**Penalty Appeals**

Taxation Article: 18 October 2017, Andrew Hubbard

**Why is it so difficult for taxpayers to win penalty appeals before the tribunal?**

Research by Tolley has emphasised just how difficult it is for taxpayers to successfully challenge penalties imposed by HMRC. In a sample of the last 50 reported appeals to the First-tier Tribunal in income and corporation tax cases, the taxpayer was successful in only seven with HMRC winning 35. The remaining eight had a split outcome: the taxpayer still had to pay a penalty but managed to get the amount reduced. The figures for appeals against VAT penalties are remarkably similar: six wins for the taxpayer, with 36 for HMRC and 8 split decisions.

Why is this? Shouldn’t the balance be more like 50/50? After all, the tribunal is a neutral arbitrator. What these figures point to is the very narrow scope for challenging penalties for failures to submit returns or pay tax on time. The law does allow an escape clause where there is a ‘reasonable excuse’ but, as these figures clearly show, the tribunals interpret this in a very narrow way and many people who feel that they have been hard done by find to their cost that the tribunals take a hard line and confirm the penalty.

Penalties are a major part of the work of the tax tribunals. Since 2009, when the current system started to replace the old system of separate appeal routes for income tax and VAT, there have been something like 4,500 reported decisions. Of those, about 1,500 – a third – have involved penalties (this probably underestimates the number as the data is not recorded consistently and there are almost certainly penalty aspects of cases reported in other categories). So, if the 100 most recent cases are typical (and there is no reason to suppose they are not) and only 13% of cases are decided wholly in favour of the taxpayer, that does suggest that huge amounts of the tribunal’s resources are being taken up in dealing with cases where the taxpayer has no realistic chance of success.

 Is this a problem? We think that it is. Appeal rights are important, but if the reality is that most appeals will have no realistic chance of success there comes a point where the reality is that the appeal right is no more than an illusion. We don’t think that we are quite there yet, but the danger is clear. HMRC are looking at how penalties will work in the digital area: let’s hope that proper consideration is given to giving taxpayers appeal rights which have real substance.

**Julian Stafford commentary:**

*• The review process before matters get to Tribunal will take out the more obvious cases and I believe that some of the more meritorious cases will be accepted by HMRC so never get to Tribunal.*

*• HMRC will only take cases that they feel they have a good chance of winning so any where they feel in doubt will be dealt with in some other way;*

*• A few might end up being dealt with by Mediation (though not fixed penalties with only reasonable excuse as the ground of appeal);*

*• Lack of representation by the taxpayer who is severely hampered by not being aware of the arguments which might work/won’t work and by not knowing what evidence to bring along to the Tribunal;*

*• Poor quality representation (sadly quite common) particularly where the taxpayer’s accountant turns up;*

*• HMRC are (generally) much better prepared than they were in the past and will usually have all their ducks in a row before the hearing commences (Statement of case, Bundle of Authorities, summary of correspondence etc);*

*• Inherently low chance of success, usually accompanied by an erroneous view of the powers of the Tribunal (i.e. they think we can do what we want regardless of our limited jurisdiction, the constraints of the law and precedent);*

*• A desire by taxpayers to “be heard” even if they know they are unlikely to succeed;*

*• Asking for cases to be heard “on the papers” rather than at an oral hearing. This is linked to the lack of evidence point above. At least at an oral hearing, the Tribunal can be slightly inquisitorial to tease out information that HMRC might not have previously been aware of. HMRC are notoriously uninquisitive once they have decided to pursue a case and rarely engage with the taxpayer in any sort of dialogue to find out what’s going on below the surface. Basically paper cases have an extremely poor chance of success in my view.*

*i think the article would only be right if every single dispute automatically went to Tribunal with no internal review or other intervening process. Then you might expect something nearer to 50/50. To suggest that there is something wrong with the system is incorrect for the reasons set out above. Indeed, although the tribunals have to apply the law fairly and even-handedly, I think it is true to say that most are very sympathetic to the realities and hardships of everyday life and the reasons why taxpayers might have “under-performed”.*

*I also don’t think that reasonable excuse is interpreted narrowly though it is true that “reasonable" does not carry its common sense meaning. HMRC seem to think it means “cast-iron” or “copper-bottomed” which is not the case and, within reason and bearing in mind the statutory exceptions, Tribunals can take a fairly broad view of the facts. The reality is of course that some judges are more sympathetic than others.*

*The main reason people feel hard done by is because they don’t understand the law and the limited jurisdiction of the Tribunals. This is particularly obvious when looking at Customs seizures where taxpayers who fail to take proceedings in the Magistrates Court are estopped from disputing the underlying facts when they get to the Tax Tribunal. There, they can only appeal on the grounds that the Border Force decision not to restore the goods/vehicle was “unreasonable” in a Judicial Review sense.*

*Where I think the article is correct is that a significant waste of resources occurs dealing with cases where there is no realistic prospect of success. This could be best dealt with by widening the “mediation” element prior to Tribunal hearings so that an independent person can tell the taxpayer what they would need to establish to succeed, why on an initial review the situation looks fairly terminal and that it doesn’t matter if it’s only a day late!*

*I also agree that there is a problem but it’s not really a problem with the system or the interpretation of reasonable excuse. It’s the other factors (above) which tip the scales. Without wanting to blow my own trumpet, I think that our Irish client who recently got off at Tribunal would have had no prospect of success whatsoever if he had turned up on his own or with his accountant. I think the biggest single factor in the apparent inequality of results is the quality of representation the taxpayer has (or usually doesn’t have).*

**Barry Whiffin commentary**

*However, should we be a little wary of drawing the conclusion reached in this article. It might be wothwhile, if it were indeed possible, to look at the overall outcome starting from penalty reviews and also to consider what proportion are appeals based on justification by evidence other than administrative error.*

*It may be, and I accept this might be wishful thinking, that HMRC are getting better at reviewing penalties and are seriously considering the possibility of their success, and the consequence is that many penalties are cancelled before the formal appeal stage is reached.*

*My point is that such conclusions as reached in the article may give the impression that objections to penalties are hardly worthwhile, when it may be that HMRC are just getting better at which cases to resist to the formal stage as a consequence of, a few years ago, the Tribunal becoming very critical of HMRC’s attitude.*