Neutral Citation: [2024] UKFTT 1161 (TC)

Case Number: TC09389

FIRST-TIER TRIBUNAL
TAX CHAMBER

Location: Decided on the papers

Appeal references: TC/2022/14100
TC/2022/14097

COSTS – whether HMRC acted unreasonably in seeking further and better particulars of the Appellants' grounds of appeal – Rule 10, Tribunal Procedure (First-tier Tribunal)(Tax Chamber) Rules 2009

Judgment date: 20 December 2024

Decided by:

TRIBUNAL JUDGE ALEKSANDER

Between

(1) P SEHGAL
(2) MK SEHGAL (deceased)

Appellants

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

The Tribunal determined the appeal on 18 December 2024 without a hearing pursuant to Rule 29 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009.

DECISION

INTRODUCTION

1. These appeals challenged closure notices issued by HMRC on 30 June 2021, which determined that tax paid by Visage Imports Ltd ("VIL") in relation to bonus payments made for the Appellants' benefit in the year ending 5 April 2004:

   (a) should be treated as their earnings under the provisions of s223 ITEPA; and

   (b) had not been "made good" to VIL by the Appellants (and the Appellants were therefore liable to pay tax on those earnings without any deductions) .

2. The tax in dispute was over £500,000 for each of the Appellants.

3. The Appellants' Notices of Appeal are dated 22 November 2022. The appeals were assigned to the standard category and directed to be heard together.

4. On 8 February 2023 HMRC applied for further and better particulars of the Appellants' grounds of appeal, which the Appellants provided voluntarily on 14 April 2023.

5. Subsequently, HMRC determined that s223 ITEPA was not engaged. Rather VIL was required to operate PAYE in respect of the payments by virtue of s710 ITEPA.

6. The appeals were settled by agreement on 6 July 2023.

7. On 1 August 2023 the Appellants applied for an award of costs on the grounds that HMRC had acted unreasonably in putting the Appellants to costs in having to pursue an obviously meritorious appeal.

8. Included with the application was a schedule of the costs claimed using form N260. The total costs claimed are £21,444 (inclusive of VAT), of which £5000 (excluding VAT) represented counsel's fees.

9. Sadly, Mr MK Sehgal died on 15 December 2023, and these proceedings were stayed in order to allow his family a period of mourning and time to organise his affairs.

THE LAW

10. Section 29, Tribunal Courts and Enforcement Act 2007 provides that the award of costs of and incidental to all proceedings in the Tribunal shall be at the discretion of the Tribunal and subject to the FTT Rules.

11. The relevant provisions of Rule 10, Tribunal Procedure (First-tier Tribunal)(Tax Chamber) Rules 2009, are as follows:

> **Orders for costs**
>
> 10 (1) The Tribunal may only make an order in respect of costs (or, in Scotland, expenses)—
>
> (a) under section 29(4) of the 2007 Act (wasted costs) and costs incurred in applying for such costs;
>
> (b) if the Tribunal considers that a party or their representative has acted unreasonably in bringing, defending or conducting the proceedings;
>
> [...].
>
> (2) The Tribunal may make an order under paragraph (1) on an application or of its own initiative.
>
> (3) A person making an application for an order under paragraph (1) must—

(a) send or deliver a written application to the Tribunal and to the person against whom it is proposed that the order be made; and

(b) send or deliver with the application a schedule of the costs or expenses claimed in sufficient detail to allow the Tribunal to undertake a summary assessment of such costs or expenses if it decides to do so.

(4) An application for an order under paragraph (1) may be made at any time during the proceedings but may not be made later than 28 days after the date on which the Tribunal sends—

(a) a decision notice recording the decision which finally disposes of all issues in the proceedings; or

(b) notice under rule 17(2) of its receipt of a withdrawal which ends the proceedings.

(5) The Tribunal may not make an order under paragraph (1) against a person (the "paying person") without first—

(a) giving that person an opportunity to make representations; and

(b) if the paying person is an individual, considering that person's financial means.

(6) The amount of costs (or, in Scotland, expenses) to be paid under an order under paragraph (1) may be ascertained by—

(a) summary assessment by the Tribunal;

(b) agreement of a specified sum by the paying person and the person entitled to receive the costs or expenses (the "receiving person"); or

(c) assessment of the whole or a specified part of the costs or expenses, including the costs or expenses of the assessment, incurred by the receiving person, if not agreed.

12. The Appellants' application is made under Rule 10(1)(b) on the grounds that HMRC acted unreasonably in putting the Appellants to costs in having to pursue an obviously meritorious appeal.

13. What constitutes "unreasonable conduct" for the purposes of Rule 10 was considered by the Upper Tribunal in *Distinctive Care Ltd v HMRC* [2018] UKUT 155 (TCC), and upheld on appeal by the Court of Appeal ([2019] EWCA Civ 1010). In its decision, the Upper Tribunal set out at [44] to [46] the basis on which conduct is to be assessed:

> 44. In *Market & Opinion Research International Limited v HMRC* [2015] UKUT 12 (TCC) ("MORI") at [22] and [23], the Upper Tribunal endorsed the approach set out by the FTT in that case to the question of whether a party had acted unreasonably. That approach could be summarised as follows:
>
> (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;
>
> (2) it is possible for a single piece of conduct to amount to acting unreasonably;
>
> (3) actions include omissions;
>
> (4) a failure to undertake a rigorous review of the subject matter of the appeal when proceedings are commenced can amount to unreasonable conduct;

(5) there is no single way of acting reasonably, there may well be a range of reasonable conduct;

(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;

(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

(8) the power to award costs under Rule 10 should not become a "backdoor method of costs shifting".

45. We would wish to add one small gloss to the above summary, namely that (as suggested by the FTT in *Invicta Foods Limited v HMRC* [2014] UKFTT 456 (TC) at [13]), 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.

46. In assessing whether a party has acted unreasonably, this Tribunal in *MORI* went on to say this (at [49]):

"It would not, we think, be helpful for us to attempt to provide a compendious test of reasonableness for this purpose. The application of an objective test of that nature is familiar to tribunals, particularly in the Tax Chamber. It involves a value judgment which will depend upon the particular facts and circumstances of each case. It requires the tribunal to consider what a reasonable person in the position of the party concerned would reasonably have done, or not done. That is an imprecise standard, but it is the standard set by the statutory framework under which the tribunal operates. It would not be right for this Tribunal to seek to apply any more precise test or to attempt to provide a judicial gloss on the plain words of the FTT rules."

BACKGROUND FACTS

14. On 24 January 2008 HMRC opened enquiries into the Appellants' self-assessment tax returns for 2005/6. Final closure notices were issued by HMRC on 30 June 2021 bringing bonuses paid by VIL into charge under s233 ITEPA on the basis that:

(a) the bonuses fell within s223(1) (as payments to persons employed as directors of a company);

(b) the deductible tax on those payments that had been accounted for to HMRC was to be treated as the Appellants' earnings by virtue of s223(4);

(c) by virtue of s223(5), the bonuses received from VIL in the year ended 5 April 2004 were chargeable to income tax in the year they resigned their directorships (the year ended 5 April 2006); and

(d) no reduction was to be made to the tax due by virtue of s. 223(6) as the Appellants had not made good the deductible tax.

15. In 2010 the shares in the ultimate parent company of VIL were sold.

16. The Appellants' Notices of Appeal were apparently drafted by their son. The grounds for appeal as set out in MK Sehgal's Notice of Appeal included the following paragraphs:

> In November 2017 VIL settled the tax liabilities for the 2003/2004 scheme with HMRC agreeing that tax should have been paid on the bonuses.
>
> The monies VIL used to settle the tax liabilities were monies payable to the sellers under the [share purchase agreement] where the tax liability had been retained from earnout consideration otherwise payable. Those shareholders at the point of the sale were principally [various relatives].
>
> HMRC have agreed that [various relatives] did in effect meet the tax liability on the bonuses they had received by way of the reduction in the earnout consideration and so have waived the claims against them.
>
> However whilst they accept that myself and my wife have also made good the tax, the issue appears to be that it was from the monies owing to [various relatives] that than monies owing specifically to me and my wife.
>
> […]
>
> I don't accept that a gift to pay the tax can properly be categorised as "earnings". […].

17. P Sehgal's grounds of appeal were in substantially the same form.

18. On 8 February 2023 HMRC applied for the Appellants to provide further and better particulars of their grounds of appeal, on the grounds that the Appellants had not provided any explanation for how or why the requirement that a director make good deductible tax should be read to include immediate family. HMRC submitted that the grounds of appeal amounted to a bare denial and referred to the decisions of this Tribunal in *Unicorn Shipping v HMRC* [2017] UKFTT 464 (TC) and in *Rapid Brickwork (in liquidation) v HMRC* [2015[UKFTT 190 (TC).

19. On 14 April 2023 the Appellants voluntarily filed further and better particulars in the form of amended grounds of appeal. The amended grounds of appeal were settled by tax counsel and extended to 36 paragraphs over eight pages. The amended grounds contended that:

> (a) the conditions at s223(1) were not met, because the bonuses were not paid to a person who was employed as the director (but to a company); or
>
> (b) in the alternative, if a charge did arise under s223 it was made good under s.223(6)(c) because:
>
> > (i) The Appellants gave PAYE indemnities to Visage Holdings Limited ("VHL") giving VHL an enforceable right to the tax; and
> >
> > (ii) The Appellants made good the tax indirectly through indemnities given directly to VHL and to the purchasers of VHL in 2005 (following which the purchasers allowed part of the consideration on the sale in 2010 to be used to pay the tax liabilities – including those of the Appellants); and the Appellants' relatives made a payment or accepted reduced consideration for the sale so that the tax relating to the Appellants could be made good.

20. On 13 June 2023, HMRC determined that s223 did not apply. However, it reached this determination for reasons that differed from those submitted by the Appellants. HMRC determined that the underlying PAYE liability arose on a notional payment rather than an "actual payment", so VIL was required to operate PAYE in accordance with s710 ITEPA (in consequence, s223 ITEPA did not apply).

DISCUSSION

21. The Appellants submit that it was unreasonable for HMRC to put the Appellants to costs to pursue an obviously meritorious appeal. The Appellants submit that HMRC's application

for further and better particulars meant that they incurred costs in having to instruct tax counsel to settle revised grounds of appeal in order to explain why s223 ITEPA did not apply.

22. In considering whether HMRC has acted unreasonably, my focus must be on their standard of handling the Appeal rather than the quality or handling of HMRC's original decision (see *Distinctive Care Ltd* (UT) at [44(6)]). In other words, my focus is on the conduct of HMRC following the filing of the Notices of Appeal by the Appellants.

23. Grounds of appeal must set out the basis for challenging HMRC's decision. Grounds which merely assert that HMRC's decision is wrong do not meet this test.

24. I agree with HMRC that the grounds of appeal in the Notices of Appeal were insufficiently particularised. I note that HMRC's submissions to this effect at the time were not challenged in any way by the Appellants. The Appellants did not object to HMRC's application and voluntarily complied by filing amended grounds of appeal.

25. The Appellants' decision to instruct tax counsel to settle amended grounds of appeal arose because their original grounds had been inadequately pleaded, and not because of any unreasonable conduct on the part of HMRC. They were not asked to produce entirely new grounds of appeal, merely to set out the reasoned legal basis and the specific facts on which they relied for their Appeals.

26. I agree with HMRC and find that the fact that the Appellants voluntarily filed amended grounds of appeal settled by tax counsel and extending to 36 paragraphs over eight pages implicitly acknowledges that the original grounds were insufficiently particularised.

27. I find that HMRC had acted reasonably in applying for further and better particulars of the Appellants' grounds of appeal.

28. The fact that HMRC then agreed to settle the Appeals does not mean that they had acted unreasonably in the conduct of the litigation up until that point. In *Distinctive Care* the Upper Tribunal held that merely because an argument fails does not mean that the party running that argument (in this case, that s223 was engaged) were acting unreasonably. It is only if they persist in running the argument in the face of an unbeatable argument to the contrary could they be found to have acted unreasonably.

29. I find that it was only when the Appellants filed their amended grounds of appeal that the merits of their case were clearly set out. Indeed, I find that by settling the appeal at an early stage, following the filing of properly pleaded grounds, HMRC were acting entirely reasonably.

30. I find that HMRC has not acted unreasonably in defending or conducting this Appeal.

31. It follows that the Appellants' application for costs must be dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

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.

Release date: 20th DECEMBER 2024