La peine quotidienne

Management of taxes

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Keith Gordon discusses the validity of £10 daily penalty notices for late tax returns

Key Points

What is the issue?

The *Donaldson* case concerns HMRC's appeal against a First-tier ruling that the legislative requirements for the daily penalties had not been met

What does it mean for me?

Whereas the statute provides that liability for the £100 and £300 penalties arises automatically once a tax return is late, the statute is more convoluted for the £10 daily penalties

What can I take away?

The Upper Tribunal decided in favour of HMRC. This gives rise to the oddity that an individual might be notified of the risk of daily penalties when it is already too late to do anything to avoid them

In my article ‘The rise and fall of Christine Perrin’ in the August 2014 issue of Tax Adviser – which concerned the case of *Perrin v HMRC* [2014] UKFTT 488 (TC) – I discussed the harmonised penalty rules for late returns and late payments of tax as set out in FA 2009 Schs 55 and 56. There was one aspect of Mrs Perrin’s appeal that the First-tier did not consider – the daily £10 penalties for late returns because their validity was the subject of another case which the Upper Tribunal has now heard, namely *HMRC v Donaldson* [2014] UKUT 0536 (TCC).

The facts of the case

The case concerned Mr Donaldson’s 2011 tax return. A valid notice under TMA 1970 s 8 had been issued to Mr Donaldson in April 2011. That meant that the return was due to be submitted by 31 October 2011 (if submitted on paper), or by 31 January 2012 (if submitted online).

Mr Donaldson did not submit his return in any form by the latter day. Under Sch 55, para 3, he incurred a penalty of £100, which was imposed by notice issued on 15 February 2012.

Mr Donaldson appealed against the penalty notice on the ground of having a reasonable excuse; he said that the delay was his agent’s fault. HMRC told Mr Donaldson by letter on 18 April 2012 that they were unable to process the appeal unless he submitted his return and advised him of the risk of daily penalties. Presumably in response to this letter, Mr Donaldson filed his tax return by post on 1 May 2012.

Since it was a paper return sent more than six months late, Mr Donaldson was issued with a further penalty notice of £300 under Sch 55, para 5. At the same time, HMRC issued Mr Donaldson with a penalty notice imposing the maximum 90 days' worth of £10 daily penalties under para 4, for tax returns that are more than three months late.

Mr Donaldson appealed against these further penalties also on the ground of having a reasonable excuse. This excuse was rejected both by HMRC and the First-tier Tribunal.

However, the First-tier considered that the legislative requirements on the daily penalties had not been met. It therefore allowed Mr Donaldson's appeal so far as it concerned the £900 relating to the daily penalties. HMRC appealed to the Upper Tribunal against this part of the First-tier's decision.

The relevant legislation

Whereas the statute provides that liability for the £100 and £300 penalties arises automatically once a tax return is late (or, in the case of £300 penalties, more than six months late), the statute is more convoluted about the £10 daily penalties. Para 4(1) reads as follows:

4(1) P is liable to a penalty under this paragraph if (and only if) –

(a) P's failure continues after the end of the period of three months beginning with the penalty date,
(b) HMRC decide that such a penalty should be payable, and
(c) HMRC give notice to P specifying the date from which the penalty is payable.

In Mr Donaldson's case, there was no dispute that the condition in para 4(1)(a) was met. The First-tier Tribunal held, by the presiding judge's casting vote, that para 4(1)(b) was met. However, the First-tier held that the condition in para 4(1)(c) was not met. The basis of this conclusion was the First-tier's belief that the documents sent to Mr Donaldson did not constitute adequate notice.

Mr Donaldson took no active part in the appeal, so the Upper Tribunal's attention was focused on the subject matter of HMRC's appeal (para 4(1)(c)), although the interpretation of para 4(1)(b) was also considered by the Upper Tribunal.

The Upper Tribunal’s conclusion

The appeal came before the president of the Tax and Chancery Chamber of the Upper Tribunal, Mr Justice Warren, who sat with the president of the Tax Chamber of the First-tier Tribunal, Judge Colin Bishopp.

HMRC’s arguments focused on two notifications sent to Mr Donaldson, neither of which the First-tier Tribunal had considered sufficient to satisfy the requirements of para 4(1)(c).

The first of these documents was the reminder to file a tax return, sent to Mr Donaldson in late December 2011 or early January 2012. Although Mr Donaldson’s return was not necessarily late at that stage – he might still have filed online – the reminder notified the taxpayer that ‘daily penalties can be charged from 1 February for paper tax returns or 1 May for online tax returns’.

The second document was the £100 penalty notice issued automatically in February 2012. That was issued because a £100 penalty had been incurred by that stage, irrespective of how the return might eventually be filed. The notice contained advice on what to do next, including a request to submit the return ‘now to avoid further penalties’. It explained that daily £10 penalties ‘will’ be charged’, and that ‘daily penalties can be charged … starting from 1 February for paper returns or 1 May for online returns’.

Whereas the First-tier Tribunal had concluded that these documents were informal warnings as opposed to the notice required by the statute, the Upper Tribunal considered that they were sufficient to comply with para 4(1)(c). The First-tier had noted the mismatch in the wording between the statements that a daily £10 penalty ‘will be charged’, on the one hand, and the sentences that followed which used the more permissive ‘may’. However, the Upper Tribunal considered that the overall meaning was clear: penalties would indeed be charged and that two different start dates were possible.

Thus, HMRC’s appeal was allowed.

Commentary

Ever since I was engaged in the Tax Law Rewrite Project, I have had a particular interest in the drafting of clear tax legislation.

One positive aspect of the project has been the use of shorter sentences or at least ones with more sub-paragraphing and consequently a better, easier-to-follow layout. However, there seems to me a trend in recent years of having legislation that is superficially ‘rewrite-style’, but is in fact just as unclear as the legislation that the rewrite was supposed to replace.

Whenever I raise this issue, I am given the same answer: legislation is drafted in a hurry, often with unclear political aims, and therefore the quality of the output is less than ideal. I suspect that that is indeed part of the problem, but in my view it is not the only cause. There are some drafting techniques that should have been eradicated by the rewrite, but which have stubbornly remained in place.

However, returning to the stated reasons for unclear legislation, is it really excusable that the taxpaying public and their advisers have to deal with poor legislation because the politicians do not give the drafters adequate guidance on what they want or enough time for the drafting process to be properly undertaken? If a tax adviser were to tell a tribunal that they had made errors on a client’s tax return because of the volume of work, the tribunal would turn around and say that the adviser should take on more staff to ensure that the job is done properly. However, the rules that apply to taxpayers seem not to apply to government.

FA 2009 is an example of the problem. It is 458 pages long, including 61 schedules, plus the additional sheet issued in 2010 correcting the typos. Sch 55 contains the rules for penalising taxpayers who are late with their returns. We are not exactly talking about the most esoteric part of the tax system, so one would have expected the legislation to be relatively straightforward. However, as Donaldson demonstrates, four judges have reached three different views on the meaning of para 4(1). And I do not think that HMRC have got it right yet.

The Upper Tribunal’s decision means that the point on which Mr Donaldson won – determined by whether the condition in para 4(1)(c) was met – has now been decided in favour of HMRC. On balance, I think that the tribunal was correct on that point, but it does give rise to the oddity that an individual might be notified of the risk of daily penalties when it is already too late to do anything to avoid them.

The Upper Tribunal also considered in passing the meaning of para 4(1)(b). Since Mr Donaldson took no active role in the proceedings, the tribunal was not asked to comment on the point where the First-tier Tribunal had been divided. The dissenting view in the First-tier was that, for HMRC to 'decide' that daily penalties should be issued, this had to be effected by an individual officer on a case-to-case basis. However, the Upper Tribunal considered that the condition in that sub-paragraph was met by virtue of a policy decision taken by HMRC before the legislation came into force. For what it's worth, I am happy to accept that the wording of condition 4(1)(b) is satisfied by such a policy decision.

Nevertheless, the more natural meaning of para 4(1) is that a sequence of events is taking place: first, the return is more than three months late; second, a decision is taken that daily penalties should be payable; and third, a notice is given to the taxpayer to advise the taxpayer what is going on. Further, there were several issues on which the Upper Tribunal did not state an opinion and, had these points been considered, it is possible that it might have accepted what I describe as the more natural reading of the legislation.

Therefore, although the purpose of HMRC's appeal was partly to seek clarification of the meaning of para 4, it is my view that it would still be worth another taxpayer continuing to challenge the imposition of daily penalties.

The first issue that could be contested lies in para 4(1)(c) itself. That provision specifies that 'HMRC must give notice' to the taxpayer of the start date of the daily penalties. It seems to have been accepted by the Upper Tribunal that this can be satisfied by the issuing of notices via an automated process effected by computer. This is closely related to the dissenting view in the First-tier in relation to para 4(1)(b). However, it is my view that the point is even more pertinent to para 4(1)(c).

As I have said, the Upper Tribunal has proceeded on the assumption that a notice from HMRC is indeed the product of, what the statute requires being, 'HMRC give notice'. But how does the law interpret 'HMRC'? Para 27(3) defines 'HMRC' as 'Her Majesty's Revenue and Customs', which seemingly does not take us much further.

However, it is enough. In CRCA 2005 s 4(1), we find that 'the Commissioners and the officers of Revenue and Customs may together be referred to as Her Majesty's Revenue and Customs'. Therefore, consistent in fact with the Upper Tribunal's interpretation of para 4(1)(b), HMRC cannot be some mere computer, but requires

an individual, either a board member or an officer of the board. If that is correct it would appear that automated notices are not sufficient to comply with para 4(1)(c).

Second, the same point could be made in respect of para 18 of Sch 55. That requires the assessment and notification of a penalty to be by HMRC, which means an individual, not a computer. (There is a similar argument that could be deployed in relation to automated penalties issued under the previous legislation in the TMA 1970, which I have written about in Taxation – see ‘Hamstrung durch Technik’, 6 February 2014, p8 and ‘Technikal progress’, 20 November 2014, p8.)

Third, there is a point raised tentatively by the Upper Tribunal itself. I have not seen a penalty notice issued under para 18 and therefore cannot comment on whether this argument would succeed in practice. Nor did the Upper Tribunal, although it did see a specimen notice. The Upper Tribunal commented that the specimen did not appear to comply with the requirement in para 18(1)(c) which provides that the penalty notice must state ‘the period in respect of which the penalty is assessed’. As the meaning of para 18 was not a matter that was before the Upper Tribunal, it did not pursue the point. However, that does not rule out the matter being considered afresh in another case.