TC02000

Appeal number: TC/2011/08280

CAPITAL GAINS TAX – penalty under Finance Act 2007 Schedule 24 – reliance on agent – reasonable care to avoid inaccuracy – appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

MR J R HANSON **Appellant**

- and -

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

TRIBUNAL: JUDGE JONATHAN CANNAN

Sitting in public at Manchester on 11 April 2012

Mr Martyn Arthur of Forensic Accountant Ltd for the Appellant

Miss Ros Shields of HMRC for the Respondents

DECISION

Background

1. This appeal concerns a penalty imposed on the appellant pursuant to *Schedule 24 Finance Act 2007*. The penalty charged is £14,365.56. The respondents say that the appellant incorrectly claimed relief against chargeable gains in his tax return for 2008-09. As a result they say that *Schedule 24* is engaged because there was an inaccuracy in the return which was careless.

2. I heard evidence from the appellant and from Mr Martin Clarke who is a Chartered Certified Accountant. Mr Clarke's firm, Clarke Broome Fleming ("CBF") acted on behalf of the appellant at all material times. The appellant's evidence was in the form of a short witness statement. Mr Clarke gave oral evidence. I also had submissions from Miss Shields on behalf of the respondents and from Mr Arthur on behalf of the appellant. There is no real dispute as to the facts. The real issue is whether the appellant took reasonable care to avoid inaccuracy in his tax return for 2008-09.

Findings of Fact

3. I have no reason to doubt the evidence of the appellant and Mr Clarke and I accept it unreservedly. Based on the evidence I heard and the undisputed documents before me I make the following findings of fact.

4. In or about September 2006 the appellant received certain loan notes as part of the consideration for the sale of a business to Kuoni Travel Limited. Mr Clarke of CBF acted for the appellant in relation to this transaction. Mr Clarke had long acted as the appellant's accountant. The appellant also received advice at the time of the sale of the business from, amongst others, BDO Stoy Hayward and Halliwells LLP. It is not suggested that this advice was relevant to the way in which the 2008-09 tax return was completed.

5. During the course of 2008 the appellant disposed of the loan notes. Disposal of the loan notes gave rise to chargeable gains for capital gains tax ("CGT") purposes amounting to £1,261,387. At or about the time of disposal of the loan notes Mr Clarke considered whether any form of relief would be available for CGT purposes. He concluded that Entrepreneurs Relief would not be available. Some time after this the appellant was given a press cutting by a financial adviser which suggested that UK holiday letting properties could be used to mitigate a CGT charge. The appellant had already purchased such a property. He consulted Mr Clarke and provided him with a copy of the article. Mr Clarke indicated to the appellant that a form of holdover relief would be available to mitigate the CGT charge on disposal of the loan notes.

6. In late 2009 the appellant came to prepare and lodge his tax return for 2008-09. He instructed CBF to undertake the task. CBF was responsible for completing the tax return and Mr Clarke accepted in evidence that the appellant was relying on his firm

to complete it correctly. Mr Clarke described himself as a "high street practitioner". He regretted that the firm did not carry out a second review of the position at the time the return was submitted and also that the firm did not obtain specialist advice from a tax consultant prior to advising the appellant. He accepted that the appellant was acting on the firm's advice and the appellant was specifically told that holdover relief was available.

7. The CGT pages of the appellant's tax return for 2008-09 show at box 19 gains in the year of £1,261,387. Box 20 is crossed to indicate that the appellant was making a claim for relief. The Guidance Notes for these pages include a paragraph about making claims. They state as follows:

> "*You must also provide details of each claim ... in the 'Any other information' box, box 35 or in your computations providing a clear statement that a claim ... is being made ... in respect of a particular gain or loss.*"

8. Box 35 of the tax return was simply completed to say "Sale of Kuoni Travel Ltd. Loan notes" and gave no further details of the claim. The accompanying computation only showed the taxable gain after deduction of relief but without identifying the amount of relief claimed.

9. On 11 August 2010 an enquiry was opened into the appellant's 2008-09 tax return. It was an aspect enquiry looking only at the disposal of loan notes. The information initially requested included a CGT computation for the gain on disposal of the loan notes and an explanation as to what claim had been made and why. In response CBF provided a computation showing relief of £462,659 and identified this as being Entrepreneurs Relief. In evidence Mr Clarke accepted that this description was incorrect because they had ruled out the application of Entrepreneur's Relief before submitting the return.

10. HMRC requested further explanations of the claim. In response CBF explained that their previous reference to Entrepreneur's Relief was mistaken and that it was a claim to roll-over relief. HMRC replied to state that roll-over relief was not available because the loan notes were not qualifying assets. CBF responded to say that they were claiming hold-over relief under section 135 Taxation of Chargeable Gains Act 1992. This was described as "share exchange relief". Following a further exchange of correspondence CBF accepted that no relief was available and that there was an additional tax liability of £83,278. There is no dispute on this appeal that this is the additional CGT liability arising as a result of an invalid claim to relief.

11. During the course of the correspondence with HMRC, Mr Clarke did consult an external tax consultant. Initially the consultant had agreed that some form of relief was available but subsequently, when he went through the files in more detail, the consultant advised that no relief was available.

The Law

12. The penalty regime with which this appeal is concerned appears in *Schedule 24 Finance Act 2007*. The relevant provisions are set out below. *Paragraph 1* provides:

"*(1) A penalty is payable by a person (P) where—*

*(*a*) P gives HMRC a document of a kind listed in the Table below, and*

*(*b*) Conditions 1 and 2 are satisfied.*

(2) Condition 1 is that the document contains an inaccuracy which amounts to, or leads to—

*(*a*) an understatement of a liability to tax,*

*(*b*) a false or inflated statement of a loss, or*

*(*c*) a false or inflated claim to repayment of tax.*

(3) Condition 2 is that the inaccuracy was careless (within the meaning of paragraph 3) or deliberate on P's part."

13. The list of documents to which these provisions apply includes the self assessment return which the appellant completed in this case.

14. *Paragraph 3* provides in so far as relevant:

"*(1) For the purposes of a penalty under paragraph 1, inaccuracy in a document given by P to HMRC is –*

(a) "careless" if the inaccuracy is due to failure by P to take reasonable care …"

15. Paragraph 18 deals with the liability of a taxpayer to penalties under the schedule where agents are acting on behalf of the taxpayer. It provides as follows in so far as relevant:

"*(1) P is liable under paragraph 1(1)(a) where a document which contains a careless inaccuracy (within the meaning of paragraph 3) is given to HMRC on P's behalf.*

…

(3) Despite sub-paragraphs (1) and (2), P is not liable to a penalty under paragraph 1 or 2 in respect of anything done or omitted by P's agent where P satisfies HMRC that P took reasonable care to avoid inaccuracy (in relation to paragraph 1)…"

16. Neither party drew my attention to paragraph 18 in their submissions. During the course of the hearing I therefore invited submissions in relation to the effect of that paragraph in the circumstances of the present case. Mr Arthur for the appellant relied on *paragraph 18(3)*.

17. Miss Shields made no submissions specifically in relation to *paragraph 18*. She did however rely on a decision of the First-tier Tribunal in *Heaney-Irving v HMRC*

TC01619. That case was concerned with whether a taxpayer who relied on his accountant to file a self-assessment return had a reasonable excuse such that the taxpayer should not be liable to a penalty under *section 93 Taxes Management Act 1970*. The tribunal judge in that case referred to a number of other decisions of the First-tier Tribunal to the effect that reliance on a third party to file a return or to make a payment of tax on time can be a reasonable excuse but must involve something exceptional.

18. I do not consider that the meaning of reasonable excuse in the context of a failure to make a return or make a payment of tax gives any real assistance in construing *Para 18 Schedule 24 Finance Act 2007*. *Paragraph 18* is specifically dealing with the reasonableness of reliance on a third party agent whose act or omission causes an inaccuracy in a return. It is plainly directed towards those professional advisers who assist taxpayers in completing their tax returns and documents associated therewith. In those circumstances the focus of whether a taxpayer has taken reasonable care will be whether he was reasonably entitled to rely upon his adviser, and what steps the taxpayer himself might reasonably be expected to take given that he has instructed a professional adviser.

19. In my view carelessness can be equated with "negligent conduct" in the context of discovery assessments under *section 29 Taxes Management Act 1970*. In that context, negligent conduct is to be judged by reference to the reasonable taxpayer. The test was described by Judge Berner in *Anderson (deceased) v Revenue and Customs Commissioners* [2009] UKFTT 206 at [22], cited with approval by the Upper Tribunal in *Colin Moore v Revenue and Customs Commissioners* [2011] UKUT 239 (TCC):

> "*The test to be applied, in my view, is to consider what a reasonable taxpayer, exercising reasonable diligence in the completion and submission of the return, would have done.*"

20. I am satisfied that the effect of *paragraph 18* is to remove the liability of a taxpayer to a penalty where:

(1) a return is completed and lodged by an agent, and

(2) an inaccuracy in the return is the result of something done or omitted by the agent, but

(3) the taxpayer took reasonable care to avoid that inaccuracy.

21. What is reasonable care in any particular case will depend on all the circumstances. In my view this will include the nature of the matters being dealt with in the return, the identity and experience of the agent, the experience of the taxpayer and the nature of the professional relationship between the taxpayer and the agent. In my view, if a taxpayer reasonably relies on a reputable accountant for advice in relation to the content of his tax return then he will not be liable to a penalty under *Schedule 24*.

22. I am fortified in these conclusions in relation to *paragraph 18* by the content of the HMRC Compliance Handbook at CH84540 which states in relation to paragraph 18 as follows:

> "*A person cannot simply appoint an agent and deny responsibility for their tax affairs. The person still has a duty to take reasonable care, within their ability and competence, to make sure that what they are signing for is correct. The person has to show that they took reasonable care, within their ability and competence, to avoid default by their agent. This will include*
>
> - *making sure that they give the agent all relevant information with which to work ...*
> - *implementing the professional advice received, and not neglecting some vital step*
> - *checking the agent's work to the extent that the person is able to do so. For example, an ordinary person cannot be expected to challenge specialist professional advice on a complex legal point. But they ought to be able to recognise the complete absence of a major transaction.*
>
> *A person saying and meaning 'I leave it all to my agent' is hardly taking care, let alone reasonable care, over their obligations or the work of their agent.*
>
> *... The person has an obligation to choose an adviser who is trained and competent for the task in hand ...*
>
> *The benchmark is a person who goes to an apparently competent professional adviser*
>
> - *gives the adviser a full and accurate set of facts*
> - *checks the adviser's work or advice to the best of their ability and competence and*
> - *adopts it.*
>
> *The person will then have taken reasonable care to avoid inaccuracy on the part of themselves and their agent.*"

23. At one extreme is an error of omission, for example failing to declare a source of income. In those circumstances it seems to me that a taxpayer will almost always be expected to identify the error. At the other extreme an error might involve wrongly construing a complex piece of legislation. In those circumstances the possibility of a penalty may still arise because of the carelessness of the agent, but the taxpayer's liability to a penalty might well be excluded on the basis that he took reasonable care but did not identify the error.

24. I agree with the general thrust of the guidance given in the HMRC Compliance Handbook. In particular that a taxpayer cannot simply leave everything to his agent. A taxpayer must certainly satisfy himself that the agent has not made any obvious error. That might involve the taxpayer seeking to understand the basis upon which an entry on his return has been made by the agent. However in matters that would not be straightforward to a reasonable taxpayer and where advice from an agent has been sought which is ostensibly within the agent's area of competence, the taxpayer is entitled to rely upon that advice. At the heart of this issue is the extent to which a taxpayer is required to satisfy himself that the advice he has received from a professional adviser is correct. The answer to that will depend on the particular circumstances of the case.

25. *Paragraphs 4-8 Schedule 24* deal with the amount of the penalty which is set by reference to the "*potential lost revenue*". There is no dispute in the present case that the potential lost revenue in respect of the inaccuracy in the appellant's return is £83,278. The standard amount of the penalty, subject to reductions, is 30% of the potential lost revenue in a case of careless action.

26. *Paragraphs 9 and 10* deal with reductions for disclosure of an inaccuracy. *Paragraph 9(1)* provides that a person discloses an inaccuracy by:

> "*(a) telling HMRC about it*
>
> *(b) giving HMRC reasonable help in quantifying the inaccuracy ... and,*
>
> *(c) allowing HMRC access to records for the purpose of ensuring that the inaccuracy ... is fully corrected*"

27. *Paragraphs 9 and 10* also distinguish between a prompted disclosure and an unprompted disclosure. For present purposes it is not disputed that the disclosure given by the appellant was prompted. In those circumstances HMRC must reduce the standard penalty of 30% "*to one that reflects the quality of the disclosure*". Having said that in a case of prompted disclosure the minimum penalty that can be imposed is 15% of the potential lost revenue.

28. *Schedule 24* also contains provisions for suspension of penalties, but the parties agreed that no issue in relation to suspension arises in this appeal.

Reasons

29. This is an appeal against a penalty. In general the burden of establishing that the penalty is due lies on the respondents. It is not disputed that there was an inaccuracy in the appellant's return for 2008-09. The respondents must therefore satisfy me that the inaccuracy was careless on the part of the appellant or his agent. In circumstances where the liability to a penalty is in respect of anything done by a taxpayer's agent, *Para 18(3) Schedule 24* provides that it is for the taxpayer to satisfy HMRC that he took reasonable care to avoid inaccuracy. As in the case of penalties which are subject to a plea of "reasonable excuse" I take it that the burden of demonstrating reasonable care lies on the appellant.

30. I have no hesitation in finding that there was carelessness on the part of CBF. Mr Arthur did not suggest otherwise. The entitlement to relief for CGT purposes in these circumstances was an area that a reasonably competent accountant ought to have been able to advise upon. It is then necessary to consider whether the appellant himself took reasonable care to avoid the inaccuracy.

31. I have come to the conclusion that the appellant did take reasonable care. He instructed an ostensibly reputable firm of accountants who had acted as his accountants for many years. The matters on which he instructed them were ostensibly within their expertise. He had no reason to doubt their competence or their advice that relief was available. They were in possession of all relevant facts. In the circumstances of this case the appellant was entitled to rely on CBF's advice without himself consulting the legislation or any guidance offered by HMRC. I suppose that the appellant might have asked Mr Clarke for a technical analysis of why relief was available although Miss Shields did not criticise him for not doing so. In my view in the circumstances of this case that would be a counsel of perfection. Failure to do so does not demonstrate a lack of reasonable care on the part of the appellant.

32. Miss Shields made a number of submissions to the effect that the appellant should still be responsible for the inaccuracy. She identified that the guidance notes required detail of the claim to be given in box 35. In my view the detail required to be included in Box 35 is a matter of judgement. The appellant was entitled to consider that his accountants had addressed the level of detail required. In any event, failure to give detail of the claim was not the inaccuracy which led to the penalty. The inaccuracy was making the claim to relief in the sum of £462,659 and calculating and paying the tax on that basis.

33. Miss Shields submitted that the appellant's responsibility to ensure the correctness of his return could not be "offset to an agent or third party". She also submitted that it was the appellant's responsibility to ensure that the advice he had received was correct. However those submissions fail to take into account the provisions of *Paragraph 18* and fail to acknowledge that the appellant's responsibility was limited to that which was in all the circumstances reasonable.

34. Miss Shields did acknowledge that the appellant could not be expected to know the "ins and outs" of the conditions for making a claim to relief. However she submitted that the loan notes were clearly not a qualifying asset for the purposes of hold-over relief. In support of that submission I was not referred to the legislation governing hold over relief on the sale of an asset with re-investment in a holiday letting property. Nor was I referred to any relevant guidance notes or help sheets from which it could be said that loan notes were clearly not a qualifying asset. The appellant was present at the hearing and whilst his evidence was given in the form of a witness statement there was no application to cross-examine him. In those circumstances I cannot find that the appellant ought himself to have realised that the claim to relief was not available to him.

35. If the appellant had simply read an article suggesting he might be entitled to relief and then gone on to claim relief I would have no hesitation in finding that he had been

careless. However that is not what happened. He plainly had some discussion with his financial adviser which prompted the financial adviser to give him a copy of the article. He provided a copy of the article to his long standing accountant and asked for advice. He received positive advice that he was entitled to relief. Later, when it came to submitting his tax return the advice was repeated and the claim was made on the strength of that advice. On the basis of the evidence I find that the appellant did take reasonable care to avoid inaccuracy.

36. Mr Arthur also submitted that in any event the penalty was too high. For the sake of completeness, if the appellant had failed to take reasonable care and a penalty were properly payable, \I would not have reduced the amount of the penalty. The basis on which a reduction to a penalty can be made is exhaustively set out in *Schedule 24*. In cases such as the present it depends on the quality of disclosure given. I cannot help feeling that CBF ought to have accepted the liability to tax at an earlier stage of the correspondence.

Conclusion

37. I have found as a fact for the reasons given above that the appellant did take reasonable care to avoid the inaccuracy in his tax return for 2008-09. In those circumstances I cancel HMRC's decision to impose a penalty and allow the appeal.

38. 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.

JONATHAN CANNAN
TRIBUNAL JUDGE

RELEASE DATE: 26 April 2012