# Tax update

May 2018

**In this month's update we report on HMRC's recently published guidance relating DOTAS for inheritance tax; its guidance for the GAAR; and a new consultation relating to tax avoidance involving Profit Fragmentation. We also comment on three recent decisions relating to annual payments; discovery assessments; and penalties.**

## News items

### DOTAS for inheritance tax – new guidance published

On 29 March 2018, HMRC published new guidance which provides advice in relation to notifiable inheritance tax avoidance schemes. This follows changes to the description of inheritance tax avoidance arrangements that must be disclosed to HMRC from 1 April 2018. more›

### GAAR – updated guidance published

On 28 March 2018, HMRC published updated guidance for the general anti-abuse rule (GAAR). more›

### Tax avoidance involving profit fragmentation – consultation issued

On 10 April 2018, HMRC issued a new consultation seeking views on proposals to address tax avoidance involving profit fragmentation. more›

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### *Hargreaves*: Loyalty pays

In *Hargreaves Lansdown Asset Management Ltd v HMRC* [2018] UKFTT 127 (TC) TC06383, the First-tier Tribunal (FTT) has found that loyalty bonus payments paid to investors were not "annual payments" for the purpose of section 683, Income Tax (Trading and Other Income) Act 2005 (ITTOIA). more›

### *Hicks*: Discover the limits

In *J Hicks v HMRC* [2018] UKFTT 22, the FTT, in allowing the taxpayer's appeal, has held that discovery assessments issued by HMRC were invalid as the condition contained in section 29(5), Taxes Management Act 1970 (TMA), was not satisfied. more›

### *Jackson*: HMRC penalised in penalties case

In *Jackson v HMRC* [2018] UKFTT 0064 (TC), the FTT has held that HMRC misapplied the law in respect of penalties it had issued to the taxpayer for filing late returns. more›

### Any comments or queries


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### About this update

The Tax update is published on the first Thursday of every month, and is written by members of RPC's Tax team.

We also publish a VAT update on the final Thursday of every month, and a weekly blog, RPC's Tax Take.

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# News items

## DOTAS for inheritance tax – new guidance published

On 29 March 2018, HMRC published new guidance which provides advice in relation to notifiable inheritance tax avoidance schemes. This follows changes to the description of inheritance tax avoidance arrangements that must be disclosed to HMRC from 1 April 2018.

The guidance sets out the tests for determining whether a scheme is relevant, the relevant conditions, and the effect of the applicable hallmark. The guidance also includes some examples of notifiable and non-notifiable inheritance tax schemes.

A copy of the guidance is available to view here.

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## GAAR – updated guidance published

On 28 March 2018, HMRC published updated guidance for the general anti-abuse rule (GAAR).

In particular, Parts A, B and C have been updated to explain:

- the purpose and status of the guidance
- what the GAAR is designed to achieve, and
- how the GAAR operates.

Advice is also given on how to recognise an abusive tax arrangement and the process for counteracting such an arrangement.

A copy of the guidance is available to view here.

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## Tax avoidance involving profit fragmentation – consultation issued

On 10 April 2018, HMRC issued a new consultation seeking views on proposals to address tax avoidance involving profit fragmentation.

The target is arrangements involving offshore trusts and companies in low or nil tax jurisdictions that accrue profits attributable to the exploitation of a UK resident individual's earning capacity (for example, as an entertainer) by arranging for the receipts of that activity to accrue to the overseas entity.

HMRC believes that existing structures may be challenged through existing legislation, for example under the transfer of assets abroad legislation, but it claims that delays by promoters and taxpayers in supplying requested information make it difficult for HMRC to apply existing legislation.

Consequently, HMRC is proposing:

- that UK resident individuals will be liable to tax on profits attributable to that person's professional or trading skills which are passed to an entity where "significantly less tax" is paid if the UK resident has "power to enjoy" the economic benefits from the alienated profits and some of the foreign entity's profits are excessive considering what it does or,
- those who use such arrangements will have to notify HMRC who will then consider the facts of the arrangement in question and if it forms the view that the profits of the foreign entity are "excessive" it will issue a "charging notice" requiring tax to be paid within 30 days.

HMRC is proposing to introduce legislation in the 2018/19 Finance Bill, to take effect from April 2019. If enacted, the legislation will apply to both new and existing arrangements.

A copy of the consultation paper is available to view here.

The consultation period ends on 8 June 2018 and anyone wishing to respond can email their responses to profitfragmentation.mailbox@hmrc.gsi.gov.uk or post them to:

Profit Fragmentation Consultation,
HM Revenue and Customs,
Specialist Policy Team,
Room 3C/04,
100 Parliament Street,
London
SW1A 2BQ

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# Case reports

## *Hargreaves*: Loyalty pays

In *Hargreaves Lansdown Asset Management Ltd v HMRC* [2018] UKFTT 127 (TC) TC06383, the First-tier Tribunal (FTT) has found that loyalty bonus payments paid to investors were not "annual payments" for the purpose of section 683, Income Tax (Trading and Other Income) Act 2005 (ITTOIA).

**Background**

Hargreaves Lansdown Asset Management Ltd (the taxpayer) was an investment company. It operated a platform through which investment products from different fund providers were made available directly to investors.

In 2014, the Financial Conduct Authority (FCA) issued new rules requiring platform service providers to charge clients a direct fee for their services, rather than retain payments from the product providers. The taxpayer charged investors a platform fee. An annual management charge (AMC) was also levied on investors, which was deducted monthly from the investor's fund. The taxpayer had negotiated lower AMCs with investment providers on behalf of its clients and the providers rebated part of the management charge to the taxpayer, who passed it on to investors in the form of a "loyalty bonus". This was paid by crediting cash to the investor's client account, and reinvesting the cash into shares or units once it had reached a minimum amount.

HMRC claimed that the payments were "annual payments", under section 683, ITTOIA 2005 and therefore subject to income tax.

The taxpayer appealed against assessments issued by HMRC under section 957, Income Tax Act 2007. The assessments were issued on the basis that the taxpayer should have deducted basic rate income tax from loyalty bonuses paid to investors.

**FTT decision**

The appeal was allowed.

The issue before the FTT was whether the payments made by the taxpayer to investors required it to deduct and account for sums representing income tax on those payments because they were "annual payments" for the purpose of section 683, ITTOIA.

The FTT observed that section 683 does not define "annual payments". However, case law had established that an annual payment bore the following four characteristics:

1. was payable under a legal obligation
2. recurred or was capable of recurrence (although the obligation to pay could be contingent)
3. constituted income and not capital in the hands of the recipient, and
4. represented "pure income profit" to the recipient.

The taxpayer accepted that the loyalty bonus payments constituted income and not capital in the hands of investors, but disputed that the remaining criteria were satisfied.

*Legal obligation*
Whether there was a binding legal obligation to make the payments depended on whether the taxpayer had a contractual obligation to pay the loyalty bonus to investors who satisfied the relevant criteria. Before the FCA's rule change, the taxpayer's terms and conditions expressed the loyalty bonus as a percentage of funds invested, or a reduction in the net AMC for particular funds. After the introduction of the new rules, it was shown as "an ongoing saving from [the taxpayer]" expressed as a percentage.

The FTT concluded that that language was apt to describe an offer by the taxpayer to pay a stated amount as a loyalty bonus at the end of a month, capable of acceptance by an investor who satisfied the criteria the taxpayer had set for that month.

The investor was on notice that the amount and frequency of the loyalty bonus could be changed, but not with retrospective effect. Therefore, at the end of a given month the taxpayer would be bound to pay the loyalty bonus to an investor who satisfied the criteria. After the introduction of the new FCA rules, it was even clearer that the loyalty bonus payments were made by the taxpayer under a binding legal obligation because under the FCA's Code of Business Sourcebook, it was obliged to pass on the full amount of any rebate from an investment provider.

*Capable of recurrence*
The taxpayer argued that if an offer could be withdrawn at any time, the necessary feature of recurrence was lacking.

The FTT disagreed with such an approach which it considered would deprive the words "capable of" of any substantive meaning and would extend the first characteristic so that it was necessary to establish a continuing binding legal obligation with the minimum period of such continuance at large. The loyalty bonus payments recurred over many months and they were not prevented from being recurrent simply because they were dependent on a contingency. Nor were they prevented from being annual because they were made monthly, provided they might continue beyond a month. Section 683(3) states that the frequency with which payments were made is to be ignored in determining whether such payments are "annual payments".

*Pure income profit*
The FTT said that examples of annual payments given in *Campbell v Inland Revenue* [1970] AC 77 were a signpost to the primary intent and purpose of section 683, which was to identify a category of payments where the payee had satisfied his substantive obligation at the outset of the contract or agreement.

The FTT concluded that the AMC deprived the loyalty bonus of its character as pure income profit. The AMC was a compulsory charge directly borne by the investor as a term of investing through the taxpayer and that investors would (or should) have understood that the AMC would be reduced by the loyalty bonus. The FTT said:

"The assertion by HMRC that an investor does not need to pay or bear an AMC to receive a Loyalty Bonus and that there is nothing in the contract between HL and investors to impose the AMC ignores the plain terms on which HL offers and permits investment to be made.

Investment on terms that HL would meet what I have found (and HMRC assert) to be a binding legal obligation to pay the Loyalty Bonus each month, but without the recipient being charged the applicable AMC, is not an option, and would be a commercial nonsense. Yet that in substance is what HMRC say occurs when a Loyalty Bonus is received, because it is 'pure income profit'."

The FTT concluded that the nature and quality of the loyalty bonus was such that it was not a "profit" to an investor, but rather a reduction of the net cost. This reflected the true factual matrix. The FTT said it was unlike an annuity payment, or interest, in respect of which a recipient need do nothing but sit back and receive the payments.

Accordingly, the FTT held that the loyalty bonus payments could not constitute annual payments as they were not pure income profit.

**Comment**
This decision provides a useful consideration and summary of the relevant case law relating to the meaning of "annual payments".

It is also worth noting that the FTT considered the proposition put forward by HMRC, that the taxpayer would meet a binding legal obligation to pay the loyalty bonus each month, without the recipient having to pay the relevant charges in relation to his investment, to be 'commercial nonsense' and simply not a true reflection of the facts. HMRC regularly argues in tax disputes that the facts must be viewed realistically, normally in a situation where the facts are unhelpful to its case. It would appear that it failed to review the facts realistically in this instance.

A copy of the decision is available to view here.

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## *Hicks*: Discover the limits

In *J Hicks v HMRC* [2018] UKFTT 22, the FTT, in allowing the taxpayer's appeal, has held that discovery assessments issued by HMRC were invalid as the condition contained in section 29(5), Taxes Management Act 1970 (TMA), was not satisfied.

The below is based on an article first published in Tax Journal on 23 March 2018. A copy of that article is available to view here.

**Background**
In 2009, John Hicks (the taxpayer) entered into a tax avoidance scheme devised by Montpelier, which had been disclosed to HMRC under the DOTAS rules. The scheme generated a loss for the taxpayer of some £1.2m. On 27 January 2010, the taxpayer submitted his tax return for 2008/09, which showed the loss of £1.2m as available to be carried forward and the scheme reference number (SRN), which had been allocated to the scheme by HMRC. On 3 December 2010, HMRC opened an enquiry into the return.

On 8 January 2011, the taxpayer submitted his return for 2009/10 and on 31 January 2012, he submitted his return for 2010/11. Both returns showed a carried forward loss from 2008/09 that eliminated all taxable profit. HMRC did not open an enquiry into either of the returns.

In March 2015, HMRC issued discovery assessments, under section 29, TMA, in relation to the taxpayer's 2009/10 and 2010/11 returns. The assessments were upheld by HMRC following an internal statutory review. The taxpayer appealed the assessments to the FTT.

The appeal raised four issues:

1. whether HMRC had made a "discovery", within the meaning of section 29, TMA
2. whether HMRC was prevented by the conclusions of its statutory review from relying on an insufficiency of disclosure to permit the discovery assessment which had been issued in relation to the 2010/11 year
3. if the answer to (2) was no, whether a discovery assessment was permitted for 2010/11, on the basis of an insufficiency of disclosure, and
4. whether the taxpayer was careless, for the purposes of section 29(4), so as to permit a discovery assessment to be made for either or both of 2009/10 and 2010/11.

**FTT decision**
The appeal was allowed.

*Issue 1*
The FTT began by setting out the genesis of present day section 29. It stressed, by reference to the Court of Appeal's dicta in *Tower McCashback LLP 1 v HMRC* [2010] EWCA Civ 32, that the current section 29 was far more restrictive than its predecessor, which was enacted before the introduction of the self-assessment regime in 1996.

The FTT was required to determine two questions: first, did the officer "cross a threshold", as discussed below and second, was the issue of the assessments sufficiently proximate to the discovery.

HMRC presented witness evidence from Mr Boote, the officer who authorised the issue of the discovery assessments. The FTT, in considering his evidence, commented that Mr Boote had been somewhat opaque in describing the process. Mr Boote's evidence was that the decision to issue the discovery assessments, which were issued a few days before the expiry of the statutory time limits, was not informed by the impending deadline. However, the FTT concluded that it would have been "extraordinarily unlikely" that the process was not so informed.

The taxpayer contended that the discovery had become "stale" by the time the assessments were issued. The concept of assessments becoming "stale" was discussed in *Pattullo v HMRC* [2016] UKUT 270 (TCC), where it was held that an officer could not assess for tax sometime after he had made the relevant discovery without first acting on the discovery in some way. HMRC presented evidence of the fact finding exercise it claimed to have carried out over several years, culminating in its decision to issue the discovery assessments at the end of 2014. The FTT confirmed that the threshold for HMRC to demonstrate that a discovery had been made was low (*HMRC v Charlton* [2012] UKUT 770 (TC)) and that, on the facts of this case, it was likely that it had made a discovery around the summer of 2014.

*Issue 2*
The taxpayer argued that HMRC was shut out from running any argument in respect of section 29(5). His argument was that, since sections 49F and 54, TMA , treat the decision of the HMRC reviewer as final, except "to the extent that the appellant notifies the appeal to the tribunal", HMRC could not subsequently seek to rely on section 29(5) as the reviewer's decision had determined that issue against HMRC.

HMRC argued that this analysis was misconceived and that the review "decision" was to uphold HMRC's decision to issue the discovery assessments. The validity of HMRC's reasons for doing so was not part of the deemed settlement. The FTT decided this issue in favour of HMRC.

*Issue 3*

The condition in section 29(5) requires that, at the time when the enquiry window closed, a hypothetical HMRC officer could not reasonably have been expected, on the information made available to him before that time, to be aware of the insufficiency of tax. The frequently cited cases of *Langham v Veltema* [2004] EWCA Civ 193, *Charlton*, *Patullo* and *Sanderson v HMRC* [2016] EWCA Civ 19, were considered by the FTT.

The FTT indicated that the previous authorities presented it with some difficulties in terms of application and said:

"… how certain does the hypothetical officer have to be for it to be unreasonable for him not to be 'aware' of the insufficiency? Is it enough if the hypothetical officer could have concluded on the basis of the information then available that HMRC would have a good case in proving an insufficiency? Does awareness mean that HMRC would be more likely than not to succeed if the matter were contested, or some other level of certainty? Further, is awareness of an insufficiency different from the real HMRC officer crossing the threshold in a discovery and if so how?

I confess that I do not find the Court of Appeal's analysis of these issues in Sanderson, which is of course binding on me, entirely easy to understand or apply in practice. In particular, I do not find the phrase 'actual insufficiency' helpful as a measure of awareness, because the natural reading of those words in my view is that awareness of an actual insufficiency would (save perhaps for a glaring error or omission) be established only when a matter had been tested or settled."

The FTT concluded that the practical effect of *Sanderson* is to require the exercise to focus on the level of disclosure in any particular case, and the extent to which that disclosure arms the hypothetical officer with sufficient information to justify the making of an assessment. The FTT commented:

"Subsection (5) is all about disclosure by the taxpayer (as defined by section 29(6)). The more extensive the taxpayer's disclosure by the closure of the enquiry window, the more difficult it would be for HMRC to establish that the hypothetical officer could not reasonably have been expected to be aware of the insufficiency. The taxpayer is incentivised by the legislation to place HMRC in a position where he can put them to proof at the close of the enquiry window with the question 'what more need I have disclosed to have placed the officer in a position to be justified in raising an assessment?'".

The taxpayer's return had included his participation in the scheme referred to by the SRN. His return had also showed a significant tax loss and a matching non-taxable receipt. The information made available to HMRC before the closure of the enquiry window had included details of the dividend trades claimed to give rise to the loss; "reasonably extensive" information in relation to the transactions implemented under the scheme arrangements; and information regarding the trading activities undertaken before the scheme trades by the taxpayer in his regular financial trade.

Perhaps not surprisingly, the FTT concluded that the hypothetical officer had sufficient information, at the time the enquiry window had closed, to establish an insufficiency of tax. This was particularly so as the central issues were not matters of great complexity. The FTT said:

"… I do not consider that subsection (5) allows or is intended to allow HMRC to issue assessments which ignore the normal time limits while they spend further time in polishing a justifiable assessment as at the closure of the enquiry window into a knockout case.

… Mr Nawbatt is correct to state that HMRC's process of gathering information in relation to the Scheme was continuing when the enquiry window closed. However, that is not carte blanche for HMRC to omit to open an enquiry—whether intentionally or by omission—and then simply rely on subsection (5) in every case to issue assessments which would otherwise be out of time. The statutory time limits for assessments are a critically important safeguard for the taxpayer, just as the onus of disclosure on the taxpayer, and the duty not to act carelessly or deliberately, are a protection for HMRC where those limits are not met."

*Issue 4*

With regard to issue 4, the FTT noted that the authorities on this issue "are in conflict". In *Atherton v HMRC* [2017] UKFTT 831 (TC), the FTT reached a different conclusion to that reached by the FTT in *Bessie Taube Trust v Revenue & Customs* [2010] UKFTT 473 (TC). In *Atherton*, the FTT concluded that it could not have been Parliament's intention for a taxpayer to avoid any liability on the basis that he had derogated certain obligations to a third party. In the current appeal, the FTT noted:

"In my respectful opinion, the tribunal in Atherton misinterprets the quoted passage in Bessie Taube. It appears to consider the consequence of Judge Berner's approach to be that a taxpayer can escape his statutory duties and avoid the consequences of being careless by 'passing on' his statutory liabilities to a third party who, the taxpayer alleges, is not acting on his behalf. I do not read anything in section 29, or the passage from Bessie Taube, as having this effect … The consequence for the taxpayer of carelessly submitting a return with an insufficiency is not narrowed by these words but potentially widened, to (in effect) treat the carelessness of the person acting on the taxpayer's behalf as the taxpayer's carelessness. Where a taxpayer seeks to rely as a defence on the advice of a third party who did not act on his behalf, the issue then is the taxpayer's carelessness."

In terms of defining "carelessness" for the purposes of section 29(4), the FTT relied on the reasoning of the FTT in *Alan Anderson v HMRC* [2016] UKFTT 335 (TC), where it was stated:

"Our view is that the correct approach in this context also is to follow that adopted in Collis and Hanson of assessing what a reasonable hypothetical taxpayer would do in all the applicable circumstances of the actual taxpayer."

In the view of the FTT, the issue was not whether the taxpayer or Mr Bevis (his agent) was careless in general, or in the abstract, but whether their failure to take reasonable care brought about the insufficiency in the 2008/09 return, or the two subsequent returns.

In the view the FTT, it is not necessarily careless (for the purposes of section 29(4)) to enter into a tax avoidance scheme, even in the knowledge that HMRC might challenge the taxpayer's interpretation of the legislation. The FTT also rejected HMRC's argument that the taxpayer had been careless to claim a loss in his 2010/11 return, when his 2009/10 return was under enquiry in relation to the same scheme. In the view of the FTT, at that time, the enquiry into the taxpayer's 2009/10 return was still a typical HMRC enquiry. The FTT therefore concluded that the taxpayer had not been careless for the purposes of section 29(4).

**Comment**
This is an important decision as it contains a detailed analysis of section 29(5) and the conditions which must be satisfied in order for HMRC to be able to issue a valid discovery assessment.

On the facts of the case, the disclosure which had been made to HMRC, and the inclusion of the SRN in the taxpayer's tax return, was sufficient to prevent HMRC from successfully arguing that the condition in section 29(5) had been satisfied.

Consistent with *Charlton*, the inclusion by the taxpayer of the SRN in his tax return was considered by the FTT to be sufficient disclosure. We are aware that HMRC regularly argue that inclusion of an SRN in a taxpayer's return is insufficient disclosure for the purposes of section 29(5). It is to be hoped that the approach adopted by the FTT in this case will be followed by future tribunals.

Interestingly, the HMRC reviewing officer in this case had advised HMRC against relying on section 29(5), because no further information became available to HMRC between closure of the enquiry period and the date on which the assessments were issued.

A copy of the decision is available to view here.

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## *Jackson*: HMRC penalised in penalties case

In *Jackson v HMRC* [2018] UKFTT 0064 (TC), the FTT has held that HMRC had misapplied the law in respect of penalties it had issued to the taxpayer for filing late returns.

The below is based on an article first published in Taxation on 28 March 2018. A copy of that article is available to view here.

**Background**
Since 6 April 2015, disposals of UK residential property by non-UK residents have been subject to non-resident capital gains tax (NRCGT). A return must be filed within 30 days of disposal of the relevant property.

Alan Leslie Jackson (the taxpayer) was non-UK resident for tax purposes. He disposed of two properties in the UK in May and September 2015, with no gain arising.

In line with the other cases on this subject (*Rachel McGreevy v HMRC* [2017] UKFTT 690 (TC); *Hesketh v HMRC* [2017] UKFTT 871 (TC); *Robert Clive Welland v HMRC* [2017] UKFTT 870 (TC); and *Patsy-Anne Saunders v HMRC* [2017] UKFTT 0765 (TC)), the taxpayer did not realise that the rules had changed, creating an additional filing obligation. It was his intention to comply with what he thought was the relevant deadline and to this end he visited his accountant on 1 October 2016 to discuss his annual self-assessment return which had to be filed by 31 January 2017. It was on this visit that he became aware of the change in the law and immediately completed the required NRCGT returns which showed that no capital gain had been made on the disposal of either property and as a consequence no capital gains tax was due. The returns were received by HMRC on 2 October 2016 and as they were late, HMRC issued eight penalties, pursuant to paragraphs 1, 3, 4, 5 and 6, Schedule 55, Finance Act 2009.

The penalties originally totalled £3,200, which included daily penalties of £1,800. HMRC exercised its discretion to reduce the daily penalties to nil leaving a balance of £1,400 outstanding (£100 for being late, £300 for being six months late and £300 for being twelve months late in respect of each property).

The taxpayer appealed against the penalties claiming that the returns were submitted late due to the fact that he had missed the relevant changes in UK tax law in respect of when notification was to be made.

**FTT decision**
The appeal was allowed.

The taxpayer contended that the penalties were disproportionate and should not have been issued.

HMRC contended that the taxpayer had an obligation to stay up to date with legislation affecting his activities in the UK. On the sale of his UK properties, HMRC expected the taxpayer, acting as a prudent person, exercising reasonable foresight and due diligence and having proper regard to his responsibilities under the Tax Acts, to have researched what is required of him. HMRC further contended that the taxpayer did not take care to avoid the failure to ensure that the NRCGT returns were filed within the statutory 30 day time limit and did not have a reasonable excuse for this failure.

In determining the appeal, the FTT considered whether:

1. HMRC had correctly addressed and notified the penalties
2. HMRC had applied the penalty legislation correctly including in relation to the calculation of the amount of the penalties
3. the taxpayer had a reasonable excuse for his failure to submit the returns on time
4. there were special circumstances which would allow HMRC to reduce the penalties and whether HMRC's decision on special circumstances was flawed
5. the penalties were disproportionate, harsh or unfair.

*Issue 1*
Issue 1 was determined in favour of HMRC as the taxpayer had referred to the penalty notices in correspondence, albeit HMRC could not produce copies of the notices.

*Issue 2*
Paragraph 3, Schedule 55, Finance Act 2009, imposes a fixed penalty of £100 if a return is submitted late. This is a fixed penalty with no reference to the amount of tax due. The FTT concluded that HMRC had applied this aspect of the legislation correctly and upheld those penalties.

With regard to the remaining penalties (issued under paragraphs 5 and 6, Schedule 55, which provide that a penalty issued under those paragraphs is the greater of (i) 5% of any liability to tax which would have been shown in the return in question, and (ii) £300), the FTT concluded that HMRC had erred in its interpretation of the legislation.

It was accepted by HMRC that with regard to the disposal of each property, no capital gains tax was due. Accordingly, in determining which was the greater, HMRC proceeded on the basis that as 5% of a nil liability to tax is nil, the penalty should be in the greater amount of £300. HMRC had issued two penalties, each in the sum of £300, in respect of each property.

The FTT observed that in making these four penalty calculations, HMRC had to consider the taxpayer's liability to tax and said:

"The Tribunal considers that in making the 4 assessments of £300 HMRC have overlooked the provisions of paragraphs 1(3) and 17 (3) of Schedule 55. Paragraph 17(3) states:

(3) Where P is liable for a penalty under more than one paragraph of this Schedule which is determined by reference to a liability to tax, the aggregate of the amounts of those penalties must not exceed 100% of the liability to tax.

It is clear that the appellant was liable to a penalty under more than one paragraph of Schedule 55 namely paragraphs (3),(4),(5), and (6) albeit HMRC have cancelled or withdrawn the daily penalty described in paragraph (4) … . The penalties under paragraphs (5) and (6) for each disposal were all notified to the appellant by HMRC on the same day, 21 November 2016, so HMRC must have been aware for each disposal that they had notified more than one penalty determined by reference to a liability to tax.

**It is accepted that the tax liability for each disposal is nil. 100% of a nil liability to tax is nil. Therefore the aggregate of the penalties determined by a liability to tax must not exceed nil.** The Tribunal has therefore applied this provision and concludes that none of the four penalties of £300 should have been assessed." (Emphasis added).

The FTT therefore concluded that none of the four penalties of £300 should have been issued.

*Issue 3*
The taxpayer's "reasonable excuse" for failing to file the returns on time was that he was unaware of the relevant legislative changes concerning filing deadline dates. Following the reasoning of the FTT in *Robert Clive Welland v HMRC* [2017] UKFTT 870 (TC), the FTT concluded that ignorance of the law did not provide the taxpayer with a reasonable excuse for the late filing of his returns.

*Issues 4 and 5*
Paragraph 16(1), Schedule 55, Finance Act 2009, allows HMRC to reduce a penalty below the statutory minimum if there are "special circumstances".

In concluding that the taxpayer was able to rely upon such special circumstances, the FTT again referred to the *Welland* decision in which the FTT had held that the taxpayer in that case had not been given an opportunity to correct his behaviour. In *Welland*, the taxpayer had sold three properties and incurred three penalties before he became aware that he was required to submit a NRCGT return within 30 days of the date of disposal of the properties. In allowing the taxpayer's appeal, the FTT held that there were special circumstances that would engage HMRC's discretion to reduce the penalty under paragraph 16(1). This was because the taxpayer had made three property sales in quick succession and so was unable to learn from his non-compliance with the NRCGT reporting deadline. The FTT therefore considered that only the first out of the three penalties should be payable.

In the present case, and in line with *Welland*, the FTT concluded that the 6 month and 12 month penalties should not have been issued and cancelled them because the taxpayer had not been given an opportunity to learn from his non-compliance.

In relation to whether the penalties were disproportionate, harsh or unfair, the FTT said:

"... HMRC consider that there are no special circumstances that gave rise to the late submission and the Tribunal considers that HMRC's decision on that is flawed. It must be unusual for an appellant to receive eight penalties on one day in respect of two failures. The fact that all the penalties were issued on the same day clearly gave the appellant no opportunity to correct his behaviour or learn from his first mistake. It is clear that the system of penalties is designed in such a way as to progressively penalise a taxpayer until he rectifies his error. Eight penalties in one day denied the appellant that opportunity. Therefore the Tribunal has decided there were special circumstances and reduces the penalty to nil."

The FTT therefore reduced the penalties to nil in relation to the second return, and confirmed that the penalty of £100 in relation to the first return was correctly imposed, for the reasons set out in *Welland*, namely, that a taxpayer should be given an opportunity to affect future compliance. Issuing more than one penalty in one day was contrary to that requirement.

**Comment**

This decision confirms the view of the FTT expressed in *Welland* that, as the taxpayer had had no opportunity to correct his behaviour between the two late returns, special relief should be given to reduce the penalties on the second return to nil.

Perhaps of greater significance is the view expressed by the FTT in relation to Issue 2. The FTT noted that where a penalty is raised under more than one paragraph of Schedule 55, which is determined by reference to a liability to tax (ie a "tax geared" penalty), paragraph 17(3) limits the total amount of those penalties to 100% of the tax liability. This means that where there is no tax liability, the total amount of penalties issued under more than one paragraph of Schedule 55, which are determined by reference to a liability to tax, will be nil. In this case, the FTT determined that the taxpayer was subject to more than one tax geared penalty and therefore, given that the total amount of tax payable was nil, the total liability of the penalties issued under paragraphs 5(2) and 6(5) should not exceed nil.

However, such an interpretation could lead to an anomalous result. For example, a taxpayer is required to file his 2015/16 self-assessment return by 31 January 2017. If we assume that no tax is due and the taxpayer misses this date, HMRC may issue a flat rate penalty of £100 under paragraph 3, Schedule 55. If the taxpayer continues to fail to file his return until 29 July 2017, HMRC may impose a flat rate daily penalty of £10 per day under paragraph 4(2), Schedule 55. If the return remains unfiled until 2 August 2017, HMRC may impose a penalty of 5% of any liability to tax or £300, whichever is the greater, under paragraph 5(2), Schedule 55.

So far so good, as paragraph 17(3) does not apply because the taxpayer is not subject to a tax geared penalty under more than one paragraph of Schedule 55. However, if the return is not submitted until, say, 14 March 2018 (ie more than 12 months after the due filing date of 31 January 2017), HMRC may impose a penalty of 5% of any liability to tax or £300, whichever is the greater, under paragraph 6(5), Schedule 55. In such circumstances, paragraph 17(3) would apply as there are now two tax geared penalties (imposed under paragraphs 5(2) and 6(5)) and it would appear from the FTT's decision in *Jackson* that the aggregate of all the penalties imposed under paragraphs 5(2) and 6(5) cannot exceed 100% of the liability to tax which, on the facts of our example, is nil. Accordingly, the aggregate of all the penalties imposed under paragraphs 5(2) and 6(5) would also be nil. If correct, this means that by delaying submission of his return by more than 12 months the taxpayer can escape all penalties imposed under these paragraphs.

An alternative interpretation, which would avoid such an anomalous result, would be to treat penalties imposed under paragraphs 5(2)(a) and 6(5)(a) as tax geared penalties and treat penalties imposed under paragraphs 5(2)(b) and 6(5)(b) (ie the £300 penalties) as flat rate penalties.

A copy of the decision is available to view here.

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