[2019] UKFTT 226 (TC)

TC07073

Appeal number: TC/2018/03266

PROCEDURE – application for costs – rule 10(1)(b) Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 – application dismissed.

FIRST-TIER TRIBUNAL
TAX CHAMBER

MICHAEL & FLORA HEGARTY **Appellants**

- and -

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

TRIBUNAL: JUDGE RICHARD THOMAS

Decision made on the papers on 27 March 2019 having read submissions by Keith Gordon of counsel for the Appellants and by Paul Marks, litigator, for the Respondents

DECISION

1. On 28 August 2018 the Tribunal (Judge Richard Thomas and Ms Patricia Gordon) sitting in Belfast heard the appeals of Mr Michael and Mrs Flora Hegarty ("the applicants") against the issue of notices by the respondents ("HMRC") for information to each of them under Schedule 36 Finance Act 2008. On 27 December 2018 the Tribunal released its decision in the case, cited as [2018] UKFTT 774 (TC).

2. The Tribunal upheld the applicants' appeals and set aside the notices. It is important to note that the notices which were the subject of the appeal were the second (or possibly third) set of notices issued in the case.

3. On 24 January 2019 the applicants sent to the Tribunal an application under rule 10(1)(b) of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ("the Rules") for their costs to be paid by HMRC. That application was copied to HMRC who have made representations on it, and so HMRC, as the potential "paying person" have been given an opportunity to make representations within the terms of rule 10(5).

4. The parties were content for the Tribunal to decide the matter on paper and because I do not think an oral hearing is required, I do so.

5. Rule 10(1)(b) provides that I can only order payment by a party in a basic case such as this where that party has acted unreasonably in bringing, defending or conducting the proceedings.

Binding authority

6. The Upper Tribunal has considered rule 10(1)(b) in a number of cases. In *Tarafdar v HMRC* [2014] UKUT 362 (TCC) the Upper Tribunal observed that:

> "[18]…The scope of [unreasonable conduct] has been discussed in this Tribunal in *Catana* [2012] UKUT 172 (TCC) where Judge Bishopp, at [14], described it as covering:
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> > 'cases in which an appellant has unreasonably brought an appeal which he should know could not succeed, a respondent has unreasonably resisted an obviously meritorious appeal, or either party has acted unreasonably in the course of proceedings, for example by persistently failing to comply with the rules and directions to the prejudice of the other side'
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> [19] The costs 'incidental to the proceedings' cover only those costs incurred in the course of preparing and pursuing the appeal…, and, on an application by the appellant, it is only the reasonableness of HMRC's conduct in defending or conducting the proceedings that falls to be considered. The reasonableness of the original decision against which the appeal has been made is not directly in point, but is relevant to the question whether it was reasonable of HMRC to defend, or to continue to defend, the appeal.
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> [20] Even if the tribunal is satisfied that a party has acted unreasonably in the terms of rule 10, the tribunal nevertheless has a discretion whether or not to make a costs order, or as regards the extent of a costs

order. Such a discretion, like any other discretion conferred on the tribunal, must be exercised judicially."

7. The way the "discretion" referred to in Tarafdar at [20] is to be exercised by the Tribunal was enlarged upon in *Willow Court Management Company (1985) Ltd v Mrs Ratna Alexander (and other cases)* [2016] UKUT 290 (LC) ("*Willow Court*"), a decision of Martin Rodger QC (Deputy Chamber President, Lands Chamber) and Siobhan McGrath (Chamber President, First-tier Tribunal (Property Chamber)). This decision, which is binding on me, discusses Rule 13(1)(b) of the Tribunal Procedure (First-tier Tribunal) (Property Chamber) Rules 2009, the equivalent to Rule 10(1)(b) of the Rules, in these terms:

> "**The element of discretion in rule 13(1)(b)**
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> 27 When considering the rule 13(1)(b) power attention should first focus on the permissive and conditional language in which it is framed: "the Tribunal *may* make an order in respect of costs *only* ... *if* a person has acted unreasonably...." We make two obvious points: first, that unreasonable conduct is an essential pre-condition of the power to order costs under the rule; secondly, once the existence of the power has been established its exercise is a matter for the discretion of the tribunal. With these points in mind we suggest that a systematic or sequential approach to applications made under the rule should be adopted.
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> 28 At the first stage the question is whether a person has acted unreasonably. A decision that the conduct of a party has been unreasonable does not involve an exercise of discretion but rather the application of an objective standard of conduct to the facts of the case. If there is no reasonable explanation for the conduct complained of, the behaviour will properly be adjudged to be unreasonable, and the threshold for the making of an order will have been crossed. A discretionary power is then engaged and the decision maker moves to a second stage of the inquiry. At that second stage it is essential for the tribunal to consider whether, in the light of the unreasonable conduct it has found to have been demonstrated, it ought to make an order for costs or not; it is only if it decides that it should make an order that a third stage is reached when the question is what the terms of that order should be.
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> 29 Once the power to make an order for costs is engaged there is no equivalent of CPR 44.2(2)(a) laying down a general rule that the unsuccessful party will be ordered to pay the costs of the successful party. The only general rules are found in section 29(2)-(3) of the 2007 Act, namely that "the relevant tribunal shall have full power to determine by whom and to what extent the costs are to be paid", subject to the tribunal's procedural rules. Pre-eminent amongst those rules, of course, is the overriding objective in rule 3 , which is to enable the tribunal to deal with cases fairly and justly. This includes dealing with the case "in ways which are proportionate to the importance of the case, the complexity of the issues, the anticipated costs and the resources of the parties and of the Tribunal." It therefore does not follow that an order for the payment of the whole of the other party's costs assessed on the standard basis will be appropriate in every case of unreasonable conduct."

8. In *Distinctive Care Limited v HMRC* [2018] 155 (TCC), at [44], the Upper Tribunal referred to its decision in *Market and Opinion Research International Limited v HMRC* [2015] UKUT 12 (TCC) ("*Mori*") in which it endorsed the following approach:

> (1) the threshold implied by the words "acted unreasonably" is lower than the threshold of acting "wholly unreasonably" which had previously applied in relation to proceedings before the Special Commissioners;
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> (2) it is possible for a single piece of conduct to amount to acting unreasonably;
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> (3) actions include omissions;
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> (4) a failure to undertake a rigorous review of the subject matter of the appeal when proceedings are commenced can amount to unreasonable conduct;
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> (5) there is no single way of acting reasonably, there may well be a range of reasonable conduct;
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> (6) the focus should be on the standard of handling the case (which we understand to refer to the proceedings before the FTT rather than to the wider dispute between the parties) rather than the quality of the original decision;
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> (7) the fact that an argument fails before the FTT does not necessarily mean that the party running that argument was acting unreasonably in doing so; to reach that threshold, the party must generally persist in an argument in the face of an unbeatable argument to the contrary; and
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> (8) the power to award costs under Rule 10 should not become a "backdoor method of costs shifting".

9. The Upper Tribunal added, at [45]:

> "…one small gloss to the above summary, namely that …questions of reasonableness should be assessed by reference to the facts and circumstances at the time or times of the acts (or omissions) in question, and not with the benefit of hindsight"

The amount of costs claimed

10. There is a dispute between the parties about the period in relation to which costs may be claimed. The applicants say that what is said in *Tarafdar* at [19] (see §6) does not prevent the costs incurred before the lodging of the appeal being claimable: HMRC disagree.

11. The applicants have also not produced a detailed schedule of costs in sufficient detail to enable me to make a summary assessment should I decide to do that. They apologise for that and ask for a waiver of, or extension of time to comply with, the (mandatory) relevant rule, rule 10(3)(b). The problem they had was that the decision was issued on 27 December and the applicants' representative was working seven day weeks to meet the 31 January deadline for filing his clients' tax returns. They

considered it better to comply with the time limit for making the application rather than delay the application to comply with rule 10(3)(b).

12. I leave consideration of these points until after I have given my decision on the principle.

The "unreasonable" conduct complained of

13. As the Upper Tribunal says in *Willow Court* at [28], the first step is to determine whether the conduct complained of is unreasonable. In terms of what was said in *Catană* by Judge Bishopp (see §6), the question is whether HMRC have "unreasonably resisted an obviously meritorious appeal". In coming to my decision on this I have taken into account the matters set out as the *Mori* approach (see §8).

14. The applicants say that from their perspective all the Schedule 36 notices issued in the case were unjustified and that the investigations begun in 2015 about transactions going back to 2005-06 were inappropriate. But they recognise that their view is not determinative, and that if HMRC genuinely held the beliefs they claimed to hold they should be entitled to act accordingly.

15. But, they say, the Schedule 36 legislation "clearly envisages" that an officer asserting suspicions of deliberate conduct should be prepared to put themselves forward to be cross-examined so that those views could be tested.

16. That did not happen, despite the applicants having made it clear three months before the hearing in a letter of appeal to the officer and in the notice of appeal to the Tribunal that the relevant officer was being put to strict proof to demonstrate that she had reason to believe there was an underassessment and that there was a sensible or practical possibility of HMRC being able to prove any deliberate underassessment. The issue continued to be made clear to HMRC up to 3 August 2018.

17. The officer's reluctance to put herself forward as a witness despite being in the courtroom and contributing actively in the proceedings suggests that she had something to hide.

18. The applicants drew my attention to the costs application in *Ryan Gardiner and others v HMRC* [2015] UKFTT 115 (TC) as the Tribunal referred to the substantive case ([2014] UKFTT 421 (TC)) in our decision.

HMRC's representations

19. HMRC say that for the appeal the applicants focussed on a number of preliminary issues including whether the notices were invalid because the matter was *res judicata* or an abuse of process, where the burden of proof was and whether the law required HMRC to show a reasonable prospect of HMRC being able to prove any deliberate underassessment.

20. On the substantive issue HMRC characterise the applicants' arguments as that the information was not reasonably required and that HMRC had no reason to suspect an underassessment of tax.

21. HMRC say there was sufficient case law to establish that the Tribunal could accept documents as evidence in lieu of witness statements under rule 15(1) where the witness evidence would be tantamount to merely confirming that the document had been produced by them. They agree that the applicants did put HMRC to "strict proof", but they contended that that does not mean that oral witness evidence had to be given where there was documentary evidence before the tribunal, the origin of which was not being contested. [SEP]

22. In support of this approach they refer, as they did before the Tribunal, to *Paul Munford v HMRC* [2017] UKFTT 19 (TC) ("*Munford*") and to rule 15(2) of the Rules allowing the Tribunal to admit evidence even if it was not admissible in court proceedings. They point out that the applicants were aware that HMRC did not intend to call any witnesses, but the applicants did not seek a witness summons under rule 16. That documentary evidence was *capable* of supporting the satisfaction of Condition B in paragraph 21 Schedule 36 was a proposition with which the Tribunal agreed, but the Tribunal found that in this case it did not. That did not make HMRC's conduct unreasonable.

23. As to the "sensible or practical possibility" of issuing a valid s 29 assessment and the applicants' suggestion that HMRC went against its own guidance, they disagreed with the applicants about the meaning of the guidance, and more importantly on the need to show a "sensible or practical possibility", and they had two FTT cases in their favour on that point.

24. HMRC admit that their case could have been better prepared and that with hindsight and with more time they might have decided to put forward the relevant officer to give oral evidence and be cross-examined, though they point out that this was categorised as a basic case where the formalities of a standard or complex case are not generally required. HMRC did not wish to delay proceedings any further.

Discussion

25. In my view HMRC's conduct in defending and conducting the proceedings was not unreasonable. I say this for the following reasons.

26. There were preliminary issues of law to be decided which the applicants were putting forward and which it was obviously proper for HMRC to defend. On the issues of *res judicata* and abuse of process HMRC succeeded.

27. They did not succeed on the burden of proof, but there were differences of view in this Tribunal on the question of the burden in Schedule 36 appeals: we happen to have preferred one view over another. In no sense could HMRC be said to have defended an obviously unmeritorious position in relation to the matter.

28. On the Condition B point, that HMRC must have reason to believe there was an underassessment, I consider that HMRC made a tactical error in not producing a witness to be cross-examined, something they now recognise. But *Munford* gives them a good reason to think that if they honestly believe that the facts speak for themselves then a witness was not necessary.

29. As to the "sensible or practical possibility" point, this was an issue of law which was by no means clear cut. HMRC had 2 decision of this Tribunal, both by experienced full time judges (Roger Berner and Jonathan Cannan), to support their view. Our decision on this point covers 10 pages and over 40 paragraphs with an extensive examination of the case law and was a close call. It may have tipped the balance in HMRC's favour had there been a witness, but it was perfectly reasonable for them to defend the point by reference to the law. Nor are HMRC required, as Mr Gordon seems almost to suggest, to withdraw a case because they would be arguing in an appeal in contradiction of their own guidance. I find unconvincing the suggestion by HMRC that they were not so doing, but it does not matter. As Mr Gordon well knows that point was a public law point if it was anything.

30. In summary I do not think that the arguments made by the appellants on the two crucial issues (failure on either of which would be fatal to HMRC) were so obviously meritorious, ie bound to succeed, or that the HMRC responses to them were so obviously unmeritorious, ie bound to fail, that HMRC acted unreasonably in not withdrawing before the hearing. The other issues are of lesser importance, as if HMRC should have decided that their case on the two crucial issues was hopeless, it would have availed them nothing to try nevertheless to succeed at the hearing on the preliminary issues of *res judicata* or abuse of process.

31. It follows from this decision that I do not need to consider whether to waive or extend time for compliance with rule 10(3)(b). Had I needed to decide the point I would probably have extended the time for compliance (I certainly would not have waived the need for compliance). Nor do I need to decide whether the applicants' point about costs incurred before the appeal was lodged was correct. But my strong inclination is to agree with HMRC, so that it would only be costs incurred after 9 May 2018 that would have been in issue.

32. 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.

RICHARD THOMAS
TRIBUNAL JUDGE

RELEASE DATE: 04 APRIL 2019