[2021] UKFTT 0272 (TC)

TC08217

COSTS – rule 10(1)(b) FTT Rules – unreasonable conduct by HMRC in late withdrawal – no – unreasonable conduct in refusing disclosure of listed documents – yes – ALLOWED IN PART

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2018/04947

DECISION
ON AN APPLICATION FOR COSTS
IN THE CASE OF

LENITY LIMITED **Appellant**

-and-

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

1. This is an application for costs made by Lenity Limited ("**the Appellant**") pursuant to rule 10(1)(b) Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rule 2009 ("**FTT Rules**").

BRIEF CHRONOLOGY

2. On 18 April 2018 HM Revenue & Customs ("**HMRC**") issued an assessment in respect of input tax they considered to be irrecoverable in period 04/15 ("**the April 2018 Assessment**"). HMRC considered that the assessment was due because goods were said to have been acquired by way of a zero-rated intracommunity acquisition from a supplier in Germany and immediately sold by way of zero-rated export to a purchaser in Poland in circumstances in which no VAT had been declared by the Polish recipient. The assessment was a replacement assessment for one issued on 26 January 2018 and withdrawn (following statutory review) on 18 April 2018.

3. The transactions giving rise to the assessments referred to in paragraph 2 above had previously been the subject of a previous assessment which had also been withdrawn.

4. All assessments were made within the statutory time limits.

5. The April 2018 Assessment was subject to statutory review which was completed on 14 June 2018 and the Appellant appealed on 13 July 2018. At the time the appeal was made the tax due on the assessment had not been paid and thus, if the Tribunal was to have jurisdiction in respect of the appeal, hardship had to be established.

6. On the papers there is a dispute between the parties as to when the hardship application was formally made. The Appellant (by its response to HMRC's objection) contends it was made on 13 July 2018 (no document supporting that contention is provided). HMRC contend that it was not formally made, or any documentation provided, until 31 August 2018 (again no documentary support is provided to substantiate that date). It is impossible for the Tribunal to

determine which of those dates is accurate. The Tribunal considered requesting the information but decided, in the end, any delay, or otherwise, in the making of the hardship application, made little difference to the decision on whether costs were payable. The parties do not dispute that, in any event, further information was iteratively requested and provided, and hardship was acceded to on 19 March 2019. By reference to the chronology provided by HMRC, which the Appellants is taken to agree as accurate (other than as to the date on which the application was made), the delay in the resolution of hardship appears to have been shared between the Appellant and HMRC.

7. The proceedings themselves were protracted. HMRC's statement of case was due to be served by 3 June 2019. Before the due date HMRC sought an extension of time for service to which the Appellant consented. The basis of the extension was that HMRC wanted policy input on how the supplies "should be rated". A further extension of time was sought (again before the expiry of the previous one) in which to "clarify instructions as to whether the Decision can be maintained". Again the Appellant consented to the application and the Statement of Case was ultimately served in accordance with the extension on 12 August 2019.

8. By reference to the material provided in relation to the costs claim, the parties crossed swords over the best means of providing for adequate disclosure. However, on 17 September 2019 the Tribunal directed the service of lists of documents by 8 November 2019 and witness statements by 6 December 2019 with the parties subsequently agreeing to vary the directions. In accordance with the varied directions lists of documents were exchanged on 22 November 2019.

9. The Appellant requested copies, by way of disclosure, of documents from HMRC's list of documents. However, HMRC failed to comply with the request asserting that certain documents had been included on the list of documents in error (on the grounds that the documents were either privileged or not relevant to the appeal). A dispute arose between the parties as to the relevance of the documents withheld and HMRC applied to amend their list of documents. That dispute was not fully resolved between the parties by the time the general covid stay was made on 26 March 2020.

10. Despite the dispute on disclosure. the parties continued to prepare their witness evidence. HMRC provided draft witness statements dealing with certain redacted documents on 9 April 2020. The Appellant requested an extension of time (as a consequence of the ongoing disclosure dispute and covid restrictions) to serve its witness statements to 1 September 2020. The Appellant's witness statements were duly served on 1 September 2020.

11. HMRC's witness statements were due to be served on 29 September 2020. No HMRC witness statements were served by that date and no application was made to extend time for service. With a continued failure to serve statements, on 8 January 2021, the Tribunal issued an unless order on HMRC compelling compliance with the requirement to serve witness statements by no later than 22 January 2021. On 22 January 2021, HMRC confirmed it did not intend to serve witness statements and sought a stay of proceedings "to review its position and to obtain further input from its policy team".

12. On 28 January 2021, having submitted the application for a stay, HMRC communicated on a without prejudice basis that they intended to withdraw the assessment. Despite this communication the Appellant objected to the request for a stay.

13. The assessments were withdrawn on 25 February 2021 (outside the 30-day requested stay).

BASIS ON WHICH THE TRIBUNAL MAY AWARD UNREASONABLE COSTS

14. 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.

15. Rule 10 FTT Rules provides that the Tribunal may only make an order for costs in certain limited cases including: a) wasted costs; b) unreasonable costs and c) in a case allocated to the complex track and in respect of which the appellant has not opted out of the costs' regime.

16. The leading and binding authority on the question of unreasonable costs is *Distinctive Care Ltd v HMRC* [2019] EWCA Civ 1010. In that case, and by reference to the approval of the Upper Tribunal judgment, it was determined:

(1) The earliest conduct that was relevant in the context of determining whether a party had behaved unreasonably was the point at which the proceedings commenced with the issue of a notice of appeal as the discretion applies only to unreasonable conduct in the proceedings and not to the investigation leading to those proceedings.

(2) The focus of the Tribunal was to be the handling of the litigation and not as to the quality of the original decision. The Tribunal is warned that the award of costs should not represent a wide-ranging analysis of the parties conduct prior to the appeal.

(3) The granting of an unreasonable costs order is not to be seen as a "back-door" means of costs shifting with the consequence that what constitutes unreasonable behaviour is unlikely to extend to improper or negligent behaviour.

(4) Where a party withdraws from an appeal it is necessary to consider whether they had acted promptly once it was identified that the proceedings were to be discontinued.

(5) Where costs are awarded on the grounds of unreasonable behaviour the scope of the costs award may include costs incurred prior to the commencement of proceedings provided that such costs are within the scope of the ultimate appeal.

17. In respect of the approach to be taken to considering whether a decision to withdraw amounts to unreasonable conduct the Tribunal is also bound to follow the approach directed by the Upper Tribunal in *Tarafdur v HMRC* [2014] UKUT 00362 in which the Upper Tribunal considered the approach to be to answer the following questions:

(1) What was the reason for withdrawal of that party from the appeal?

(2) Having regard to that reason, could that party have withdrawn at an earlier stage in proceedings?

(3) Was it unreasonable for that party to not to have withdrawn at an earlier stage?

PARTIES SUBMISSIONS

18. The Appellant contends that HMRC's conduct was unreasonable. In summary they assert that HMRC acted unreasonably in the following regards:

(1) HMRC were guilty of delay in determining the Appellant's hardship application.

(2) Repeated extensions in which to prepare the statement of case.

(3) The issues with disclosure

(4) Failure to serve witness statements and/or seek an extension of time to do so prompting the Tribunal to issue an unless order

19. The Appellant also contends that HMRC delayed in withdrawing unmeritorious assessments. In this regard, in particular, the Appellant points to the basis on which the

statement of case was delayed (indicating discomfort with the basis of assessment); the fact that the April 2018 Assessment represented the third attempt to assess in respect of a single deal; the delay in withdrawal following service of the Appellant's witness evidence; and the absence of any supporting evidence as to the enquires of the German authorities which HMRC contend was the basis of the withdrawal.

20. HMRC contend that the Tribunal is required to focus only on conduct in the proceedings and not prior to them. Through this lens they contend that their conduct of the proceedings has been in compliance with all time limits set by the Tribunal (save for non-compliance in respect of witness statements) with the necessary application for extensions of time having been made in time. They defend their conduct of the decision on hardship by reference to the delays contributed by the Appellant.

21. In respect of late withdrawal/resisting an obviously meritorious appeal HMRC contend that the basis of the Appellant's appeal was not the basis on which they ultimately withdrew the assessments. The Appellant asserted that the ability to assess them under the "fallback provisions" did not arise because they had acted with due diligence and could not have known that the goods were transported to Poland where the purchaser was not registered for VAT purposes (the Appellant believing the recipient was a Czech business registered for VAT purposes). Whereas the assessment was withdrawn on the basis that the goods were delivered on a FOB basis by the Appellant's supplier directly to the Appellant's customer which, by virtue of the relevant CJEU case law, represented a domestic supply in Germany requiring the Appellant to be registered in Germany. HMRC contend that it was the Appellant's witness statement and the documentation referred to therein which, when taken together with a response from the German authorities, led to the withdrawal of the assessments.

APPLICATION OF THE RELEVANT TEST

22. The Tribunal is mindful of the overarching direction given by the Court of Appeal that the award of costs in a standard category appeal is to be the exception and that the focus of attention is on the conduct of the litigation and not the underlying quality of the taxing decision.

23. Having carefully considered the detailed chronology provided by each party the Tribunal considers that, in the main, HMRC's conduct in the proceedings was not unreasonable. However, the Tribunal considers there are two episodes of questionable conduct by HMRC:

(1) the inclusion of documents on HMRC's list of documents which they subsequently sought to exclude from disclosure; and

(2) non-compliance with the direction to serve witness statements.

24. With regard to the non-compliance with a direction to serve witness statements, the Tribunal's view is that it is not conduct which should justify a costs order. It did show a disrespect for the Tribunal and the Appellant but to award costs in such a circumstance would be to significantly broad the scope of an unreasonable costs order. There are many occasions where the Tribunal is forced to issue an unless order to compel compliance. If each such occasion constituted unreasonable conduct justifying an award of costs, costs would almost become the norm – something explicitly contrary to the judgment in *Distinctive Care*.

25. However, the inclusion of documents on a list of documents, followed by a refusal to disclose such documents does, in the Tribunal's view, amount to unreasonable conduct. The obligation in the Tribunal process is not that arising under the CPR: it is simply to list documents on which the party intends to rely. It must therefore, be reasonably expected that all documents on a party's list of documents have been considered and appropriately determined to be relevant to the appeal and documents which may then be requested by the other party. To seek to refuse to make disclosure once the documents have included on the list

of documents and to seek to amend a list of documents to exclude (rather than introduce) documents is not conduct to be reasonably expected of a represented party of any sort.

26. For that reason the Tribunal considers that the Appellant is entitled to their reasonable costs determined on the standard basis arising from HMRC's change of heart and for all matters associated with seeking to secure disclosure of the listed documents. Such costs were incurred in the period 22 November 2019 (when the lists of documents were exchanged) through to resolution of the disclosure issues. The precise date of resolution is unclear from the papers and there may have been outstanding disclosure matters through to when the assessments were withdrawn. The Appellant is entitled to their costs for all activities associated with securing disclosure of the listed items, including the costs associated with the reviewing the draft witness statements of Peter Birchfield and Paddy Millar which concerned the SCAC documents. However, the order for costs does not extend to other activities undertaken in that period.

27. Turning to the question as to whether HMRC's conduct was unreasonable as a consequence of failing to withdraw the assessment until 25 February 2021. The judgments in *Tarafdur* and *Distinctive Care* are both relevant in this regard (as set out above) so as to determine whether HMRC could and should have withdrawn earlier.

28. The Tribunal is acutely aware of the direction of Rose LJ regarding which conduct is relevant in determining whether a rule 10(1)(b) costs order should be made and that the focus on conduct post the proceedings commencing is all that is relevant for determining unreasonable conduct. However, the authorities also require the Tribunal to determined whether HMRC, in this case, could have withdrawn the assessments earlier. In that regard the assessment history is, as the Appellants submitted, a relevant factor. But, in the Tribunal's view, it does not assist the Appellant in this matter. The Tribunal considers that the assessment history indicates an attempt by HMRC to properly identify the correct tax position with regard to the transactions under scrutiny. Transactions, with the Appellant at the centre, and which had escaped a charge to tax in any member state. HMRC were obliged to identify whether there was a tax liability in the UK as a consequence of the use of the Appellant's VAT registration number to secure a chain of zero rated supplies which should have been subject to tax somewhere in the EU.

29. The Tribunal has found the reasons given for the extensions of time for service of the statement of case more challenging to reconcile in the context of what the Appellant contends was an unreasonably late withdrawal/unreasonable assessment. It is apparent from the terms of the extension requests that HMRC were not 100% confident in the basis of their assessment. Further, they were told by the Appellant in a letter dated 23 February 2018 (and before the April 2018 Assessment was raised) that the goods had been sold on an FOB basis with the Appellant's purchaser collecting them from the Appellant's supplier. That appears to have been a critical factor in the decision ultimately reached on the application of the fall-back provisions (which cannot apply to a domestic German transaction).

30. However, there is no question that the focus of the letter of 23 February 2018 and the grounds of the Appellant's appeal, perhaps understandably given the likely consequences for the tax liabilities that would arise in Germany, did not assert that there was no UK VAT liability on the basis that the supply was a domestic German supply. As HMRC correctly contend the Appellant sought to assert no UK liability to VAT on an entirely different basis to that on which the assessments were ultimately withdrawn. The Appellant's witness statement dated 1 September 2020 added factual detail to the transactions and facilitated further investigation leading to the withdrawal of the assessment.

31. Again the Tribunal reminds itself that this is a standard track case. Costs claims should not be granted except in the clearest of cases. On balance and in exercise of the discretion

afforded to it, in light of all of the circumstances, and by reference to the overriding objective the Tribunal considers that the failure to challenge the assessment on the basis on which it was ultimately withdrawn is fatal to the costs claim for late withdrawal. HMRC identified the potential issue for themselves by reference to the factual circumstances, supplemented with additional material in the Appellant's witness statement, and was not assisted in that regard by the Appellant. The transactions appear, on their face, to have given rise to lost tax which HMRC were bound to investigate fully. The fact that ultimately the responsibility to tax appears to fall in Germany and that no UK assessment is due supports the approach taken by HMRC (who were by the time of the April 2018 Assessment close to the time limits for assessing) to protect the lost revenue albeit that ultimately it was not lost UK revenue.

32. On this basis the Tribunal concludes that HMRC's conduct was, in one respect, unreasonable and that costs associated with that conduct only should be awarded. In all other respects the costs application is refused.

33. The Appellant's schedule of costs does not provide sufficient information for the costs awarded to be assessed. The parties should look to agree the reasonable costs to be paid and, in the absence of such agreement, the costs are to be assessed by a Senior Costs Judge.

34. If either party is dissatisfied with the outcome of the application for costs, they have a right to apply to the Upper Tribunal for permission to appeal the decision in this appeal. Such an application must be made in writing to the Upper Tribunal at 5th Floor, Rolls Building, 7 Rolls Building, Fetter Lane, London EC4A 1NL no later than one month after the date of this notice. Such an application must include the information as explained in the enclosed guidance booklet Appealing to the Upper Tribunal (Tax and Chancery Chamber).

AMANDA BROWN QC
TRIBUNAL JUDGE

RELEASE DATE: 28 JULY 2021