[2019] UKUT 0391 (TCC)

Appeal number: UT/2018/0135

INCOME TAX – penalties under Schedule 55 and Schedule 56 of Finance Act 2009

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS — **Appellants**

-and-

DUNCAN HANSARD — **Respondent**

TRIBUNAL **MR JUSTICE NUGEE**
JUDGE JONATHAN RICHARDS

Sitting in public at The Royal Courts of Justice, Rolls Building, London on 27 November 2019

Laura Poots, instructed by the General Counsel and Solicitor to Her Majesty's Revenue and Customs, for the Appellants

Keith Gordon for the Respondent

DECISION

1. This appeal concerns penalties that the appellants ("HMRC") imposed on Mr Hansard for (i) failures to file tax returns on time and (ii) failures to pay tax due on time. Those failures are penalised by different statutory provisions: late filing penalties are dealt with in Schedule 55 of Finance Act 2009 ("Schedule 55") with late payment penalties dealt with in Schedule 56 of Finance Act 2009 ("Schedule 56") although there are several similarities between the two sets of provisions. A feature of both Schedule 55 and Schedule 56 is that an initial failure (whether to pay tax on time, or to file a tax return on time) is penalised with subsequent penalties becoming due if the default continues.

2. HMRC charged Mr Hansard a number of penalties under both Schedule 55 and Schedule 56 in connection with the 2010-11 and 2011-12 tax years. In a decision released on 4 June 2018 (the "Decision") the First-tier Tribunal (Tax Chamber) (the "FTT") allowed Mr Hansard's appeal against some of those penalties and dismissed his appeal against others. HMRC were content to accept some aspects of the Decision but have appealed against other aspects of it. The penalties at issue for the purposes of this appeal are summarised in the attached table which we have gratefully adapted from Ms Poots's skeleton argument:

Year	**Type of penalty**	**Provision**	**Amount**	**Definition used in this decision**
2010-11	6 and 12 months late filing (assessed before return submitted)	Paras 5 and 6 of Schedule 55	2x£300	Initial £300 Penalties
	6 and 12 months late filing (assessed after return submitted)	Para 24(2)(b) of Schedule 55	2x£1,020	Recalculated Penalties
	Late Payment	Paras 1 and 3 of Schedule 56	3x£1,002	Late Payment Penalties
2011-12	Late Payment	Para 1 of Schedule 56	£120	

The applicable statutory regime

3. This appeal relates to points of detail relating to the way in which HMRC impose penalties. We need quote only certain statutory provisions in full; others can be summarised as their effect was not in dispute.

Late filing penalties under Schedule 55

4. Paragraph 5 of Schedule 55 provides for a penalty to be payable where a person has failed to deliver a return and that failure continues for more than six months. The penalty is:

> The greater of-
>
> > (a) 5% of any liability to tax which would have been shown in the return in question; and
> >
> > (b) £300.

5. Paragraph 6 of Schedule 55 provides for a further penalty where the failure to deliver the return continues for more than 12 months after the filing date. In the circumstances of this appeal, paragraph 6 provided for the penalty to be calculated on the same basis as in paragraph 5 (i.e. as the greater of 5% of the tax that would have been shown in the return or £300).

6. That formulation of the penalty gives rise to the obvious problem that, since both penalties are triggered by non-receipt of a tax return for a protracted period, HMRC may not know, at the point they wish to impose a penalty, how much tax "would have been shown in the return in question". That issue is addressed by paragraph 24 of Schedule 55 which provides, so far as relevant, as follows:

> **24 Determination of penalty geared to tax liability where no return made**
>
> (1) References to a liability to tax which would have been shown in a return are references to the amount which, if a complete and accurate return had been delivered on the filing date, would have been shown to be due or payable by the taxpayer in respect of the tax concerned for the period to which the return relates.
>
> (2) In the case of a penalty which is assessed at a time before P makes the return to which the penalty relates—
>
> > (a) HMRC is to determine the amount mentioned in sub-paragraph (1) to the best of HMRC's information and belief, and
> >
> > (b) if P[1] subsequently makes a return, the penalty must be re-assessed by reference to the amount of tax shown to be due and payable in that return (but subject to any amendments or corrections to the return).

7. Insofar as applicable to the penalties in dispute, paragraph 18 of Schedule 55 imposed requirements in connection with the charging of a penalty as follows:

> **18 Assessment**
>
> (1) Where P is liable for a penalty under any paragraph of this Schedule HMRC must—

[1] Throughout both Schedule 55 and Schedule 56, a taxpayer who is to be made subject to a penalty is referred to as "P".

(a) assess the penalty,

(b) notify P, and

(c) state in the notice the period in respect of which the penalty is assessed.

(2) A penalty under any paragraph of this Schedule must be paid before the end of the period of 30 days beginning with the day on which notification of the penalty is issued.

(3) An assessment of a penalty under any paragraph of this Schedule—

(a) is to be treated for procedural purposes in the same way as an assessment to tax (except in respect of a matter expressly provided for by this Schedule),

(b) may be enforced as if it were an assessment to tax, and

(c) may be combined with an assessment to tax.

(4) A supplementary assessment may be made in respect of a penalty if an earlier assessment operated by reference to an underestimate of the liability to tax which would have been shown in a return.

(5) A replacement assessment may be made in respect of a penalty if an earlier assessment operated by reference to an overestimate of the liability to tax which would have been shown in a return.

8. For tax years 2014-15 onwards, paragraph 18(5) was replaced by different machinery for dealing with the situation where there has been an overestimate of the liability to tax which would have been shown in the return.

Late payment penalties under Schedule 56

9. Schedule 56 penalises a failure to pay tax on time (as distinct from a failure to file a return on time which is the province of Schedule 55). Successive penalties are imposed depending on how late payment is made. In the context of income tax (with which this appeal is concerned), the first penalty arises under paragraph 3 of Schedule 56 if the payment is more than 30 days late. Paragraph 1(4) of Schedule 56 defines the date 31 days after the due date as the "penalty date". Paragraph 3 of Schedule 56 imposes further penalties if payment has not been made by 5 months after the penalty date (broadly 6 months after the due date) or 11 months after the penalty date (broadly 12 months after the due date). The amount of all these penalties is, by virtue of paragraph 3 of Schedule 56, 5% of the unpaid tax.

10. Paragraph 11 of Schedule 56 imposes requirements in connection with the charging of late payment penalties that are in all material respects identical to those of paragraph 18 quoted above. In particular, therefore, a penalty under paragraph 1 of Schedule 56 has to be both "assessed" and "notified to P".

The decision of the FTT

11. We summarise below the key aspects of the Decision only insofar as relevant to this appeal. References in this section in square brackets are to paragraphs of the Decision unless stated otherwise.

12. Mr Hansard submitted his tax return for the 2010-11 tax year on 23 April 2013 in paper form. When submitted, the tax return showed an aggregate liability to tax and Class 4 NICs of £26,416.36 ([19]). The due date for a return in paper form was 31 October 2011 ([13]). The due date for payment of the 2010-11 tax liability was 31 January 2012 but Mr Hansard did not pay his liability until 22 May 2013 ([150]).

13. The date by which income tax was due for the 2011-12 tax year was 31 January 2013 ([24]). Mr Hansard did not pay that tax until 22 May 2013 ([155]).

14. On 7 August 2012, HMRC issued a notice of assessment of an Initial £300 Penalty under paragraph 5 of Schedule 55 on the basis that Mr Hansard's return for 2010-11 was over 6 months late. The penalty was set at £300, the lowest amount permitted by paragraph 5 of Schedule 55 ([11]).

15. On 19 February 2012, HMRC issued a notice of assessment of a further Initial £300 Penalty under paragraph 6 of Schedule 55 on the basis that Mr Hansard's return for 2010-11 was over 12 months late. That penalty was also set at £300, the lowest amount permitted by paragraph 6 of Schedule 55 ([12]).

16. On 28 May 2013, by which time HMRC had received Mr Hansard's return for 2010-11, HMRC issued[2] the Recalculated Penalties of £1,020 each ([14] and [15]). The sum of each Recalculated Penalty of £1,020 and each corresponding Initial Penalty of £300 was £1,320 which was (when rounded down to the nearest whole pound) 5% of the aggregate tax and NIC liability of £26,416.36 ([96]).

17. Also on 28 May 2013, HMRC issued three Late Payment Penalties in respect of the 2010-11 tax year (each for £1,002) on the basis that the tax due for that year had not been paid within 30 days of the due date, or within 5 months or 11 months of the penalty date ([16] to [18]).

18. On 23 May 2013, HMRC issued a Late Payment Penalty in respect of the 2011-12 tax year ([24]). (In fact, Ms Poots pointed out that evidence before the FTT suggested that this penalty might have been issued on 23 April 2013 which might be significant since, if issued on that date, it might have been sent to the correct address. However, HMRC are not seeking to re-open this issue so we, and both parties, proceed on the basis that the Late Payment Penalty for 2011-12 was indeed issued on 23 May 2013).

19. Mr Hansard's grounds of appeal against the penalties HMRC imposed raised no issues as to the validity of those penalties or the procedure that HMRC had followed

[2] We use this neutral term because the FTT decided that penalty notices issued between 23 May 2013 and 9 July 2013 were not sent to the right address. Moreover, in referring to the "issue" of penalty notices, we are simply using a shorthand and should not be taken as prejudging the question whether an assessment of a penalty is a separate step from the notification of that penalty to a taxpayer.

before deciding to impose them. Nor did Mr Hansard seek to challenge the amount of the penalties that had been imposed. Rather, in his grounds of appeal, he argued that he had a reasonable excuse for the various defaults and so was not liable to penalties at all. The FTT decided that there was no reasonable excuse for either the failures to pay tax on time or the failures to file returns on time ([57] and [140]). Despite having rejected the only grounds of appeal that Mr Hansard had advanced, the FTT allowed his appeal against penalties on other grounds.

20. The FTT noted, in relation to the Initial £300 Penalties, that the penalty due was the higher of £300 and 5% of the liability to tax that would have been shown in the return in question ([82]). Moreover, since they were assessed before Mr Hansard had submitted his return for 2010-11, paragraph 24(2)(a) required HMRC to determine those penalties "to the best of their information and belief". At [84], the FTT concluded that it had been shown no evidence that any officer of HMRC (or any of the Commissioners of Revenue & Customs) had sought to determine what amount would have been shown in Mr Hansard's return if delivered. Instead, the FTT concluded in line with HMRC's published practice that HMRC's computer had simply generated, automatically, penalties of £300 (representing the minimum penalty that could be charged). The FTT concluded that this was not sufficient to meet the requirements of paragraph 24(2)(a) of Schedule 55 reasoning:

> 85. Nor was it suggested in the SoC, by HMRC at the hearing or in post-hearing submissions that the computer used by HMRC for this purpose had been programmed to consider what the amount might have been based, say, on previous returns. But in any event we do not think that any computer, however smart, let alone HMRC's one, can form a belief however much information it might have….
>
> 89. …In paragraph 24 HMRC is enabled to short cut the process of establishing what the tax actually is by making an early assessment of a tax geared penalty on the basis of a belief of an officer formed from information that officer has received or acquired. In our view when HMRC seek to short cut the penalty process by assessing before the return is filed they must follow the law, even if the automatic exercise may sometimes underestimate the actual penalty that will become due and will never overestimate it.
>
> 90. We therefore find that in the absence of any exercise such as is required by paragraph 24 Schedule 55 FA 2009 the assessment of £300 is not a valid assessment made in accordance with the requirements of paragraph 24 Schedule 55. We therefore cancel it.

21. Turning to the Recalculated Penalties, the FTT observed that paragraph 24 of Schedule 55 required penalties to be "reassessed" once the relevant tax return was submitted. The FTT concluded that a "reassessment" had to replace completely the original assessment ([103] and [108]). Therefore, the FTT concluded that the Recalculated Penalties were determinations of the total amount of late filing penalties that were and that HMRC were not entitled to both the Recalculated Penalties and the Initial £300 Penalties. Applying that approach, the FTT indicated that, subject to what followed in the Decision, it would have upheld the Recalculated Penalties of £1,020 ([108]) on the basis that they represented assessment of the total 6-month and 12-month

late filing penalties but would, in consequence, have set aside the Initial £300 Penalties. The FTT acknowledged that it did not need to set aside the Initial £300 Penalties on this basis since it had already set them aside for different reasons.

22. The FTT went on to decide that the Recalculated Penalties were not validly served on Mr Hansard. It noted that HMRC's records showed that, on 23 May 2013, when the Recalculated Penalties were served, HMRC's records on their self-assessment systems simply showed Mr Hansard's address as "Lot 2" with nothing further ([110]). The FTT noted evidence that HMRC produced from their PAYE system which showed a much fuller address for Mr Hansard. However, the FTT concluded that the Recalculated Penalties would simply have been addressed to "Lot 2" (as that was the address appearing in the self-assessment system) and as such these penalties were not properly addressed. The Recalculated Penalties were therefore cancelled as not being validly served ([112]).

23. The FTT reached a similar conclusion on the Late Payment Penalties for the 2010-11 tax year of £1,002 each. The FTT was briefly troubled by the fact that these Late Payment Penalties were not for 5% of the amount of income tax and Class 4 NIC unpaid (£26,416) but rather represented 5% of the smaller amount of £20,040. However, the FTT concluded that little turned on that point since the real problem with these Late Payment Penalties was that they had not been validly served on Mr Hansard ([154]) and it cancelled them for that reason[3].

24. The FTT's conclusion on the Late Payment Penalty for 2011-12 was identical: it was cancelled on the basis that it had not been validly served on Mr Hansard (see [166]).

HMRC's Grounds of Appeal

25. Both parties agree that HMRC's grounds of appeal are appropriately summarised as follows:

> (1) The FTT erred in law in concluding that the Initial £300 Penalties were invalid.
>
> (2) The FTT erred in law in concluding that the Recalculated Penalties replaced the Initial £300 Penalties rather than supplementing them.
>
> (3) While, having not obtained permission to appeal against the FTT's factual findings, HMRC must now accept that the assessments for the Recalculated Penalties and Late Payment Penalties were not properly notified to Mr Hansard, the underlying assessments remain valid and so the FTT should not have cancelled them.

[3] At the hearing before us, counsel and HMRC between them worked out that Mr Hansard had been charged late payment penalties of £1,002 because, owing to overpayments in previous years, the amount of tax actually paid late for 2010-11 was not the full amount shown in his return for that year.

Ground 1

26. We accept Mr Gordon's submission that the penalties imposed by paragraphs 5 and 6 of Schedule 55 are mandatory. If a taxpayer is, to use a shorthand, 6 months or 12 months late in filing a tax return, that taxpayer "is liable to a penalty" under those paragraphs. HMRC have no general discretion (absent the presence of "special circumstances" referred to in paragraph 16 of Schedule 55 which are not argued to be present in this appeal) as to the amount of the penalty. Therefore, for the purposes of this appeal, Mr Hansard could only be charged penalties under paragraph 5 and 6 of Schedule 55 of the higher of £300 and 5% of any liability to tax which would have been shown in the return in question.

27. Mr Gordon points to what he submits to be the mandatory requirement of paragraph 24(2)(a). If a penalty under paragraph 5 or paragraph 6 is to be assessed before a taxpayer has submitted a return, HMRC "is to determine" the amount mentioned in paragraph 24(1) (i.e. the amount that would have been shown in a hypothetical complete and accurate return) to the best of HMRC's information and belief. That, he argues, means that before HMRC can validly issue any penalty under paragraph 5 or 6 when a return has not yet been delivered, an officer or officers of HMRC must turn their mind to the question of what amounts would, to the best of their information and belief, have been shown in an accurate tax return. That requirement is not met if HMRC, or HMRC's computers, simply generate a penalty of £300 without any thought or consideration of the taxpayer's likely true tax liability.

28. We quite accept that the phrase "HMRC is to determine" can, as a matter of ordinary English, mean that "HMRC must in all cases determine". As Mr Gordon observed in his oral submissions, a statement that "bicycles are not to be chained to these railings" is a statement that, in no case, may a bicycle be so chained.

29. Ms Poots submitted that the correct construction of paragraph 24(2)(a) was that it means that where HMRC determines the amount that would have been shown in a return, HMRC have to do so to the best of their information and belief.

30. In our view this is indeed a possible interpretation of the statutory language. To adapt and extend Mr Gordon's analogy, on this view the requirement of paragraph 24(2)(a) is not dissimilar to the familiar requirement in notices on escalators that "dogs must be carried". This, of course, does not impose a mandatory requirement on all passengers to carry dogs; rather it is saying that if a passenger is accompanied by a dog while on an escalator that dog must be carried. Ms Poots's construction of paragraph 24(2)(a) is similar: the apparently mandatory requirement is engaged only where relevant: i.e. if the liability that would have been shown in a return is germane to the amount of a penalty.

31. It can be seen that the rival constructions do not depend on giving a different meaning to the words "HMRC is to determine". Both counsel accept that this imposes a requirement. The difference is that Mr Gordon invites us to read the paragraph as in effect saying "In every case HMRC must determine the amount to the best of their information and belief" whereas Ms Poots invites us to read it as in effect saying

"Where HMRC determine the amount they must do so to the best of their information and belief."

32. Where there are two possible constructions of a statute, the task of the tribunal is to seek to identify what Parliament intended. In doing so it can have regard, among other things, to the structure of the legislation as a whole, and the practical consequences of the rival constructions.

33. For the reasons that follow we prefer Ms Poots's construction.

34. First, we consider that it is significant that paragraph 24(2) of Schedule 55 expressly envisages that HMRC are entitled to charge a penalty under paragraph 5 or 6 before the taxpayer submits a return and so before the amount of tax shown in that return is known. Paragraph 24(2)(b) deals with that by providing that, if the taxpayer submits a return, the penalty must be reassessed so that it is for the (mandatory) amount required by the legislation. More generally, paragraph 18(4) and 18(5) of Schedule 55 recognise that there might need to be "supplementary" or "replacement" penalty assessments as better information becomes available. In short, the legislation envisages that the process by which penalties under paragraph 5 and 6 are issued may be iterative which leads, over a period of time, to assessment of the correct, mandatory amount.

35. Second, paragraphs 5 and 6 specify the penalty to be the higher of £300 and 5% of any "liability to tax which would have been shown in the return in question". That latter phrase is treated as a defined term whose meaning is given by paragraph 24(1). If HMRC are proposing to issue a penalty under paragraphs 5 and 6 before the return is submitted (as paragraph 24(2) expressly permits), both they and the taxpayer can be confident that a penalty of £300 can never exceed the penalty that is due. Moreover, even if the actual penalty payable turns out to be more than £300 a process of iteration can be followed to ensure that ultimately the correct penalty is charged. Therefore, there is no obvious need why the meaning of the defined term in paragraph 24(1) needs to be considered in a situation where HMRC are proposing to issue an initial penalty of exactly £300.

36. Third, we accept Ms Poots's submission that if Parliament had intended to require HMRC to make a calculation at the outset in every case, one would expect Parliament to have used clearer language. This is especially so as it must have been apparent that for HMRC to have to estimate the amount of tax that would have been shown in a return at a time when it is not known what that return would say would in many cases be something that would be difficult for HMRC to do, and in every case place a significant and resource-intensive burden on HMRC. It is far from obvious why Parliament would have wanted that: as long as a return was in due course made, it would not lead to any greater penalties ultimately being collected, but in the meantime it would expose taxpayers to the risk of having to pay penalties that turned out to be too high. By contrast, it is not difficult to see why Parliament would have wanted to ensure, in the interests of taxpayers, that if HMRC did estimate the amount, they should have to do so to the best of their information and belief.

37. For these reasons it is our view that, when Parliament specifies in paragraph 24(2)(a) that HMRC "is to determine" the amount of tax that would be shown in an accurate return, it is not imposing a mandatory requirement for HMRC to perform that calculation at all stages in the iterative process of determining penalties. Rather, Parliament is stating that if the amount of tax that would have appeared in an accurate return is germane to a penalty being charged at a particular point in the iterative process, HMRC must determine that amount to the best of their information and belief.

38. Understood in that context, the purpose of paragraph 24(2)(a) is to protect taxpayers against penalty assessments, made at a time when no tax return has been delivered, on the basis of wildly inaccurate estimates of the taxpayer's likely tax liability which are not supported by HMRC's information or belief. A taxpayer receiving a penalty of £300 needs no such protection since (absent special circumstances to which the specific regime in paragraph 16 of Schedule 55 applies), the penalty can never be lower than £300.

39. Mr Gordon submitted that this approach produces anomalies. For example, a taxpayer may be 6 months late with a tax return and, following the approach outlined above, HMRC might decide, without considering the taxpayer's likely tax liability, to issue a penalty of precisely £300. The taxpayer might fail altogether to submit a return (so paragraph 24(2)(b) would not be engaged so as to require HMRC to reassess the penalty). HMRC might exercise their powers under s28C of the Taxes Management Act 1970 ("TMA 1970") to make a determination that, say, £100,000 of tax is due. Mr Gordon argued that, in such a case, because paragraph 24(2)(b) is not engaged, there would be no mechanism for HMRC to increase the £300 penalty and assess the penalty at 5% of the unpaid tax (£5,000).

40. We do not accept that argument. In such a case, HMRC could make a supplementary assessment under paragraph 18(4). We acknowledge that, when assessing the penalty at £300, HMRC might have made no estimate of the taxpayer's liability to tax. However, we nevertheless consider the requirements of paragraph 18(4) would be met since a penalty of £300 could not be correct in the light of HMRC's subsequent view that (to the best of their information and belief) the tax liability that would have been shown in an accurate return was £100,000. In that sense, therefore, the penalty of £300 would have been based on an "underestimate of the liability to tax which would have been shown in a return", so triggering the application of paragraph 18(4).

41. Nor do we accept Mr Gordon's submission that our approach risks giving taxpayers a "false sense of security". The essence of that submission was that a taxpayer who is likely to have a tax liability of £20,000 might be 6 months late with a return and receive a penalty of just £300 (without any consideration of the likely tax liability). Having received a modest penalty, the taxpayer might not realise the full consequences of continued late submission and leave the return outstanding for a further 6 months (thereby becoming liable for both a 6-month and 12-month late filing penalty). On filing a return 12 months late, the taxpayer would receive two penalties each of £1,000. By contrast, if HMRC had, when the return was 6 months late, been required to issue the taxpayer with a penalty of £1,000 (following an examination of the likely overall tax

liability), the taxpayer would have realised the urgency of the situation and at least not been charged the second £1,000 penalty. We acknowledge that unwise taxpayers might find themselves in such a situation. However, we consider that has little bearing on the question of statutory construction with which we are concerned. In particular, we see no indication that Parliament intended, in paragraph 24(2)(a) of Schedule 55, to require HMRC to perform unnecessary analyses of the likely tax liabilities of taxpayers who had not submitted tax returns which have no bearing on the penalty proposed to be charged simply to avoid giving non-compliant taxpayers a "false sense of security". Taxpayers who fail to meet their statutory obligations should expect to answer for the consequences even if those consequences are more severe than they might have thought.

42. In a related argument, Mr Gordon submits that HMRC must in all cases base penalties on a "best of information and belief" determination of a taxpayer's liability to tax because a taxpayer receiving a modest £300 penalty might choose not to appeal that penalty and be out of time to appeal if and when the £300 penalty is re-assessed on submission of the return. We see little force in that argument as a taxpayer could appeal against the re-assessed penalty even in the absence of an appeal against the first £300 penalty.

43. As we have observed at [39], Mr Gordon drew our attention to the fact that an officer of HMRC has, pursuant to s28C of TMA 1970, the power to make a "determination", to the best of that officer's information and belief, of the tax liability of a person who fails to submit a return. There is, therefore, an overlap between the wording of paragraph 24(2)(a) of Schedule 55 and the provisions of s28C of TMA 1970. If Schedule 55 had provided that a penalty under paragraph 5 or 6 could only be charged once HMRC exercised their power under s28C of TMA 1970, that overlap in wording might point in favour of a conclusion that HMRC had to use the figure they applied under s28C as the basis for a penalty under paragraph 5 or 6 of Schedule 55. However, penalties under paragraph 5 and 6 can be imposed as soon as the return is six or twelve months late, whether or not a determination under s28C has been made, and we therefore saw little significance in the overlap in wording.

44. We are fortified in our conclusion as to the correct construction of Schedule 55 by the decision of the Court of Appeal in *HMRC v Donaldson* [2016] STC 2511. That case concerned, among other matters, the requirement in paragraph 4(1) of Schedule 55 for HMRC to "decide" that daily penalties should be payable. The taxpayers argued that, to be valid, any such decision had to be on a "taxpayer-by-taxpayer" basis. HMRC considered that a high level policy decision that all taxpayers who were more than 3 months late in submitting their returns should be charged daily penalties was sufficient. On this point, Lord Dyson MR said:

> [14] I start by saying that I agree with the observation made at para [43] of the decision of the UT:
>
> 'We do not think it can have been within the contemplation of the draftsman that HMRC should be required to make a decision on a taxpayer-by-taxpayer basis, since he must have been aware that it would be impractical to exercise a discretion (meaning a discretion exercised

> in respect of each taxpayer individually, rather than in relation to defaulting taxpayers as a body) in that way. Rather, we think, this provision too contemplates what HMRC have in fact done, that is decide in advance that all taxpayers who default for more than three months should suffer daily penalties. In other words, what was contemplated was that the discretion conferred by the provision should be capable of being exercised in respect of all taxpayers who default for the requisite period, or none; and if that is so the purpose of the notice is to inform taxpayers who are in danger of incurring daily penalties that HMRC have decided to impose them.'
>
> [15] It seems to me that it is inherently unlikely that Parliament intended that HMRC should be required to make a decision by exercising a discretion on an individual taxpayer-by-taxpayer basis. Parliament has addressed the issue of the individual circumstances of P by providing [the defence of "reasonable excuse" in paragraph 23 of Schedule 55].

45. We quite agree with Mr Gordon that the Court of Appeal was considering a different aspect of Schedule 55. Moreover, the penalties imposed under paragraphs 5 and 6 of Schedule 55 are calculated by reference to the tax that would have been shown in an accurate return by that taxpayer and so are necessarily more linked to a taxpayer's specific circumstances than the fixed penalties of £10 per day that the Court of Appeal was considering. However, even acknowledging those points of distinction, the Court of Appeal in *Donaldson* set out an approach to the construction of Schedule 55, namely that Parliament recognises that the provisions contained therein are of potential application to large numbers of taxpayer and therefore that those provisions should be capable of practical application. It would be impractical for HMRC to be required, in a situation where they are proposing for the time being, and as part of an iterative process, to issue a penalty of £300 which could in no circumstances be excessive, to engage in the kind of forensic analysis necessary to satisfy the requirement of determining what tax liability would have been disclosed in an accurate return (if submitted) "to the best of HMRC's information and belief". Mr Gordon's submission that, if the requirement is onerous, HMRC should petition for more resources misses the point: the fact that the requirement is impractical where a penalty of £300 is to be issued, points against the construction of paragraph 24(2)(a) that he advances.

46. Both parties referred in their skeleton arguments to draft legislation that has been published setting out possible changes to Schedule 55. However, we agree with the parties that this draft legislation can be of little, if any, assistance in construing paragraph 24(2)(a) and we will not, therefore, refer to it.

47. For the reasons we have given above, we consider Ground 1 of HMRC's appeal to be established.

Ground 2

48. Paragraph 24(2)(b) of Schedule 55 required the Initial £300 Penalties to be "reassessed" when Mr Hansard delivered his tax return for 2010-11. The parties were rightly agreed that this is a mandatory requirement. The essence of their dispute was how the "reassessment" could permissibly be achieved. HMRC argue that can be

achieved by issuing additional assessments which, when put together with the Initial £300 Penalties result in penalties being assessed in the right amount. Mr Hansard argues that a "reassessment" can only be achieved by making a new assessment that completely replaces the Initial £300 Penalties and causes the Initial £300 Penalties no longer to be due.

49. What HMRC in fact did in the present case can be seen from the Decision at [106]. The FTT did not have the actual notices sent out by HMRC but on the basis of evidence as to the standard forms, set out what they said they could confidently assume to have been sent as follows:

> **6 months late** – now you have filed your tax return you have a further penalty to pay. The revised penalty is 5% of £26,416.00 (the total tax due), less the £300 penalty already charged on the tax we determined was due. £1,020

As can be seen that explains how the calculation has been made (at 5% of the tax due) and then gives credit for the £300 already charged, thereby assessing the taxpayer to a penalty of the net figure remaining due. On the face of it that seems to us to be an eminently sensible way for HMRC to proceed which does not prejudice anybody. But if the FTT, and Mr Gordon, are right HMRC was unable to proceed in this way.

50. In our view there is no reason why HMRC cannot proceed as they have done. There is no statutory definition of the term "reassessed". We accept Ms Poots's submission that there can be a reassessment where the penalties are "assessed again". Conceptually, the process of assessing again could involve either making a new assessment which completely replaces the first or making an assessment in addition to the first. Parliament has not prescribed either course and, therefore, we conclude that either is permissible.

51. In reaching a contrary conclusion, the FTT was influenced, at [98] to [103] by the concepts of a "supplementary assessment" referred to in paragraph 18(4) and a "replacement assessment" referred to in paragraph 18(5) and by an "apparent clash" between paragraph 18(4) and paragraph 24(2)(b). In respectful disagreement with the FTT we consider that the wording of paragraph 18(4) and 18(5) provides (oblique) support for our approach to the interpretation of the word "reassessed". Specifically, in paragraphs 18(4) and 18(5), Parliament distinguished between "supplementary assessments" (which add to assessments already made) and "replacement assessments" (which completely replace assessments already made). However, having shown itself to be alive to this distinction, in paragraph 24(2)(b), Parliament used the neutral term "reassessed" which suggests to us that it did not wish to prescribe whether such assessments should be either additional to, or in replacement of, assessments already made.

52. We also agree with Ms Poots that there is no "clash" between paragraph 24(2)(b) and paragraph 18(4). Paragraph 24(2)(b) applies in the specific situation where (i) HMRC assess a penalty before a return is made and (ii) the taxpayer subsequently submits a return. Paragraph 18(4) operates more widely. For example, it could apply if the penalty is assessed after the taxpayer submits a return, but the amount of tax due changes following a valid amendment to that return. Paragraphs 18(4) and 24(2)(b)

may, therefore, deal with situations which overlap, but we do not consider they "clash". For ourselves, we would think that HMRC could satisfy the obligation (under paragraph 24(2)(b)) to "reassess" by making a "supplementary assessment" (in accordance with paragraph 18(4)). However, since HMRC focused their case on paragraph 24(2)(b), we will not make any determination to this effect.

53. Finally, in his oral submissions, Mr Gordon argued that paragraph 19 of Schedule 55 supplied an inference that, to "reassess", HMRC had to replace completely an original assessment. Paragraph 19 sets out time limits that apply to penalty assessments but provides that those time limits are not to apply to a "reassessment under paragraph 24(2)(b)". No doubt the reason why reassessments under paragraph 24(2)(b) are not subject to the time limits in paragraph 19 is because reassessments can take place only after a tax return is filed, a process over which the taxpayer alone has control. It would be undesirable if a taxpayer could make a reassessment out of time simply by delaying the submission of the very return whose late submission is to be penalised[4]. The exclusion of reassessments under paragraph 24(2)(b) from the time limits in paragraph 19 does not, in our judgment, support an inference that a reassessment under paragraph 24(2)(b) must completely replace the original assessment.

54. For the reasons set out above, we accept HMRC's submissions and allow their appeal on Ground 2.

Ground 3

55. Ground 3 relates only to the Recalculated Penalties and the Late Payment Penalties; it is not relevant to the Initial £300 Penalties.

56. As we have noted, the FTT's factual conclusion, which is not under appeal, was that these penalties were addressed simply to "Lot 2", an incomplete part of Mr Hansard's then address[5]. Having reached that factual conclusion, the FTT decided:

> 112. These penalties are therefore cancelled as not being validly served.

57. In their skeleton argument, HMRC submitted that *Honig v Sarsfield* [1986] STC 246 is authority for the proposition that there is a distinction between the making of an assessment and the giving of notice of that assessment. Therefore, they submit that they made a valid assessment of the penalties (when they were entered into HMRC's computer system being the modern-day equivalent of the "assessment books" referred to in *Honig v Sarsfield*) and that, if they failed to notify that assessment to Mr Hansard, the consequence was simply that the penalties could not be enforced until they were notified applying the principle in *Grunwick Processing Laboratories Ltd v Customs*

[4] We do not immediately see why no time limit at all should apply (and why, for example, the time limit for making a reassessment is not expressed as a certain period after the return is submitted) although that is not an issue that arises in this appeal.

[5] We have some doubts whether we would have come to the same conclusion on the facts as what the computer record before the FTT showed was line 1 of the address, and it was never explained how, on the assumption the notices were simply addressed to "Lot 2", Mr Hansard was able to appeal them as he did. But as we have explained this is not a matter for us.

and Excise Commissioners [1986] STC 441. In HMRC's submission, the FTT was wrong to "cancel" the penalties even though (as HMRC are now bound to accept) those penalties were not validly served.

58. That position was developed in Ms Poots's oral submissions. In those submissions, Ms Poots accepted that Mr Hansard had exercised his right of appeal against HMRC's decision that penalties were payable (paragraph 20(1) of Schedule 55 and paragraph 13(1) of Schedule 56) and had not exercised his right (in paragraphs 20(2) of Schedule 55 and 13(2) of Schedule 56) to appeal against the amount of the penalty payable. She accepted that, in those circumstances, the FTT's power under paragraph 22(1) of Schedule 55 and paragraph 15(1) of Schedule 56 was to "affirm or cancel HMRC's decision".

59. Ms Poots did not seek to argue that the FTT should have "affirmed" HMRC's decision. Rather, she observed that the wellspring of the FTT's jurisdiction was Mr Hansard's right of appeal under s31(1)(d) of TMA 1970[6] and that under s31A(4) of TMA 1970, notice of that appeal must be given within 30 days after that on which the "notice of assessment was issued". Therefore, she argued, the FTT should have concluded that, since HMRC had not served notice of the penalties on Mr Hansard, the FTT's jurisdiction was not engaged.

60. Ms Poots noted that, until the FTT hearing, HMRC did not know that there was any problem with service of the penalty notice. They only realised there was an issue when the FTT (of its own motion) enquired into the address details that HMRC had on file for Mr Hansard. In those circumstances, she submitted that the FTT should not have decided that the penalties were "cancelled". It should have left open the possibility of the FTT subsequently curing the defect in service and seeking penalties in the future.

61. In our judgment, HMRC's Ground 3 has to be considered in the light of the statutory provisions applicable to the specific penalties being charged. General principles (such as those in *Honig v Sarsfield* and *Grunwick*) can certainly illuminate the meaning of those specific provisions, but are not a substitute for them. In what follows, we will explain our reasoning by reference to the statutory provisions of Schedule 55 only as those in Schedule 56 are in all respects identical.

62. Paragraph 18 of Schedule 55 provides that, "where P is liable for a penalty", HMRC must both assess that penalty and "notify P". That suggests that the statute envisages that "liability" for a penalty is a separate matter from notification and assessment and that, once HMRC have formed the view that liability is established, they are obliged to take the procedural steps of assessment and notification. Moreover, by paragraph 20 of Schedule 55, Mr Hansard's right of appeal was against "a decision of HMRC that a penalty is payable". That suggests that his appeal was not just against HMRC's conclusion that the conditions necessary to establish liability were established, but rather against their overall conclusion that a penalty was actually payable. In particular, we consider that paragraph 20 entitles Mr Hansard, in an appeal, to argue not just that

[6] Since paragraph 22 of Schedule 55 and paragraph 14 of Schedule 56 treat appeals against penalties in the same way as appeals against an assessment to the tax concerned.

he was not "liable" to a penalty, but also that, because HMRC had not followed the mandatory requirements of paragraph 18, even if he was "liable", no penalty is actually "payable".

63. We derive some support for this approach from the decision of the Court of Appeal in *Donaldson* to which we have already referred. In that case, Mr Donaldson sought to argue that because notices that he was sent failed the requirements of paragraph 18(1)(c) of Schedule 55 (as they failed to mention the period in respect of which the penalty was assessed), his appeal against those penalties should be allowed. The Court of Appeal approached the matter by considering whether the requirements of paragraph 18(1)(c) were met. Having concluded that they were not met, the Court of Appeal decided that s114 of TMA 1970 "saved" the penalty notices. The clear implication of the judgment in *Donaldson* is that, if the notices had not been saved, the penalties would have been set aside.

64. Applying that approach, the FTT reached the factual conclusion that the penalty notices were sent simply to "Lot 2" and described this as a failure of "service". However, read in context, it was clearly considering the question whether the penalties were "notified" since, even though it considered (at [111]) how Mr Hansard had been able to appeal against the assessments without being aware of them, it made no finding to the effect that, even though the penalty assessments were sent to "Lot 2", HMRC nevertheless notified those penalties to Mr Hansard by another means. The FTT had power to make only two possible decisions: it could either affirm HMRC's decision that the penalties were payable or it could cancel those decisions. Having found that the mandatory requirements of paragraph 18 of Schedule 55 and paragraph 11 of Schedule 56 were not met, the FTT made no error of law in deciding that, of those two options, it would choose to cancel the penalties.

65. We do not accept HMRC's argument that, having found that the penalties were not notified, the FTT should have declined jurisdiction altogether on the basis of the argument summarised at [59]. Section 31A(4) of TMA 1970, on which HMRC rely, is a provision governing time-limits whose purpose is to protect HMRC against the risk of having decisions challenged unduly long after those decisions were made. We do not consider that s31A(4) is intended to deny the FTT jurisdiction in situations where a taxpayer is denying that an HMRC assessment was properly served or notified. In any event, the time limit in this case runs from the date the notices of penalty assessments were "issued". Even though those notices were not properly "notified" to Mr Hansard, we still consider they were "issued" in the requisite sense[7].

66. It follows that we dismiss HMRC's appeal on Ground 3.

67. Both HMRC and Mr Hansard urge us to express some views on the current status of the penalties. HMRC have asked us to express the view that it is still open to HMRC

[7] At [39] to [46] of the Decision, the FTT dealt with the question of whether Mr Hansard's appeals were in-time and, if not, whether it would exercise its power to permit him to make late appeals. HMRC have not sought to appeal against the FTT's decision to give Mr Hansard permission to make late appeals.

(provided that they now "notify" the penalties to Mr Hansard) to succeed in establishing that those penalties are properly payable. In particular, HMRC note that paragraph 19 of Schedule 55 and paragraph 12 of Schedule 56 set out statutory time limits for the assessment of penalties but, applying the distinction between assessment and notification set out in *Honig v Sarsfield* impose no deadlines within which notification under paragraph 18 must take place. While HMRC acknowledge that their public law duties would not permit them to make an in-time assessment of penalties and then wait 5 years before sending a notification of that penalty to a taxpayer, they submit that they have behaved reasonably in this case since the first they became aware of a problem with notification of the penalties was during the FTT hearing.

68. Mr Hansard, by contrast, submits that paragraph 18 of Schedule 55 and paragraph 11 of Schedule 56 requires that the separate stages of "assessment" of a penalty and "notification" should take place as part of a "coherent whole". He submits that, if HMRC purported following release of this decision, to notify the penalties to Mr Hansard to establish that a penalty is now payable, there would be no such "coherent whole".

69. We do not consider that we should say anything about the status of the penalties should HMRC decide to take fresh steps to notify those penalties to Mr Hansard. Doing so would involve answering hypothetical questions since (i) HMRC may decide not to seek to collect the penalties and so may be content not to notify them to Mr Hansard and (ii) Mr Hansard may decide not to appeal against any penalties that are so notified. If the penalties are notified, and appealed, it will be a question for the FTT in the first instance to decide whether HMRC's decision that such penalties are payable should be upheld or cancelled.

Disposition

70. The Decision contains errors of law. The FTT was wrong to set aside the Initial £300 Penalties (Ground 1). The FTT also made the errors of law relating to the Recalculated Penalties set out in Ground 2, but these did not affect the overall conclusion since it was correct to decide (as discussed under Ground 3) that the Recalculated Penalties and Late Payment Penalties were not payable.

71. We remake the Decision so as to uphold HMRC's decision that the Initial £300 Penalties are payable and to cancel HMRC's decision that the Recalculated Penalties and the Late Payment Penalties are payable.

72. Finally, we would like to record our thanks to Mr Gordon for acting *pro bono*, thereby ensuring that we had the benefit of his clear and useful submissions on Mr Hansard's behalf.

MR JUSTICE NUGEE
JUDGE JONATHAN RICHARDS

RELEASE DATE: 24 December 2019