TC01388

Appeal number: SC/3071/2009

Expenses; Special Commissioners (Jurisdiction and Procedure) Regulations, 1994 (SI 1994/1811) Regulation 21(1); Transfer of Tribunal Functions and Revenue and Customs and Appeals Order 2009 (SI 2009/56), Schedule 3 paragraph 7(7).

FIRST-TIER TRIBUNAL

TAX

WESTERN FERRIES (CLYDE) LIMITED **Appellant**

- and -

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

TRIBUNAL JUDGE: **J. GORDON REID Q.C., F.C.I.Arb.**

Heard on Papers Only in George House, 126 George Street, Edinburgh, August 2011

DECISION ON EXPENSES

Introduction

1. This appeal related to Tonnage Tax, introduced by Schedule 22 to the Finance 2000 to revive the British Shipping Industry. Under the tonnage tax regime, qualifying companies do not pay corporation tax based on their shipping profits, but by reference to the tonnage of the qualifying ships operated. The broad issue was whether the Appellant's ships were qualifying ships within the meaning of the legislation during the relevant fiscal period. These ships plied their trade principally between McInroy's Point near Gourock and Hunter's Quay near Dunoon.

2. There were three underlying issues about which the Tribunal heard evidence and submissions at the Hearing which took place over six days between 22-26 November 2010 and 18 January 2011, namely whether (i) the Appellant's ships were duly certified for navigation at sea, (ii) the crossing was an estuary crossing and (iii) the crossing was within a harbour. These issues reflected critical parts of the legislation around which the Hearing was focused.

3. Part of the dispute concerned an issue about the applicable safety management systems. The Appellant had to have the appropriate safety management certificate. The two systems in issue were the Domestic (DSM) and the International (ISM). In paragraph 67 of the Tribunal's Decision it is recorded that in the course of submissions the Revenue conceded that the Appellant had the appropriate certificate (DSM).

4. For present purposes, the only significant step in the procedure leading up to the Hearing in November 2010 was an application by the Revenue on or about 4 March 2010, heard by the Chairman on 29 April 2010, to amend its Statement of Case by adding the third issue mentioned above. That application was granted by paragraph 2 of the ensuing Directions, dated 28 June 2010. The Tribunal refers to paragraphs 8-23 and 26-28 of the Note accompanying those Directions.

5. In the Tribunal's Decision dated 12 April 2011 the appeal was dismissed. While the Tribunal found in favour of the Appellant in relation to the second and third issues, it found in favour of the Revenue on the first issue. The appeal therefore fell to be dismissed. The Tribunal's Decision is referred to for its findings in fact and law which are not repeated here.

The Application for Expenses

6. On or about 10 May 2011, the Appellant applied for an order that the Revenue pay the Appellant's expenses of and in relation to the Application heard on 29 April 2010 and *the preparation for and attendance at the hearing of the Appeal in November 2011 to address the "Harbour Crossing Issue" including specifically of obtaining statements from and attendance of witnesses Douglas Lindsay and James Cooper*. In compliance with Rule 10 of the Tribunal's Rules, the application was accompanied by a schedule of expenses. In relation to the April 2010 Application the

expenses claimed amount in total to £21,527.50. The charges consist primarily of junior counsel's fees for the Application Hearing, *documents and travel costs* in the sum of £15,751.50. The balance is for solicitors' fees including 14.7hrs work *done on documents and in preparation for hearing.* VAT is not included in these figures.

7. In relation to the Harbour Issue, the expenses claimed amount in total to £59,443.24. The charges consist primarily of senior counsel's fees, namely 30% Brief fee for the Hearing, documents and travel/accommodation costs, £24,018.00, and junior counsel's fee for the same items and on the same basis, £16,286.00. The balance is for solicitors' fees and expert witness fees of £5,328.74 (the expert's fees include VAT). VAT is not included in the other figures.

8. The total amount of expenses claimed is therefore £80,970.74 (£21,527.50+£59,443.24).

Procedure in relation to Application for expenses

9. The Tribunal gave parties the opportunity to proceed by way of written submissions or by oral hearing or by combination of both. After some vacillation, neither party requested an oral hearing, apparently preferring at least initially to provide written submissions. The Tribunal therefore issued Directions (on 21 June 2011) requiring the exchange of submissions but gave parties the opportunity thereafter to apply, by 26 July, for an oral hearing if they so wished. Neither party has applied for an oral hearing.

The Tribunal's Powers in relation to expenses

10. The new tax tribunal system and the Tribunal's Rules came into effect on 1 April 2009. The appeal commenced before that date. In relation to such proceedings Schedule 3 paragraph 7(7) of the Transfer of Tribunal Functions and Revenue and Customs and Appeals Order 2009 provides that an order for costs may only be made if and to the extent that an order could have been made before the commencement date on the assumption, in the case of costs actually incurred after that date, that they had been incurred before that date. This means that the old regime on expenses applies.

11. The old regime is to be found in the Special Commissioners (Jurisdiction and Procedure) Regulations 1994. Regulation 21(1) provides that a Tribunal may only make an order for expenses against a party if it is of opinion that the party has acted *wholly unreasonably in connection with the hearing in question.* That is the test the Tribunal applies. There is no dispute about this.

Submissions

12. The Appellant's submissions are contained in two documents (Submissions and a Reply) and a Schedule. The Appellant has also produced some correspondence and referred to a number of authorities discussed below.

13. The Appellant's main arguments consist of various criticisms of the successful attempt to introduce the *Harbour Issue* in April 2011. The reasons advanced by the Revenue at the hearing on 29 April 2011 are analysed by the Appellant and said to amount to the introduction at a very late stage, without any credible explanation of an unmeritorious point which is a misuse of the rules by the Revenue. The Revenue were also said to have disregarded the norms of conducting serious litigation. In their written submissions the Appellant cited authority which emphasises the exacting standard which the test requires to be met. In particular reference was made to *Carvillv Frost 2005 STC (SCD) 208, Gamble v Rowe 1998 STC 1247, Tower McCashback v HMRC 2011 2 WLR 1131 (Supreme Court) 2010 STC 809 (Court of Appeal), Macphail, Sheriff Court Practice 3rd edition paragraphs 10.19-10.29* and to *HMRC Litigation and Settlement Strategy*, published 23 July 2007.

14. The Appellant has also pointed out that the ISM Issue was conceded by the Revenue on the fourth day of the hearing. Finally, the Appellant referred to the evidence of one of the Revenue's witnesses (Mr Brown) and submitted that changes to his witness statements were facilitated by the late addition of the *Harbour Issue*.

15. The Revenue's submissions are contained in their letter dated 26 May 2011 and accompanying Note, and a further Note produced on 19 July 2011. In summary the Revenue argues that they were successful overall and were successful in their application to have the *Harbour Issue* added to the issues under appeal. They relied upon dicta in *Homeowners Friendly Society.* The Revenue's arguments on the *Harbour Issue* were stateable and the Tribunal did not say otherwise. The European dimension raised questions of public policy which the Revenue were entitled to raise; tonnage tax had not previously been the subject of judicial consideration. *Dicta* in *Tower McCashback* do not assist on the question of expenses. *Macphail* and the English CPR rules were of limited assistance. While acknowledging that the Revenue did change its position, it was pointed out that the Appellant led evidence about a third party's qualification for the tonnage tax regime, but ultimately did not rely on this line at all. The Revenue also made various submissions on the level of expenses claimed and submitted that if an award were to be made the account should be taxed by the Auditor of the Court of Session.

Discussion

16. The Application to introduce the *Harbour Issue* was opposed by the Appellant. That opposition required a hearing to take place. If the Appellant had agreed to the late introduction of the *Harbour Issue*, then it is unlikely that a hearing would have taken place on 29 April 2011. The Appellant's unsuccessful opposition caused the expense of that hearing to be incurred. It is therefore difficult to see on what basis the Appellant can be entitled to the expenses of and in relation to the application to amend the Revenue's Statement of Case. At that hearing the Appellant's position on expenses was extreme. The Appellant sought the expenses up to and including the Directions Hearing, and the expenses (not yet then incurred) up to the date of the substantive hearing. The Tribunal declined at that stage to grant such expenses for the reasons given in paragraphs 26 and 27 of the Note accompanying the Directions dated 28 June 2011.

17. It is noteworthy that, even now, there is no assertion that the Appellant was prejudiced or disadvantaged by the introduction of the *Harbour Issue* (see paragraphs 17 and 19 of the Note). The Tribunal does not, therefore, consider it appropriate to review the reasons advanced in April 2011 by the Revenue for the late introduction of the *Harbour Issue*. The main theme of that review of the history of the dispute is to show that the Revenue changed their position on several occasions.

18. However, if it is appropriate to review those reasons, an examination of the correspondence relied on by the Appellant reveals that the Revenue consistently maintained that whatever certification may have been issued by the Maritime and Coastguard Agency it was insufficient for the purposes of the tonnage tax regime (see generally paragraphs 82-83 of the Decision). ISM certification was an aspect of the certification issue. Ultimately, at the Hearing in November 2010, the Revenue recognised they were wrong on the ISM aspect or at least chose not to maintain that argument. The initial view emanating from MCA was that ISM was required (letter dated 18 May 2007). A subsequent letter from MCA (written by the same official) on 19 November 2007 indicates that the MCA's policy at the time was to require DSM certification for sea-going operation of the Appellant's ships. It is, however, clear that the certification process was complex and rendered even more complex by the introduction of EC safety regulations and their interpretation. Whether, ultimately, the question of ISM or DSM certification was a matter of policy or discretion or a question of interpretation and application of the relevant regulations did not have to be decided.

19. The *Harbour Issue* was raised at a meeting of the parties in June 2008. When the appeal first came before the Tribunal, however, the Revenue did not mention it as an issue. It was revived in April 2011 some six months before the substantive hearing. Ultimately, the Tribunal considered that, having heard the evidence and submissions, the Respondent's case on the *Harbour Issue* had no merit. The Tribunal did **not** intend to convey the view that the Revenue had somehow acted unreasonably far less wholly unreasonably in connection with any of the hearings before the Tribunal whether in April or November 2010 or January 2011.

20. This appeal has taken several years to reach a substantive hearing before the Tribunal. The reasons for that are unexplained. It is not surprising that during that period different views are expressed about the issues and the strengths and weaknesses of each party's arguments. As time passes, new lines of thought may emerge; arguments originally thought to be sound may be discarded, particularly where the facts are complicated and their analysis controversial. This was the first appeal on tonnage tax. Parties had to grapple with the complexities of the Merchant Shipping legislation, some undefined terms in the fiscal provisions and the interface between these two areas of law as well as technical expert evidence about estuaries and harbours. European Union legislation added a further dimension to the overall complexity.

21. To adopt the language of *Tower McCashback v HMRC 2011 2 WLR 1131 at paragraph 17,* the Appellant was not deprived of an opportunity fairly to marshal evidence as to the grounds subsequently advanced by the Revenue on appeal. Parties

frequently change their arguments. None of the Revenue's arguments was said to have ambushed the Appellant (*Tower McCashback at paragraph 18*) or unfairly prejudiced them.

22. The discussion of the exercise of case management powers in that case in the Supreme Court and the Court of Appeal raises quite different considerations from the question whether a party has acted wholly unreasonably in connection with the hearing in question. The Appellant's reference to what was said in *Tower McCashback* in the Court of Appeal (2010 STC 809 at paragraphs 39-41) do not assist the Tribunal. Allowing an additional argument on terms as to costs may be appropriate in some cases. It all depends on the circumstances. Here, the *Harbour Issue* was revived some six months before the hearing in November 2010. The Appellant had sufficient time to prepare. Its late introduction cannot be said to be wholly unreasonable; nor can the presentation of evidence and submissions in relation to it.

23. The Tribunal therefore does not consider that *dicta* on the meaning of *wholly unreasonably* in *Gamble v Rowe 1998 STC 1247* or *Carvill v Frost 2005 STC (SCD) 208* have been superseded by *Tower McCashback* or *HMRC Litigation and Settlement Strategy*. Plainly, *wholly* is a word of emphasis and shows that it will be unusual for actings to be classified as wholly unreasonable. In paragraph 20 of their written submissions, the Appellant correctly describes the conduct needed to justify an award of expenses under rule 21 as *exacting*. In the Tribunal's view, the Appellant has not pointed to anything which approaches that standard far less meets it.

24. *Carvill* was a somewhat extreme illustration of an award of costs. There, unlike here, the taxpayer was successful because the Revenue abandoned its opposition to the appeal several months before the hearing date. The Special Commissioners not only held the conduct of the Revenue to have been wholly unreasonable but found them liable on the (English) indemnity basis (see *Carvill v Frost No 2 2005 STC (SCD) 422*). The decision not to resist the appeal should have been taken almost four years earlier (paragraph 12). The Special Commissioners (who included Sir Stephen Oliver Q.C.) went on to point out under reference to *Gamble* that the *wholly unreasonable* test is high (paragraph 13). Nevertheless, the Revenue's conduct was held to be unreasonable to a sufficiently high degree to require the Commissioners to make the costs award on the indemnity basis (paragraph 14).

25. The detail of that conduct is to be found in the earlier report of the Decision on costs (*2005 STC (SCD) 208*). The Revenue made broad generalised allegations concerning the genuineness and commercial purpose of the Appellant's contractual arrangements which were in issue and greatly increased the scope of the factual matters which the Appellant had to prove. The Appellant's tax affairs had a complex history and there were numerous decisions over many years of dispute with the Revenue. It is in that context that the Special Commissioners observed that a thorough and objective review at a much earlier stage (paragraph 72) ought to have been undertaken. It is simply not appropriate to apply that *dictum* to the present appeal as the context is materially different.

26. *Gamble* emphasises that awards of expenses will be rare because an exacting standard has to be met. Park J, on appeal, declined to interfere with the exercise of the very experienced Special Commissioner's (economically expressed) discretion on costs (pages 1257-8).

27. In *Homeowners Friendly Society Ltd v Barrett (Inspector of Taxes) 1995 STC (SPD) 90*, the facts were not in dispute. The Special Commissioners had considerable difficulty in following the Inspector's submissions and rejected them. The Inspector had, in earlier correspondence, stated that he had little faith in his arguments. There, as here, was no authority on the point at issue. The Inspector's conduct came *very close to improper conduct.* Even then, the Special Commissioners declined to make an award of costs against him although they were of the view that it was reasonable to make the application for costs. The basis of the decision was that it was not wholly unreasonable for an appeal to be pursued on a technical point of law where there was no authority even if the Revenue had little faith in a successful outcome. The Special Commissioners also observed that questions of public policy also dictated that the Revenue should take a case to appeal in order to establish with certainty what exactly the law is.

28. In the Tribunal's view, however, there must come a point when it is no longer reasonable to pursue a technical point or to establish, as a matter of public policy, what any reasonable tax practitioner would consider the law to be. In the Tribunal's view, that point was not reached in the present appeal. The Tribunal does not agree that *Homeowners* was wrongly decided, as the Appellant has suggested, although the Tribunal does consider that the conduct of the Inspector might now be considered to have been on the wrong side of the line having regard to the terms of the letter appended to the decision. Even if it has been wrongly decided, the error must have been in the application of the law to the facts rather than the statement of legal principle being applied.

29. Insofar as relevant, the Tribunal does not consider that that HMRC Litigation and Settlement Strategy undermines the principles established in relation to a finding of expenses under the *wholly unreasonable* regime. Paragraph 18 of the Strategy, as currently set forth on the HMRC website provides *inter alia* as follows:-

> Where HMRC believes that it is unlikely to succeed in litigation it will, in the majority of cases, concede the issue. In such cases, HMRC will not attempt to 'split the difference' between its own and the customer's view of tax, interest and penalties (where appropriate) at stake. Taking a case to litigation where HMRC believes it is unlikely to succeed would need to be justified by the particular circumstances, such as a very large amount of tax at stake (in the case itself or from immediate precedent value where a large number of customers is affected), or a fundamental point of principle or behaviour at issue.

30. Even if that statement has some diluting effect on the exacting standard of the *wholly unreasonable* regime, the Tribunal does not consider that is enough to enable the Tribunal to make an award of expenses in favour of the Appellant. The appeal had to be fought to a conclusion. There appears to have been a substantial amount at stake. There was no precedent. In these circumstances, the Tribunal cannot condemn the Revenue for taking the *Harbour Issue* to a conclusion.

31. As for the European dimension (the argument that the European Commission might require the Revenue to claw back sums received by the Appellant), the Tribunal, in its Directions dated 28 June 2010, said this at paragraph 21:-

> As for the European dimension raised by HMRC, I consider that, at this stage at least, it is a red herring. It is difficult to see how any decision or potential decision of the European Commission on questions of State Aid can have a bearing on whether the Harbour Issue should be included in this appeal.

32. At *that stage*, the Tribunal had difficulty in identifying the relevancy of the question of State Aid.The Tribunal discussed the State Aid cases in its Decision (paragraphs 171-177) and, with a greater appreciation of their import and effect and a greater understanding of the merits of the appeal, it took the view that they provided a degree of support for the approach to construction which the Revenue were advancing. The Tribunal therefore considers that the Appellant's reliance on paragraph 21 is misplaced. In any event, when a party raises what a tribunal or court considers to be a bad argument that does not necessarily mean that the conduct of the party advancing it should be condemned as wholly unreasonable. Arguments condemned at first instance and on appeal sometimes win the day in the House of Lords or the Supreme Court.

33. Amendment of pleadings in Scottish court procedure is not an entirely apt comparison. The general rule is that the amender pays the expenses of the amendment but that has no bearing on who pays for the expenses of the proof or that part of the proof which related to the amendment. There are many possibilities for the division of expenses. If the motion to amend is unopposed but subsequently answered then the expenses of the amendment procedure will normally be borne by the amender. If a motion to allow a minute of amendment to be received is unsuccessfully opposed then the party advancing that unsuccessful opposition may have to pay the expenses of that part of the amendment procedure. He is unlikely to be awarded all his expenses on the subject matter of the amendment. Unsuccessful opposition at the later stage of amendment of the pleadings would also not justify a full award of expenses. Thus, there is no support for the Appellant from Scottish procedure which would persuade the Tribunal to award them the expenses of unsuccessfully opposing the addition of the *Harbour Issue. CPR* rules have no application in Scotland, although no doubt, there are principles of practice and procedure which find similar expression in the rules of practice and procedure in the Scottish courts.

34. For the sake of completeness, the Tribunal records that the submissions relating to Mr Brown's evidence and the evidence of a third party's treatment under the tonnage tax regime have little bearing on the question whether the Revenue's conduct on any aspect of the appeal was wholly unreasonable. Mr Brown was led on the *Estuary Issue*. The Tribunal refers to paragraphs 213 and 190 of its Decision.

35. Finally, had the Tribunal decided to make an award of expenses in favour of the Appellant, it would have remitted the account to the Auditor of the Court of Session to tax. At that stage, the Revenue would be able to make the various points on quantum which they made in their written submissions.

Summary

36. **Both branches of the Appellant's application for expenses are refused.**

37. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

J. GORDON REID Q.C., F.C.I.Arb.
TRIBUNAL JUDGE

RELEASE DATE: 9 AUGUST 2011