[2017] UKFTT 428 (TC)

TC05892

Appeal number: TC/2016/03907

Income tax – penalty for inaccuracy due to failure to take reasonable care – inaccuracy was claim for repayment of UK income tax withheld from pay – no income tax was in fact withheld - appellant was pregnant, gave birth and resident abroad during period for preparation of tax return – held: appellant failed to take reasonable care to avoid inaccuracy – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

JESSICA THORNLEY **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS ("HMRC") **Respondents**

TRIBUNAL: JUDGE ZACHARY CITRON
JOHN CHERRY

Sitting in public at Fox Court, London on 1 March 2017

The Appellant did not appear and was not represented

Mr Stefan Paris, Officer of HMRC, for the Respondents

DECISION

1. This issue in this case was whether an inaccuracy in the appellant's tax return was due to her failure to take reasonable care.

2. Neither the appellant, nor her accountants, Shenkers, attended the hearing. At the hearing, Mr Paris provided to the tribunal:

(1) An email from Shenkers to Mr Paris dated 23 February 2017 stating that the appellant would not be attending the hearing and would not be represented; it said "the submissions made will stand as the [appellant's] submissions."

(2) A letter from Shenkers to HMRC dated 10 February 2017 stating that they sought a "variation" to the tribunal's directions to the effect that "the appellant's evidence served by way of her grounds of appeal and by way of her agent's statements dated 9 March 2016 be admitted as her evidence before the tribunal."

3. We considered rule 33 of the Tribunal's rules and found that the appellant had notice of the hearing and that it was in the interests of justice to proceed. We did not consider it necessary to make an order of the kind proposed by Shenkers, as we would consider all the evidence previously provided by the appellant (and her representatives, Shenkers) to the tribunal.

The appeal

4. On 21 October 2015 HMRC issued a penalty assessment notice on the appellant under paragraph 1 Schedule 24 Finance Act 2007 in the amount of £1,594.13. This was done on the basis that the appellant's tax return for the 2012-13 tax year contained an inaccuracy which was "careless" as defined in paragraph 3(1) Schedule 24 Finance Act 2007.

5. On 9 March 2016 Shenkers requested a review of HMRC's decision to assess the penalty. On 22 June 2016 HMRC issued a review conclusion letter upholding their decision.

6. The appellant notified her appeal to the tribunal by notice of appeal dated 20 July 2016.

Evidence

7. We had a document bundle containing copies of correspondence between the parties. We reproduce in the paragraphs below extracts from three letters from Shenkers to HMRC that contained some of the more material evidence (on the basis of which we make our findings of fact in the following section of this decision).

8. On 19 May 2015, following the opening of enquiries into the appellant's 2012-13 tax return, Shenkers wrote a letter to HMRC which included the following:

> "We submitted [the appellant's] tax return for the [2012-13] year based on the information provided to us. However, up to August 2012, [the appellant] was treated as trading as a self-employed aid worker by GirlHub. From that date, she became employed by the company and was treated as an employee under the payroll scheme as shown in the attached P60 for the year ending 5 April 2013.
>
> We were not provided with this document when we prepared [the appellant's] 2013 tax return and relied on a spreadsheet provided to us by [the appellant] that tax had been deducted by GirlHub. This was the amount of £10,526 that we have claimed as being overpaid.
>
> It appears from the P60 that there was no tax due or paid by [the appellant].
>
> …
>
> Following the clarification of the employment status for [the appellant], we now realise that the 2012-13 tax return is incorrect and we should ask you whether you wish us to resubmit the return with the correct information or just provide information to you in writing."

9. Following further questions from HMRC, Shenkers wrote a letter to HMRC on 8 July 2015 which included the following:

> "When we commenced to act for [the appellant], it was on the basis that she was trading as a self-employed worker under the auspices of GirlHub … We prepared accounts to 5 April 2012 on a self-employed basis, having registered [the appellant] with Longbenton.
>
> [The appellant] then advised us that, from 1 October 2012, GirlHub were putting all their workers on to an employment basis with a new contract. We, therefore, prepared accounts up to 30 September 2012. It is only after this investigation commenced that [the appellant] supplied us with her employment contract and P60s from 2013 and 2014.
>
> [The appellant] then supplied us with a schedule (see attached) showed tax 'deducted' for the months of employment during 2012-13 and since she was unable to locate her P60 at that time, we assumed that this tax had been deducted by GirlHub and because [the appellant] was working overseas for more than the prerequisite days, she was entitled to a refund of this tax deducted. We were unaware that was just a memo list.
>
> ….
>
> From my recent discussions with [the appellant], it appears that inadvertently we were not given the correct information to return the 2012-13 tax return correctly and would request that since there was no tax due in any case, that all penalties be cancelled in the light of this current information."

10. HMRC asked further questions and Shenkers' response of 22 July 2015 included the following:

> "The schedule sent with our last letter that was headed "Employees Tax Withheld in Rwanda" was, in fact, an internal schedule generated by [the appellant] who had advised us that there had been a changeover in procedures within GirlHub in

September 2012. We had understood that she had recorded this information from her payslips which she could not provide to us. As explained in the previous letter, we were under the impression that the tax had been deducted by GirlHub in their UK payroll scheme.

We would answer your questions as follows:

(1) [*HMRC had asked: Was the appellant expecting a refund of UK tax to be due on completion of her return?*] We were communicating with [the appellant] regarding her 2012-13 tax return soon after the birth of her first child when she was home in New Zealand on maternity leave. We believe that [the appellant] did not really understand at that time the intricacies with regard to the tax return. We would suspect that her state of mind was affected by the fact that she was not in a working environment and, consequently, not in a position to really understand what was being returned at the time.

(2) [*HMRC had asked: What was the intended purpose of the spreadsheet provided to Shenkers detailing amounts of tax withheld in Rwanda?*] We understood the schedule to be tax deducted in the absence of the P60. However, we believe [the appellant] was given this information by GirlHub as the expected tax that would be deducted when in the discussions with the payroll personnel regarding the changeover from self-employment status to employment.

(3) [*HMRC had asked: On completion of the return, did the appellant check the return and sign it as complete and correct to the best of her knowledge?*] [The appellant] approved the return but we expect the circumstances in number 1 apply here as well.

(4) [*HMRC had asked: Did the appellant receive a copy of the tax calculation resulting from the completion of her return, showing a repayment of tax due of £10,627.59? If so, did she contact Shenkers or HMRC for an explanation of the refund?*] [The appellant] received the tax calculation from us on 30 January 2014 with her repayment of tax showing as £10,627.59. Given that we were pressurising her to confirm her agreement in order to file before the deadline, we expect [the appellant], given the circumstances above, did not check the tax return thoroughly."

Findings of fact

11. On 6 April 2013 HMRC gave notice to the appellant under s8 Taxes Management Act 1970 ("TMA") that she should provide a self assessment tax return to HMRC for the 2012-13 tax year. During that tax year, the appellant lived in Rwanda (and was tax resident there), working as a charity support worker for a UK based organisation called GirlHub Ltd.

12. The appellant went on maternity leave in July 2013 and had a baby in August 2013. Shortly afterwards, she returned with the baby to her family home in New Zealand.

13. Shenkers, who had acted as the appellant's accountants and tax agent since November 2011, were instructed to prepare her 2012-13 tax return. The appellant told Shenkers that, from 1 October 2012, her employment status was due to change from being self employed to being an employee of GirlHub. She also gave Shenkers a one-page schedule (the "schedule") entitled "Employees Tax Withheld In Rwanda (Pay

As You Earn)" and sub-titled "Employee Name: Jessica Thornley". It had three columns under the following headings:

(1) Months (from October 2012 to October 2013 inclusive)

(2) "Gross" in GBP

(3) "Taxes" in GBP

The figures for "taxes" in the schedule for the months October 2012 to March 2013 inclusive totted up to £10,627.59. The "gross" figures for those months totted up to £34,998.

14. In preparing the appellant's 2012-13 tax return, Shenkers assumed that the amounts shown in the "taxes" column of the schedule were UK income tax deducted by GirlHub. It was Shenkers' understanding that because the appellant was resident in Rwanda for that tax year, she was entitled to a refund of these amounts. The appellant's form P60 for the 2012-13 in respect of her employment by GirlHub, which was not provided to Shenkers during the period when they were preparing the appellant's tax return, indicated that no UK income tax had been deducted.

15. On 31 January 2014 the appellant's 2012-13 tax return as prepared by Shenkers and approved by the appellant on the previous day, was filed with HMRC. It included the following:

(1) The sections completed in the return were the "self employment" schedule (3F), the "residence, remittance basis etc" schedule (9) and "tax calculation summary" (SA110). The "employment" schedule was not completed.

(2) The self-employment pages showed:

(a) the taxable profits from the appellant's business as charity support worker as £34,125; and

(b) "other tax taken off trading income" in the amount of £10,627.59

(3) The residence status pages showed:

(a) the appellant was neither resident nor ordinarily resident in the UK for the tax year; and

(b) relief under Double Taxation Agreements between the UK and other countries was claimed in the amount of £9,211.

(4) The tax calculation showed:

(a) total of UK income tax and NICs due on the total taxable profits of £34,125 was calculated as £9,211.79; and

(b) £10,627.59 ("CIS vouchers and profits") and £9,211.79 ("overseas income") were subtracted from that amount, resulting in "income tax overpaid " of £10,627.59

16. On 19 December 2014 HMRC issued a notice under s9A TMA enquiring into the appellant's 2012-13 tax return.

17. On 16 September 2015 HMRC issued a notice under s28A(1) and (2) TMA closing the enquiry and amending the tax return to reverse the overpayment and claim for repayment.

18. The appellant completed an income tax return for the 2013-14 tax year. It was agreed in correspondence between Shenkers and HMRC in July 2015 that the appellant would not be required to complete a tax return for the 2014-15 tax year as she was in permanent employment outside the UK. In their penalty explanation letter to the appellant of 6 August 2015, HMRC stated: "We cannot suspend any of this penalty. You are no longer in self-assessment in the UK, there are no measurable conditions that I can set in order to suspend the penalty."

The law

References below to paragraphs are to paragraphs of Schedule 24 Finance Act 2007

19. Under paragraph 1, a penalty is payable by a person (P) where P gives HMRC a document of a kind listed (including an income tax return) and two conditions are satisfied:

(1) Condition 1 is satisfied where the document contains an inaccuracy which amounts to, or leads to, (amongst other things) a false or inflated claim to repayment of tax.

(2) Condition 2 is satisfied where (amongst other things) the inaccuracy was careless within the meaning of paragraph 3.

20. Paragraph 3 provides that inaccuracy in a document given by P to HMRC is careless if the inaccuracy is due to failure by P to take reasonable care.

21. Under paragraph 18, the above provisions of paragraph 1 also apply where a document is given to HMRC on P's behalf; and references to P in the above provisions of paragraph 3 include a reference to a person who acts on P's behalf in relation to tax. However, P is not liable to a penalty under those provisions in respect of anything done or omitted by P's agent where P satisfies HMRC that P took reasonable care to avoid inaccuracy.

22. Under paragraph 4, where the inaccuracy is in category 1, the penalty payable under paragraph 1 is, for careless action, 30% of the potential lost revenue. Under paragraph 4A, an inaccuracy is in category 1 if (inter alia) it results in a potential loss of revenue that is charged on or by reference to anything not in the following list:

(1) income arising from a source in a territory outside the UK ("abroad")

(2) assets situated or held abroad

(3) activities carried on wholly or mainly abroad

(4) anything having effect as if it were activities, assets or activities of a kind described above

23. Under paragraph 5, the "potential lost revenue" in respect of an inaccuracy in a document is the additional amount due or payable in respect of tax as a result of correcting the inaccuracy. The additional amount due or payable includes an amount that would have been repayable by HMRC had the inaccuracy not been corrected.

24. Under paragraph 10, if a person who would otherwise be liable to (inter alia) a 30% penalty under paragraph 4 has made a disclosure, HMRC must reduce the percentage to one that reflects the quality of the disclosure; but such a penalty may not be reduced below 15% in the case of a prompted disclosure. A disclosure is "prompted" unless it is made at a time when the person making it has no reason to believe that HMRC have discovered or are about to discover the inaccuracy (paragraph 9).

25. Under paragraph 11, if they think it right because of special circumstances, HMRC may reduce a penalty under paragraph 1.

26. Under paragraph 14, HMRC may suspend all or part of a penalty for a careless inaccuracy under paragraph 1 only if compliance with a condition of suspension would help P to avoid becoming liable to further such penalties.

27. Under paragraphs 15 and 16, a person may appeal against a decision of HMRC

(1) that a penalty is payable by the person; and on such an appeal the tribunal may affirm or cancel HMRC's decision;

(2) as to the amount of the penalty payable by the person; and on such an appeal, the tribunal may affirm HMRC's decision or substitute another decision that HMRC have power to make (and if the tribunal substitutes its decision for HMRC's, it may rely on paragraph 11 (special reduction) to a different extent than HMRC only if the tribunal thinks that HMRC's decision in respect of the application of paragraph 11 was flawed);

(3) not to suspend a penalty payable by the person; and on such an appeal, the tribunal may order HMRC to suspend the penalty only if it thinks that HMRC's decision not to suspend was flawed; and

(4) "flawed" in the above contexts means flawed when considered in the light of the principles applicable in proceedings for judicial review.

Appellant's arguments

28. Three numbered points were made in the notice of appeal:

(1) The appellant's claim for the refund of £10,627 was based on Girlhub changing their basis of payment of their workers from self employment to employment. Shenkers understood that PAYE was deducted from the appellant's pay and this was reflected in the schedule provided to Shenkers by the appellant. The appellant did not provide a P60 to Shenkers.

(2) As regards HMRC's argument that the appellant had 10 months (April 2013 to January 2014) to prepare an accurate tax return, it is suggested that, having had a baby in August 2013, the appellant was "far from concerned about a UK tax return at that time". Once she had returned to New Zealand with the baby, "the following five months to the end of January 2014 can be totally discounted for the purposes of having to worry about completing a tax return, due to the rigours of having a new-born child as a single parent". It is suggested that the imposition of the penalty, in these circumstances, could be a breach of human rights or "equalities" legislation.

(3) It should be taken into account that the appellant was not in the UK during the period when the tax return was prepared, making communication difficult:

(a) in Rwanda, communications were often down leading to delays in emails being dealt with;

(b) once the appellant had returned to New Zealand, the 12 hour time difference made communications much more difficult

29. The notice of appeal suggested that the imposition of a penalty on a non resident individual in these circumstances was "oppressive".

30. As to whether the appellant took reasonable care, the notice of appeal points out that

(1) the appellant appointed Shenkers as her accountants;

(2) the appellant was not financially astute;

(3) the circumstances may have affected the reliability of the information provided by the appellant to Shenkers

31. We also had regard to arguments made by Shenkers in their correspondence with HMRC.

HMRC's arguments

32. HMRC submitted that the parties agreed that the tax return in question was inaccurate; the point in contention was whether this was due to "carelessness" of the appellant.

33. The inaccuracy here, in HMRC's submission, was a false claim to repayment of tax:

(1) The figure of £10,627.59 as "other tax taken off trading income" was inaccurate and should have been zero.

(2) Shenkers' letters dated 19 May 2015 and 22 July 2015 confirmed that the return was incorrect and should be amended to nil.

34. The question for the tribunal, according to HMRC, is whether the appellant took reasonable care in preparing her return, and whether she took reasonable care to avoid an inaccuracy made by her agent.

35. HMRC's referred to the tribunal's decision in *Collis v HMRC* [2011] UKFTT 588 (TC) which states at [29]: "We consider that the standard by which this falls to be judged is that of a prudent and reasonable taxpayer in the position of the taxpayer in question."

36. HMRC submitted that the appellant failed to take reasonable care by providing Shenkers with the schedule in question, as a prudent and reasonable taxpayer in the appellant's position would have known that providing this would lead Shenkers to believe that amounts shown in the schedule as "tax" were UK tax deducted by her employer.

37. HMRC submitted that the appellant also failed to take reasonable care by approving a tax return showing tax had been overpaid by more than £10,000 without first questioning her accountants, who had prepared the tax return. A prudent and reasonable taxpayer in the appellant's position would have realised that tax had not been deducted from her pay due to the amount she had received. She would have checked her pay slips. Knowing that tax was not being deducted, such a person would know that she had not likely overpaid more than £10,0000 in tax to HMRC. A prudent and reasonable taxpayer in her position would have queried the figure with her accountants.

38. HMRC submitted that the representations made by Shenkers as to the state of the appellant's mind appear to be conjecture on their part. No evidence was produced of the appellant's state of mind.

39. Responding to the appellant's grounds of appeal, HMRC submitted:

(1) By the time she provided the schedule in question to Shenkers, the appellant should reasonably have known that no UK income tax had been deducted from her pay. She would not have needed her P60 to have known this.

(2) A person cannot be "excused" from their legal obligations as regards tax on the basis that she was pregnant or had recently given birth. Furthermore, the necessary action by the appellant to avoid the inaccuracy in her tax return would not have been onerous or time consuming: she need only have informed Shenkers that her employer was not deducting UK income tax from her pay, which she should reasonably have known.

(3) Any difficulties in communication between the UK and New Zealand should reasonably have been foreseen. In any case, the inaccuracy did not arise due to communications delays but because of the quality of the information provided by the appellant to Shenkers and the fact that she did not question the overpaid figure before approving her tax return. Moreover, a person cannot be "excused" from their legal obligations as regards tax on the grounds that they do not live in the UK.

(4) A person need not be "financially astute" to know whether tax was being deducted from their pay or not; or to know whether they had overpaid more than £10,000 in tax when that would amount to a significant proportion of their income.

40. HMRC submitted that:

(1) The potential lost revenue in this case was £10,627.59 – the amount which would have been repayable by HMRC had the inaccuracy in the appellant's tax return not been corrected.

(2) The inaccuracy fell with category 1 (in the terms of paragraph 4A) because the potential lost revenue arose from an incorrect claim to having overpaid tax on UK self employment income - it did not arise from the appellant's income, assets or activities in Rwanda because she was not UK tax resident during the year in question and therefore had no UK tax obligations in respect of her Rwandan income, assets or activities.

(3) The appellant's disclosure was prompted because it occurred after HMRC had enquired into her tax return; the penalty range was therefore between 15% and 30%; the penalty imposed by HMRC was 15% of £10,627.59, being £1,594.13.

(4) There were no special circumstances to warrant a reduction to the penalty.

(5) HMRC could not set suspension conditions to help the appellant avoid becoming liable to further penalties for careless inaccuracy because the appellant was no longer required to submit self assessment tax returns

Discussion

41. The starting point here is that there was an inaccuracy in the appellant's 2012-13 tax return. It claimed £10,627.59 of "other tax taken off trading income" whereas, in reality, no UK income tax had been deducted from the appellant's pay. This much was common ground between the parties.

42. The first matter for us to decide is: was this inaccuracy due to failure by the appellant to take reasonable care?

43. It is also relevant, at least in theory, to ask whether the inaccuracy was due to the failure of the appellant's agents, Shenkers, to take reasonable care. However, even if this were the case, the appellant would have a 'defence' to the extent she took reasonable care to avoid inaccuracy.

44. In deciding whether the appellant took reasonable care to avoid inaccuracy, we respectfully agree with the tribunal in *Collis* that the standard is that of a prudent and responsible taxpayer in her position.

45. We find that, by

(1) giving Shenkers the schedule (whose title suggested that tax had been withheld under the UK "pay as you earn" scheme),

(2) not giving Shenkers her P60 (which clearly showed that no UK income tax had been deducted from her pay) prior to submission of the tax return, and

(3) failing to notice, on review of the tax return prepared by Shenkers, that it contained a sizeable claim for repayment of UK tax which she would have known (from her payslips or from her P60) has not been withheld,

the appellant did not conduct herself to the standard of a reasonable and prudent taxpayer in her position. In finding this, we take into account the fact that the appellant had a baby during the 10-month period given by UK tax law to prepare the income tax return; however, we consider that a prudent and responsible taxpayer in these circumstances would have given her accountants better information and/or noticed the inaccuracy when asked by them to approve the tax return.

46. We thus decide that a penalty was payable. The next matter for us to decide is whether the amount of the penalty should be changed. The penalty here falls within category 1 and so is 30% of the potential lost revenue (before reduction for disclosure). We consider that the appellant's disclosure to HMRC of the inaccuracy in her tax return in this case was "prompted" – it was made after HMRC had begun to ask questions about the repayment claim in her tax return – and so the minimum to which the penalty can be reduced (for disclosure) is 15% of the potential lost revenue. That is what HMRC have assessed; and we agree with HMRC that the potential lost revenue here is that amount of the repayment claim in the appellant's tax return. We therefore decide that the amount of the penalty should remain as assessed.

47. The next matter for us to decide is whether HMRC's decision that it was not right to reduce the appellant's penalty because of "special circumstances," was flawed. The circumstances put forward as potentially "special" here are that the appellant was pregnant and gave birth in the course of the 10-month period for preparation of the tax return; and that she was living outside the UK (in Rwanda and New Zealand) in this period. We do not consider HMRC's decision that these did not amount to "special circumstances" was flawed – it seems to us reasonable to hold that having a baby and living abroad are not, either separately or together, sufficiently exceptional, abnormal or unusual occurrences to amount to "special circumstances" for this purpose.

48. The final matter for us to decide is whether HMRC's decision not to suspend the penalty was flawed. The power to suspend a penalty arises only if compliance with a condition of suspension would help the appellant to avoid becoming liable to further penalties under paragraph 1 for careless inaccuracy. Here, there is agreement between the parties that the appellant would not have to complete a UK tax return for the 2014-15 tax year on account of her being permanently employed outside the UK. It thus appears that unless and until her situation changes, the appellant will not be required to complete a UK tax return. In those circumstances, HMRC's decision that no condition could be imposed that would help the appellant avoid liability to further penalties for inaccuracy, was not, in our view, flawed.

49. In reaching our decision we have had regard to the principle of proportionality which, as the tribunal explained in *Collis* at [46-48], is introduced into the law by the First Protocol to the European Convention on Human Rights. It is to this principle which we understand Shenkers were alluding in the notice of appeal in its references to the penalty possibly being in breach of human rights or equalities legislation (due

to the appellant's circumstances of having a baby during the period for preparation of her 2012-13 income tax return), or being oppressive (due to the appellant being resident outside the UK). These points were not elaborated upon by the appellant or Shenkers in correspondence with HMRC (or at the hearing, which they did not attend). In our view, it is not disproportionate - in the required sense of being not merely harsh but plainly unfair - to impose a penalty for carelessness on someone in respect of their conduct across a 10 month period that included that person's pregnancy, giving birth and taking care of a young child; on the contrary, it would seem unfair if those circumstances shielded such a person from taking the reasonable care required of the general body of taxpayers. Similarly, it is not in our view disproportionate to impose such a penalty on a person resident outside the UK.

Conclusion

50. The appeal is dismissed; we affirm HMRC's decision that a penalty is payable by the appellant in the amount assessed.

51. 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.

ZACHARY CITRON
TRIBUNAL JUDGE

RELEASE DATE: 17 MAY 2017