The Age of Reasonable Excuse

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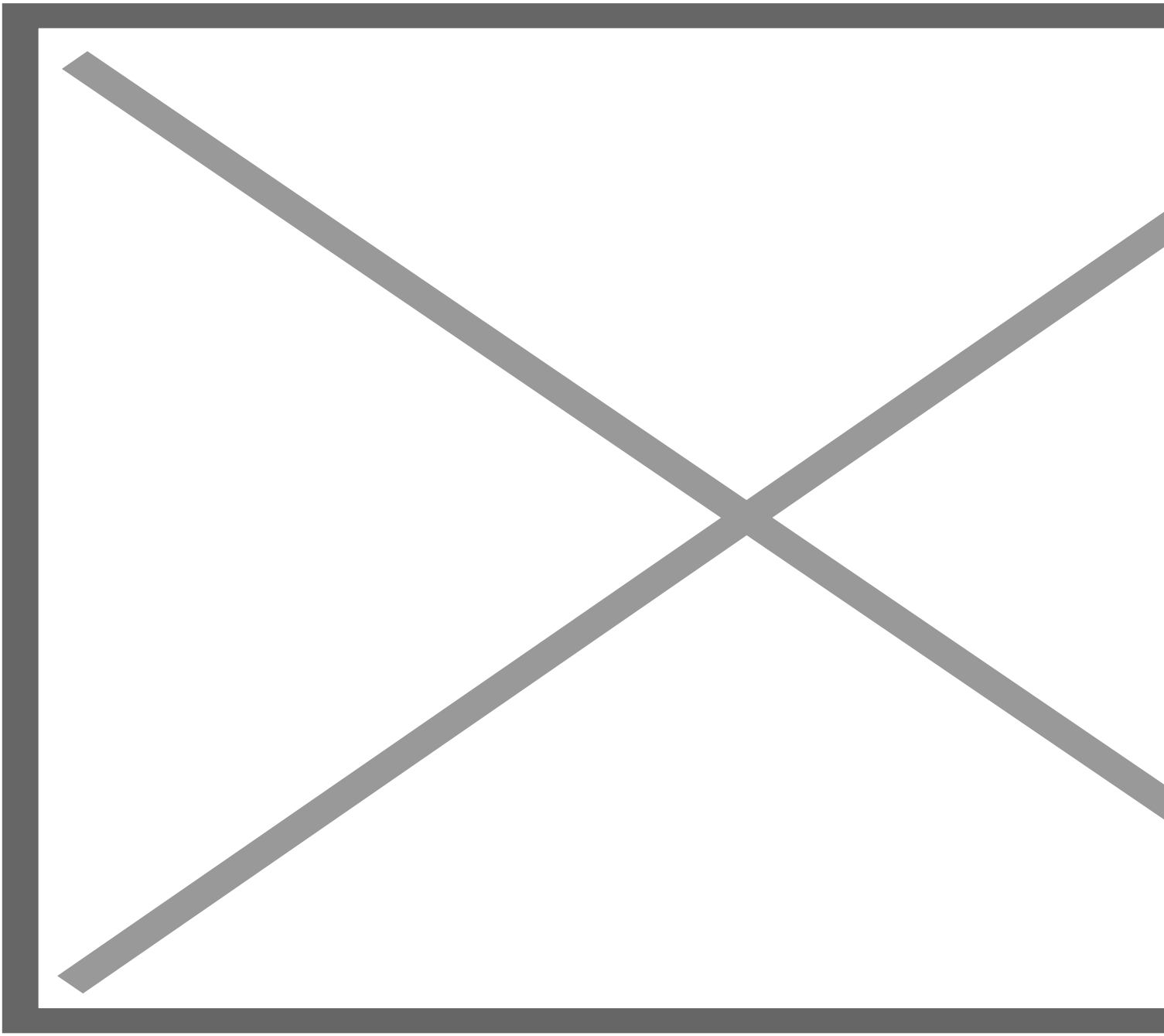

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Keith Gordon considers some penalty appeals where taxpayers failed to make a timely Non?Resident Capital Gains Tax return

Key Points

What is the issue?

FA 2015 eroded fiscal incentives afforded to non-residents who might wish to invest in the UK by extending the charge to capital gains tax to cover residential property in the UK held by non-residents.

What does it mean to me?

Perhaps unsurprisingly, not every non-resident made a timely tax return and penalties have accordingly been triggered.

What can I take away?

If you have a client who faces a NRCGT penalty, you should strongly consider appealing against it in a suitable case.

Historically, non-residents have been generally exempted from capital gains tax in respect of UK assets, with the key exception being in certain cases where the non-resident has carried on a business in the UK. However, in the Finance Act 2015, Parliament decided to erode further the fiscal incentives afforded to non-residents who might wish to invest in the UK by extending the charge to capital gains tax to cover residential property in the UK held by non-residents.

The legislation also imposed a requirement on non-residents to provide a tax return advising HMRC of the disposal, the NRCGT return being due 30 days after the completion of the disposal (Taxes Management Act 1970, section 12ZB). That return should also include a self-assessment of any tax that might be payable in relation to the disposal, although that requirement is disapplied in certain cases (particularly where the gain would be included in a normal Self Assessment tax return) (section 12ZE). The penalty provisions for late returns (FA 2009, Schedule 55) were amended so as to include late NRCGT returns.

Perhaps unsurprisingly, not every non-resident made a timely tax return and penalties have accordingly been triggered. A number of cases have been notified to the Tribunal, with taxpayers generally claiming reasonable excuse for their failure. The outcome of these appeals has been mixed, as illustrated by the two cases discussed in this article, *Smith & Smith v HMRC* [2018] UKFTT 430 (TC), [2018] UKFTT 430 (TC) and *Gilbert v HMRC* UKFTT 437 (TC).

Facts of the cases

In the *Smith* cases, the NRCGT returns for Mr and Mrs Smith were due on 27 June 2015. However, the returns were not filed until 29 January 2017. Judging by these dates, I assume that the couple’s ordinary tax returns for 2015/16 were filed on time and this alerted HMRC to the fact that NRCGT returns should also have been filed (or, perhaps, the completion of their Self Assessment returns alerted Mr and Mrs Smith to their earlier oversight).

In *Gilbert*, the NRCGT return was due on 26 November 2016 but was not submitted, however, until 23 June 2017.

The Tribunal’s decisions

The *Smith* cases were decided by Judge Tony Beare. *Gilbert* was decided by Judge Charles Hellier.

The sticking point in all of these cases is the relevance (or even accuracy) of the maxim 'ignorance is no excuse'. I remember, when discussing with friends the *Barrett* case (see 'Steptoe & so on' in the November 2015 issue of *Tax Adviser*), that maxim was the standard reply which I faced. If I might use a further maxim of my own choosing, a little knowledge is a dangerous thing. Indeed, as has since been confirmed most recently in *Perrin v HMRC* [2018] UKUT 0156 (TCC)), ignorance of a filing obligation can fall within the scope of a reasonable excuse.

Reflecting the decision in *Perrin*, a distinction was made in *Smith* between those obligations that a taxpayer might be expected to be aware of and those which are more obscure. The Tribunal considered that the taxpayer had behaved reasonably: 'This is, first, because there was no reason for the Appellant to have suspected that, in addition to reporting the disposal in his/her normal self-assessment return in respect of the relevant tax year of assessment, s/he would also need to make another, separate and self-standing, tax return in relation to the disposal. And, therefore, there was no reason why the Appellant should have gone onto the Respondents' website to look for the existence of any such additional filing obligation. Moreover, there was no reason why the Appellant should have sought the advice of a tax expert in relation to the disposal, given that it was obvious to him/her from the numbers involved that the disposal had not given rise to a chargeable gain and so s/he would be able to deal with the disposal perfectly adequately in his/her self-assessment return without recourse to expert advice. For those two reasons, I believe that a hypothetical responsible person, who was cognizant of his obligations in relation to tax and intended to comply with those obligations, might very well have acted in the same way as the Appellant.'

The Tribunal allowed Mr and Mrs Smith's appeals.

In *Gilbert*, the Tribunal also considered the Upper Tribunal's decision in *Perrin* and agreed that Mr Gilbert had not been obliged to keep up to date as to the law. Nevertheless, when responding to the taxpayer's argument that, as someone who had been non-resident for fifteen years, he could not have known about the change in the law, the Judge responded as follows: 'There was no evidence that Mr Gilbert had made any attempt to discover whether there had been any changes in the law. That is not to suggest that a reasonable taxpayer who gave reasonable priority to tax compliance in his position would have made daily enquiries, but they would have made some. Holding property in a jurisdiction exposes the owner to the rules of that jurisdiction, and I consider that the hypothetical reasonable taxpayer would have attempted some enquiries.'

Despite Mr Gilbert's disposal giving rise to a capital loss (therefore coming within the second reason given to support Judge Beare's decision in *Smith*) Judge Hellier duly dismissed Mr Gilbert's appeal.

Commentary

My understanding of many of these cases is that the filing obligation only became clear during the preparation of a subsequent Self Assessment tax return or even after HMRC had processed the taxpayer's return. In those cases, submitting NRCGT return is largely a paper-filling exercise rather than fulfilling any particular need on HMRC's part. (Indeed, I have seen one HMRC solicitor argue in the context of P14s that forms should sometimes be sent to HMRC not so that HMRC can use the information but simply because there is a statutory requirement to do so.)

Personally, I find HMRC's stock response 'the information was on our website' to have been spectacularly unhelpful. It is, in my view, equivalent to being told that a particular pin was in a haystack, several years after the event, when at the relevant time one did not know that there was even a pin that needed to be found.

When I worked for the former Inland Revenue (admittedly not in a taxpayer-facing role) I remember that the Department was supposed to be ‘enabling’, helping taxpayers to comply with their duties. Increasingly, I find that decisions and processes are carried out by officers who have become experts in a particular area of policy (in this case, the NRCGT obligations) without recognising that others might not have that particular policy or process at the forefront of their mind. Thus, it is all very well to someone who already knows about NRCGT to be expected to check on the HMRC website, but any information posted there is hardly going to be prominently visible to the average non-resident taxpayer. This is evidenced by the considerable numbers who have found themselves liable to penalties.

It is also unsatisfactory that the Smith family were potentially subject to double penalties in relation to what was ultimately the same transaction, simply because they both had an interest in the property and were therefore both liable to make NRCGT returns.

Although perhaps not an intentional part of the legislation, it does seem that the real beneficiary of the new rules has been the Exchequer, not so much in relation to the additional tax payable as a result of the wider tax net, but the penalty windfall that the rules have generated. I would really like to think that this was not a ‘deliberate design fault’ (although HMRC’s expressed policy objective of maximising revenues does perhaps suggest it was). However, giving them the benefit of the doubt, many lessons can and should be learned from this episode whenever there is a similar change of policy that brings a new taxing obligation to an entirely new set of taxpayers. For example, in this instance, hindsight suggests that HMRC should have made the filing obligations very clear to property conveyancers (through representative organisations such as the Law Society).

Indeed, Mr Gilbert’s mistake might not have been his failure to check up for any changes in the law but to alert the Tribunal to the fact that he had paid for a suitable professional to undertake the conveyance of his UK property. Given that such a professional should have been aware of the obligation to file a NRCGT return, Mr Gilbert would have therefore taken the reasonable steps to ensure that his UK legal duties were being carried out. Indeed, it was on this basis (in the context of the Construction Industry Scheme) that Mr Barrett won his appeal.

What to do next

What is perhaps the least satisfactory aspect of these rules is the fact that the First-tier Tribunal is being divided into two camps of judges – those who consider that a reasonable excuse exists in such cases and those who do not. Of course, First-tier decisions are not binding and perhaps one should be reassured by the fact that the judiciary is demonstrating its independence and not simply playing follow the leader. On the other hand, as is evident from other cases, the judiciary is itself acutely aware that the interests of justice favour a more harmonious approach across the Tribunal. Indeed, it is not satisfactory that the outcome of a taxpayer’s appeal in these cases is (seemingly) more dependent on the identity of the judge to whom the case is allocated than the actual facts of the case.

If you have a client who faces a NRCGT penalty, you should strongly consider appealing against it in a suitable case. In the meantime, it is worth hoping that a case will proceed to the Upper Tribunal in the hope that this will lead to some clarification of the position. This is in fact an ideal case for HMRC to make it clear that they will not seek costs in the Upper Tribunal even if they succeed on any such appeal.