Croner Tax Briefing – HMRC Penalties

What is Deliberate Behaviour?

Rumour has it that HMRC is taking a harder stance on the application of penalties during enquiries. This translates to them applying the penalty for deliberate behaviour to situations that others might characterise as no more than a failure to take reasonable care. The primary effect of this is to increase the maximum penalty loading for a prompted case from 30% to 70%.

This has recently resulted in a number of cases where the Tribunals have sought to clarify the question of what is "deliberate behaviour" and, in fact, on a brief review of recent cases, there have been 25 cases where the Tribunal has attempted to consider the matter of deliberate behaviour. Most of these were VAT cases and, strikingly, most of them were won by HMRC. One of the more recent of these is a VAT case but, since the legislation at Schedule 24 FA2007 is common to both direct and indirect tax, the principles apply equally.

In *Mr Anthony Clyne v The Commissioners for H M Revenue & Customs [2016] TC05123*, the case concerned the alleged misuse of the VAT flat rate scheme where the company did not meet the turnover qualification necessary to use the scheme. A penalty of £65,660 was assessed based on the assertion that the taxpayer's actions were deliberate. The normal range in an unprompted disclosure would be 35-70% of the potential lost VAT revenue, mitigated according to the level of Telling (HMRC about any irregularities), Helping (HMRC actively to progress the case) and Giving (HMRC access to all information necessary to expedite the resolution of the enquiry).

In this case, the final penalty loading was 64.75% of the VAT under assessed which, in the context of HMRC's previous attitude to assessing penalties, since they were first introduced in 2009 counts as a particularly aggressive.

However, what is instructive is the Tribunal's consideration of the word 'deliberate' at paragraph's 80-82 (reproduced below).

> *80. There is some suggestion in materials published at the time that the penalty*

PHONE 0844 561 8101
EMAIL consultancy@cronertax.com
ONLINE www.croner.co.uk

provisions were revised in 2007, that the use of the new terms was not intended to make any material change to the tests which applied previously. In the explanatory notes published with the draft legislation in 2007, it was stated that the new terms of deliberate and careless behaviour were to "provide a uniform language for behaviours, using more accessible language across the taxes covered." However, our view is that, even if it is permissible to look to such materials for guidance as to the intent of Parliament in interpreting legislation, the statements in the materials are not sufficient to conclude that the new terms are simply interchangeable with the previous ones. Parliament has chosen to use different words and it is those words which must be interpreted. The starting point must be that the term "deliberate inaccuracy" has to be interpreted according to the usual principles of statutory interpretation. In our view, therefore, cases on the meaning of "dishonesty" are not of material assistance in interpreting the provisions of schedule 24 as regards "deliberate" conduct.

81. On that basis we must seek to interpret the relevant provisions in schedule 24 according to their natural meaning looking at the context of their use in the overall scheme of schedule 24. We take the dictionary definition of the term "deliberate" as a starting point which states (in the Oxford English dictionary) that deliberate (as regards action) means:

"Well weighed or considered; carefully thought out; formed, carried out, etc. with careful consideration and full intention; done of set purpose; studied; not hasty or rash."

82. On its normal meaning, therefore, the use of the term indicates that for there to be a deliberate inaccuracy on a person's part, the person must to some extent have acted ***consciously, with full intention or set purpose or in a considered way***

Croner Tax has been arguing for some time that HMRC's application of penalties on the deliberate scale has been unjustified. Indeed in a recent case, a widow who had inherited the farm from her deceased husband and who was relying on the advice of her husband that a particular type of income was exempt from tax was adjudged by HMRC to have acted deliberately in failing to seek advice on the income, despite the fact that it had been received by her husband for the 10 years before he died and she had no reason to question his judgement.

Which brings us neatly to the fly in the ointment in the Clyne case. Para 86 of the judgement states:

86. However, we consider that the term "deliberate inaccuracy on a person's part" can extend beyond this. Our view is that, depending on the precise circumstances, an inaccuracy may also be held to be deliberate where it is found that the person consciously or intentionally chose not to find out the correct position, in

particular, where the circumstances are such that the person knew that he should do so. A person cannot simply escape liability by claiming complete ignorance where the person clearly knew that he should have taken steps to ascertain the position. We view the case where a person makes such a conscious choice not to take such steps with the result that an inaccuracy occurs, as no less of a "deliberate inaccuracy" on that person's part than making the inaccuracy with full knowledge of the inaccuracy.

There is not much to disagree with here. If you consciously or intentionally chose not to find out the correct position, by definition, you've taken a deliberate (in)action. Where I might depart from HMRC's view is, with regard to my widowed client, she didn't *know* that her husband's previous treatment of the income was incorrect, so why would she question the treatment of income that hadn't been queried in over a decade?

The support for that defence is later on the above paragraph where it states that '*a person cannot simply escape liability by claiming complete ignorance where the person* ***clearly knew*** *that he should have taken steps to ascertain the position'.* It is HMRC's assertion in this and similar cases that they 'should have known', ergo, their actions are deliberate. This conveniently leaves out the necessity of ascertaining whether they did *clearly know* they should have taken advice.

In fact, in some cases, HMRC have boiled their approach down to an assertion that there is plentiful information available in HMRC's manuals that clearly states the correct tax position, so, if you haven't looked at this, your actions must be deliberate.

However, we should pause to consider the difficulties that Compliance Officers face since the Government and HMRC are asking Officers, in marginal cases (and the margin is very wide here) to assess the subjective intentions of a taxpayer, possibly going back several years. So, whilst the dictionary definition is helpful in articulating exactly what deliberate action is, for practical purposes, proving it, even on a balance of probability, is an immensely difficult task. Accordingly, if HMRC persists in going down this route, the Tribunal Service may well be busy over the next few years deciding on the finer points of subjective intention of taxpayers.

The Tribunal did just that in the Clyne case and, in what appeared to be a well-reasoned decision by the Tribunal, they dismissed the taxpayer's appeal and upheld the penalty in its entirety. In that case, there were indications that he 'clearly knew' he should have taken further steps to establish the qualification turnover limit for the VAT flat rate scheme and his professional qualification as an accountant appeared to militate against him.

Nevertheless, we do now have some case law guidance that may assist taxpayers in defending against any attempt by HMRC to make blanket assertions on whether a clients' actions are deliberate.

Neil Tipping is a Senior Tax Consultant with Croner Tax and can be contacted on 0844 728 0120 and neil.tipping@cronertax.com

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