and standard of proof

4. The burden of establishing that the appellant is prima facie liable for penalties which have been properly notified and assessed lies with HMRC.

5. The burden of establishing that he should not be liable for such penalties because, amongst other reasons, he has a reasonable excuse, or that the penalties are disproportionate, lies with the appellant.

6. In each case the standard of proof is the balance of probabilities.

Discussion and conclusion

Appellants grounds of appeal

7. Mr Quested's grounds of appeal and submissions are straightforward:

(1) HMRC's statement on the front of a paper partnership tax return that "you will need to use commercial software that you may have to buy" (emphasis added) is misleading. It admits of the possibility that there is commercial software that a taxpayer may not have to buy.

(2) Relying on this statement, he did not investigate the availability of commercial software until after the deadline (31 October 2012) for filing a paper return.

(3) Had he known that there no alternative other than to buy commercial software, he would have filed a paper return in October, as he had done in previous years.

(4) Once he investigated the availability of commercial software in order to file online, and discovered he had to buy it (i.e. there was no alternative free option) he could not afford, nor did he feel that he should incur the costs, of that commercial software.

Respondents submissions

8. The respondents submit as follows:

(1) As the partnership return states that "you will need to use commercial software which you may have to buy" there can be no misinterpretation that the partnership return can be filed online using free HMRC software.

(2) Partnerships and individuals have a choice to file a paper return or file online. However the front of the partnership return shows it can only be filed online using 3rd party commercial software.

(3) The online guidance goes on to show a list of low cost commercial software suppliers who have products that have been successfully tested with HMRC. It goes on to list the free online forms that HMRC provide and the SA800 partnership return is not listed.

(4) Since the paper return was not received until 5 February 2013 a penalty was incurred and the appellant has no reasonable excuse for failing to submit the partnership return on time.

(5) If the partnership chose not to buy 3rd party software then it should have filed a paper return by 31 October 2012.

(6) Mr Quested should have made enquiries before the paper filing date to see whether or not the appellant would have to pay for the software. This would have enabled him to file on paper by 31 October 2012 if he then decided not to buy the software.

Reasonable excuse

9. Mr Quested submits that HMRC's statement that a taxpayer may have to buy commercial software is misleading. I agree with him. If, as appears to be the case from HMRC's submissions, it was clearly known to HMRC that there was no possibility of a taxpayer purchasing commercial software for free, then a representation that a taxpayer "may" have to purchase such commercial software is clearly misleading.

10. As HMRC knew (and presumably still knows) that a taxpayer wishing to file an online partnership tax return can only do so using commercial software for which he will have to buy, then it seems to me that this is a statement which HMRC know is inaccurate.

11. If HMRC know that a taxpayer will have to buy commercial software in order to submit an electronic partnership tax return on time, then to say may which Mr Quested points out, admits of a possibility that you may not have to buy it (i.e. that free software is available) is a clear misrepresentation.

12. HMRC submits that "there can be no misrepresentation that the partnership return can be filed online using free HMRC software". This misses the point entirely. The tax return doesn't refer to HMRC software. It refers to commercial software and it clearly implies that it may be freely available, which HMRC knows not to be the case.

13. So I have no hesitation in saying that it was entirely reasonable for Mr Quested to take the statement at face value, and thus anticipate that when he investigated the position he would have found that commercial suppliers would supply the appropriate software free of charge.

14. HMRC make the point that Mr Quested should have investigated whether or not this was the case before the 31 October filing deadline for a paper return. But for the reasons given above, I do not think that it is unreasonable for him not to have done so. Even though he clearly didn't want to pay for commercial software, he had no reason to suspect that he would have to do so given HMRC's statement on the face of the partnership tax return.

15. Of course if Mr Quested has investigated the position before 31 October, he could have filed a paper return. But HMRC's statement on the tax return gives Mr Quested a reasonable excuse for not filing the paper return on time. I remind myself that the test is to decide what a reasonable taxpayer in Mr Quested's position would have done in these circumstances and that the reasonable taxpayer is (and should be) conscious of his obligations regarding tax. I find that Mr Quested would have filed a paper return by 31 October had he known that he would have had to have bought the commercial software, something which he had done for all his previous tax returns.

16. But the problem for Mr Quested arose when he discovered, after the October filing deadline, that he had to pay for the commercial software.

17. It is not precisely clear to me when he discovered that, but I assume that it was sufficiently before the electronic filing deadline of 31 January 2013 that, had he been inclined to purchase the relevant commercial software, he could have done so, and downloaded, populated and submitted it (the S800 form) before that date.

18. So Mr Quested was on the horns of a dilemma. Should he buy the software and meet the electronic filing date; or should he not, miss the deadline and pay the (literal) penalty. He chose the latter course.

19. The reasons given by Mr Quested are that he couldn't afford the software, nor did he feel that he should have to incur any costs in order to file online. No evidence has been given of what the price for downloading the commercial software was or would have been, nor why the partnership could not afford to pay for it.

20. Unfortunately, however, for Mr Quested, with whom I have considerable sympathy, I do not think that the fact that the partnership couldn't afford it, nor that Mr Quested felt that he should have to incur any costs in order to file online (even combined with HMRC's misrepresentation), comprises a reasonable excuse for his failure to file an electronic return on or before 31 January 2013, and so avoid the penalties.

21. I come back to the principles set at [3(16)-3(18)] above. Once Mr Quested realised that he had to pay for the software, it seems to me that a reasonable taxpayer, conscious of and intending to comply with his obligations regarding tax, would have bought the software, downloaded it, populated it and submitted it before 31 January.

22. Mr Quested does not give, as a ground of appeal, the fact that he found out too late in the day to do this. His issue is purely financial.

23. Although Mr Quested has not given any details of his assertion that the partnership could not afford to pay, I strongly suspect that affordability was a lesser reason than his feeling that it shouldn't have to incur any costs to comply with an online filing obligation.

24. Mr Quested feels sufficiently strongly about this that he has since dissolved the partnership. This enables him and his daughter to file individual tax returns, online, for which there is no obligation to pay for commercial software.

25. So, although HMRC statement that on the face of the tax return was clearly misleading, once Mr Quested had investigated the position and found that he had to buy commercial software, my view is that a reasonable taxpayer would have gone on to do so. That reasonable taxpayer might have balanced the cost with the liability to penalties. I have no idea whether Mr Quested undertook such an exercise. There is no evidence that he did. He had to make a hard choice. By making the choice that he did, namely not to buy the software and to miss the filing deadline, then he must live with the consequences. One consequence is the liability to pay penalties HMRC's misleading statement and his reliance on it, whilst it might comprise a reasonable excuse for failing to submit a paper return on time, does not comprise a reasonable excuse for failing to submit an electronic return on time.

Special circumstances

26. HMRC indicate that they have taken into account special circumstances and that they "do not consider that having to purchase 3rd party software to file a partnership return online to be a special circumstance".

27. They give no reasons for this. Such failure to give reasons may render the decision unlawful. If so, then I can consider whether there are special circumstances which apply to this taxpayer. I do not believe there are. Like HMRC, I too, do not consider that having to purchase 3rd party software to file a partnership return online to be a special circumstance. It is not something out of the ordinary run of events, nor is it an exceptional, abnormal or unusual action which HMRC ask of a taxpayer. Many partnerships (I suspect the majority) file partnership returns online using commercial software for which they pay. This is part of the deal with HMRC. Should a partnership not wish to purchase commercial software, then it is open to it to file a paper return. Whilst this flies, somewhat, in the face of streamlining the process, it gives a partnership a choice. Should it choose to file online, then it will have to pay for the commercial software. That is something very much within the ordinary run of events, and is unexceptional, normal and usual.

Proportionality

28. Although not argued by the appellant, it is my view that the penalties are proportionate. In light of the principles set out at [3(22)] above, and in view of the justification for the imposition of penalties (namely that it is essential for the proper

function of a self-assessed tax regime that a taxpayer provides timely and accurate information), I consider that penalties for late filing do not go beyond what is strictly necessary for the objective pursued. The penalties are far from being not merely harsh, but plainly unfair.

Decision

29. For the reasons given above I dismiss this appeal.

Appeal rights

30. 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 a Company a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

NIGEL POPPLEWELL
TRIBUNAL JUDGE

RELEASE DATE: 05 JUNE 2017