



TC06103

Appeal number: TC/2016/02850

Penalty Income tax - FA 2007 Sch 24 - inaccuracy in tax return - Capital Gain not disclosed - whether inaccuracy was careless and prompted - yes - Sch 24 para 14 - whether penalty should have been suspended - no - Appeal dismissed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

STEPHEN MERRIE

Appellant

- and -

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

**TRIBUNAL JUDGE MICHAEL CONNELL
MEMBER DAVID MOORE**

**Sitting in public at Alexandra House 14 - 22 The Parsonage, Manchester, on 12
May 2017**

The Appellant in person

Ms Joanne Bartup, Officer of HMRC for the Respondents

DECISION

1. This is an appeal by Mr Stephen Merrie (“the Appellant”), against an HMRC decision made on 17 March 2016, to impose a penalty of £95,112.79 under Schedule 24 Finance Act 2007 (“Schedule 24”) in respect of an inaccuracy in his 2014-15 self-assessment income tax return.

2. The assessment of tax which gave rise to the penalty is not in dispute. The points at issue are:

- i. Whether the Appellant was careless in submitting the inaccurate tax return.
- ii. Whether the disclosure to HMRC was prompted.
- iii. Whether the amount of the penalty is excessive.
- iv. Whether the penalty can be suspended.

The factual background

3. The Appellant was the sole shareholder in Primary Fluid Holdings Ltd (‘PFH’) and its wholly-owned subsidiary Primary Fluid Power Ltd. PFH, based in Knowsley, Merseyside designed and manufactured hydraulic systems and purifiers, and distributed hydraulic components.

4. On 4 August 2014 the Appellant sold his entire shareholding to Flowtech Fluidpower Plc for a total consideration of £9,886,071. The Appellant had been with the business since 1987 and it was agreed that he would remain as Managing Director and join Flowtech’s operational Board.

5. The consideration for the share sale consisted of three elements as follows:

| | |
|---|-------------------|
| Cash of | £4,766,071 |
| Loan notes in the amount of | £1,620,000 |
| Shares in Flowtech Fluidpower PLC to the value of | <u>£3,500,000</u> |
| (subject to a 12 month lock in condition) | £9,886,071 |

6. Under the share sale agreement the Loan Notes were repayable in 2015-16.

7. After the deduction of £70,000 disposal costs, the total net consideration received for the shares by the Appellant was £9,816,071.

8. The Appellant was entitled to Entrepreneurs’ Relief on the sale of the shares. Entrepreneurs’ Relief reduces the amount of Capital Gains Tax on a disposal of ‘qualifying business assets’, provided the taxpayer has met the qualifying conditions throughout a one-year qualifying period either up to the date of disposal or the date the business ceased. Qualifying capital gains for each individual, for disposals on or after 6 April 2011, are subject to a lifetime limit of £10 million.

9. If entitled to Entrepreneurs’ Relief, qualifying gains will, for disposals made on or after 23 June 2010, be charged to Capital Gains Tax at the rate of 10%.

10. HMRC's guidance, HS275, states that Entrepreneurs' Relief must be claimed by the first anniversary of the 31 January following the end of the tax year in which the qualifying disposal takes place. Therefore, for a qualifying business disposal in the tax year 2014-15 as in the Appellant's disposal, a claim for Entrepreneurs' Relief must be made by 31 January 2017.

11. The Appellant's 2014-15 Self Assessment return which was received on 24 August 2015 did not include the gain from the sale of PFH as it should have done. The inaccuracy arose because the Appellant misunderstood the timeframe for declaring the gain. He understood that the gain could be returned on the whole of the consideration at a later date, when he sold the shares in Flowtech Fluidpower PLC. He therefore believed that the gain could be reported in the following tax year. The Appellant now accepts that the consideration he received for the share sale should have been treated as a gain in 2014-15.

12. On 26 September 2015, the Appellant suffered a stroke and was hospitalised for five weeks. On 21 December 2015, on the advice of his doctor, he took the decision to resign from Flowtech Fluidpower PLC.

13. An enquiry into the Appellant's 2014-15 return was opened on 28 January 2016.

14. HMRC explained that any cash paid on completion fell to be chargeable in the year of disposal. With regard to the loan notes totalling £1,620,000, when the proceeds of a sale are loaned by the vendor to the purchaser, the same principles apply as apply to cash received.

15. With regard to that part of the consideration paid in shares, the value of those consideration shares would fall to be treated, by virtue of s 127 Taxation of Chargeable Gains Act 1992, as the same asset as the shares disposed of. A disposal of the consideration shares is treated as a separate disposal and therefore the conditions for Entrepreneurs' Relief must be considered at the date of disposal. For relief to apply on the consideration shares at the date of disposal, throughout the period of one year immediately preceding the disposal the following conditions must be satisfied -

- The taxpayer must hold 5% of the ordinary share capital and have at least 5% of the voting rights.
- The company must be a trading company or holding company of a trading group.
- The taxpayer must be an officer or employee of the company or one or more companies that are members of the trading group.

16. Following his retirement in December 2015, on the basis of the information provided by the Appellant, he was not an employee of the company and therefore Entrepreneurs' relief would not be available.

17. It was explained that the Appellant could make an election under S169Q to disapply the application of s 127, in which event the share for share exchange is ignored and the value of the shares received is brought into the computation as consideration so that the £3.5 million value of the consideration shares would be brought into the computation and Entrepreneurs' Relief is then wholly allowable.

18. It was further explained to the Appellant that a penalty is chargeable under Schedule 24 if a tax return is found to be incorrect as a result of a careless error, deliberate error or deliberate and concealed error. The amount charged depends on:

- Telling (Disclosure of facts and information)
- Helping (with the enquiry)
- Giving (providing access to records)

19. The Appellant duly made an election under s 169Q TCGA 1992 which resulted in the shares in Flowtech Fluidpower PLC also being included as consideration in 2014-15.

20. In determining the penalty payable, HMRC treated the shares differently because the Appellant had a choice to either declare them in 2015, or when the shares were disposed of. He made a written election under s 169Q TCGA 1992 to disapply the application of s 127 to bring the value of the shares into the computation of the gain. His reason for doing this was so that the gain would be taxable at the Entrepreneurs' Relief rate of 10%. Had he not made this election, he would have had to meet the conditions at s 1691 TCGA 1992 on disposal as follows:

Throughout the period of a year immediately preceding the disposal -

- the company was the individual's "personal company";
- the company was a trading company or the holding company of a trading group;
- the individual was an officer or employee of the company or of one or more companies that are members of the group.

21. The Appellant had a choice as to when to declare the share element of the consideration. His 2014-15 return did not contain details of the shares, reflecting his decision not to make an election under s 169Q on the basis that he would meet the conditions of s 1691 because, having taken on the role of MD, he planned to remain with the company for a number of years. Clearly, at the point of completing his return, he understood the conditions contained in s 1691.

22. As a result of his ill health, the Appellant was forced to resign from the company. Paragraph 3(2) of Schedule 24 provides as follows:

(2) An inaccuracy in a document given by P to HMRC, which was neither careless nor deliberate [on P's part] when the document was given, is to be treated as careless if P -

- (a) discovered the inaccuracy at some later time, and
- (b) did not take reasonable steps to inform HMRC.

23. HMRC concluded that the Appellant discovered the inaccuracy 'at some later time', and 'did not take steps to inform HMRC' of the inaccuracy. HMRC further concluded that the inaccuracy occurred on the date the Appellant resigned, being the day he lost his entitlement to claim Entrepreneurs' Relief on the consideration shares. It was on that date that it ceased to be beneficial to delay returning the gain, but HMRC concluded that the Appellant

was within his rights to reinstate that benefit, albeit at a price of delivering an incorrect return under Paragraph 3(2) above.

24. He had a window of opportunity of approximately one month from the day he lost his entitlement to the day the enquiry was opened. During this period, his window was diminished by the holiday period and the likely lack of ability to engage an agent close to the 31 January Self-Assessment deadline. HMRC therefore considered his ill health, and the impact that had on his judgement and ability to notify HMRC of the inaccuracy. The window of opportunity was too small for HMRC to expect the Appellant to alert them to the inaccuracy, and on that basis accepted that the shares element was a mistake despite taking reasonable care and consequently did not charge a penalty in that aspect.

25. On 18 March 2016, a Closure Notice under s 28A TMA 1970 was issued showing additional tax due of £981,611.60 plus statutory interest under s 101 Finance Act 2009, amounting as at 29 February 2016 to £2,333 and a penalty of £95,112.79 under Schedule 24 in respect of the inaccuracy.

26. After discovering his error, the Appellant had made ten payments on account of £50,000 per day from 1 February 2016. Shortly after the closure notice he paid the further sum of £483,000 to bring his total payments on account to £983,000.

27. The Appellant appealed the penalty on 27 March 2016. He said that his understanding was that the gain should be declared on completion of the sale, in tax year 2015-16. He had originally purchased the company partly on a loan note which was never repaid in full, and therefore was not clear precisely how much he would receive on the sale. He also understood that the deferred repayment of the loan would mean that the tax would be due the year later, and the gain on the shares on the same basis due to a 12 month lock in agreement. He was aware that the final sum would be calculated on the sale of his shares and repayment of the loan note.

28. He said that his understanding of the tax treatment of his share sale was:

“...based on conversations with financial people and I did speak to the Inland Revenue prior to the sale to confirm the ER and also had some advice from my accountants prior and just after the sale. But I never used the advisors for personal advice as it seemed a simple 10% on the sale in two payments. I would have again used the tax office for my final calculations as I have done in the past.”

29. He agreed that it:

“seemed silly not to have professional advicebut the sale of the company and fees associatedled to a problem with my accountant and solicitor who tried to charge a fixed amount percentage of the sale proceeds and this led to change of advisors. I did not see an issue dealing with this myself. I accept I could have done this better. I am not sure why my understanding in hindsight seems wrong now.”

30. HMRC upheld their decision on review.

31. The Appellant appealed to the Tribunal on 24 May 2016. His Notice of Appeal states his grounds of appeal as follows.

- The imposition of the penalty based on behaviour

- The severity of the penalty of £95,112.79
- The decision not to suspend the penalty

Relevant legislation

5 Paragraph 1 of Schedule 24 Finance Act 2007 states in relevant part as follows:

- (1) A penalty is payable by a person (P) where-
- (a) P gives HMRC a document of a kind listed in the Table below, and
 - (b) Conditions 1 and 2 are satisfied.
- 10 (2) Condition 1 is that the document contains an inaccuracy which amounts to, or leads to-
- (a) an understatement of a liability to tax,
 - (b) a false or inflated statement of a loss, or
 - (c) a false or inflated claim to repayment of tax.
- 15 (3) Condition 2 is that the inaccuracy was careless (within the meaning of paragraph 3) or deliberate on P's part.
- (4) Where a document contains more than one inaccuracy, a penalty is payable for each inaccuracy.

| <i>Tax</i> | <i>Document</i> |
|---|---|
| Income tax or capital gains tax | Return under section 8 of TMA 1970 (personal return). |

20 Paragraph 3 of Schedule 24 provides for degrees of culpability as follows:

- (1) For the purposes of a penalty under paragraph 1, inaccuracy in a document given by P to HMRC is-
- (a) “careless” if the inaccuracy is due to failure by P to take reasonable care,
 - 25 (b) “deliberate but not concealed” if the inaccuracy is deliberate on P’s part but P does not make arrangements to conceal it, and
 - (c) “deliberate and concealed” if the inaccuracy is deliberate on P’s part and P makes arrangements to conceal it (for example, by submitting false evidence in support of an inaccurate figure).
- 30 (2) An inaccuracy in a document given by P to HMRC, which was neither careless nor deliberate on P’s part when the document was given, is to be treated as careless if P-
- (a) discovered the inaccuracy at some later time, and
 - (b) did not take reasonable steps to inform HMRC.

35 Paragraph 4 sets out the penalty payable under paragraph 1. Paragraph 4(1)(a) provides that the penalty, for careless action, is 30% of the potential lost revenue. For deliberate but not

concealed action, the penalty is 70% of the potential lost revenue, and for deliberate and concealed action, the penalty is 100% of the potential lost revenue.

Paragraph 5 defines “potential lost revenue” as “the additional amount due or payable in respect of tax as a result of correcting the inaccuracy or assessment”.

5 Paragraph 9 provides for reductions in the penalty for disclosure depending on whether it is prompted or unprompted.

Paragraph 10(1) provides that “Where a person who would otherwise be liable to a 30% penalty has made an unprompted disclosure, HMRC shall reduce the 30% penalty to a percentage (which may be 0%) which reflects the quality of the disclosure”. Paragraph 10(2)
10 provides that “Where a person who would otherwise be liable to a 30% penalty has made a prompted disclosure, HMRC shall reduce the 30% penalty to a percentage, not below 15%, which reflects the quality of the disclosure”.

Paragraph 11 further provides that HMRC may reduce the penalty under paragraph 1 “If they think it right because of special circumstances”.

15 Paragraph 14 also enables HMRC to suspend all or part of a penalty for a careless inaccuracy under paragraph 1, but (under paragraph 14(3)) “only if compliance with a condition of suspension would help P to avoid becoming liable to further penalties under paragraph 1 for careless inaccuracy”.

Under paragraph 15, a person may appeal against a decision of HMRC that a penalty is
20 payable (sub paragraph (1)), or as to the amount of a penalty payable, (subparagraph (2)) or a decision not to suspend a penalty payable, (subparagraph (3)) or a decision as to the conditions of suspension (subparagraph (4)).

Paragraph 17 deals with the powers of the Tribunal in any such appeal.

25 (1) On an appeal under paragraph 15(1) the appellate tribunal may affirm or cancel HMRC’s decision.

(2) On an appeal under paragraph 15(2) the appellate tribunal may

(a) affirm HMRC’s decision, or

(b) substitute for HMRC’s decision another decision that HMRC had power to make.

30 (3) If the appellate tribunal substitutes its decision for HMRC’s, the appellate tribunal may rely on paragraph 11

(a) to the same extent as HMRC (which may mean applying the same percentage reduction as HMRC to a different starting point), or

35 (b) to a different extent, but only if the appellate tribunal thinks that HMRC’s decision in respect of the application of paragraph 11 was flawed.

(4) On an appeal under paragraph 15(3)

(a) the appellate tribunal may order HMRC to suspend the penalty only if it thinks that HMRC’s decision not to suspend was flawed, and

(b) if the appellate tribunal orders HMRC to suspend the penalty

40 (i) P may appeal to the appellate tribunal against a provision of the notice of suspension, and

(ii) the appellate tribunal may order HMRC to amend the notice.

(5) On an appeal under paragraph 15(4) the appellate tribunal

(a) may affirm the conditions of suspension, or

(b) may vary the conditions of suspension, but only if the appellate tribunal thinks that HMRC's decision in respect of the conditions was flawed.

5 (6) In sub-paragraphs (3)(b), (4)(a) and (5)(b) flawed means flawed when considered in the light of the principles applicable in proceedings for judicial review.

(7) Paragraph 14 (see in particular paragraph 14(3)) is subject to the possibility of an order under this paragraph.

10 HMRC's Compliance Handbook ("Manual") provides guidance on its powers of suspension of penalties as follows:

CH 83130:

15 'In certain circumstances it will not be possible to set suspension conditions to avoid future penalties. This may be because of the nature of the tax that the penalties related to, or because of the capacity in which the person has incurred the penalties.'

CH 83150:

20 'Penalties will not be suspended where the circumstances mean that the inaccuracy is a one off. For instance an inaccuracy in an Inheritance Tax account for a deceased person...However, certain types of settlement may have a continuing requirement to make returns. This means that it may be possible to set suspension conditions.'

CH 83160:

25 'Penalties for inaccuracies that are not likely to recur, whether because of the nature of the tax or the nature of the understatement, are generally not suitable for suspension because it is not usually possible to set conditions that will avoid careless inaccuracies in the future, or during a period of suspension.'

HMRC's guidance on Entrepreneurs' Relief HS275 (205) states:

30 This Helpsheet provides information to help you decide if you're entitled to Entrepreneurs' Relief. It provides a guide to straightforward situations, but does not cover all cases. You can get help from your tax adviser. You can also consult the HM Revenue and Customs (HMRC) [Capital Gains Manual](#) which contains sections (CG63950 to CG64171) that explain the rules in more detail.

What is Entrepreneurs' Relief?

35 Entrepreneurs' Relief reduces the amount of Capital Gains Tax on a disposal of qualifying business assets on or after 6 April 2008, as long as you've met the qualifying conditions throughout a one-year qualifying period either up to the date of disposal or the date the business ceased. Qualifying capital gains for each individual are subject to a lifetime limit as follows:

- 40
- for disposals on or after 6 April 2008 to 5 April 2010, £1 million
 - for disposals on or after 6 April 2010 to 22 June 2010, £2 million
 - for disposals on or after 23 June 2010 to 5 April 2011, £5 million
 - for disposals on or after 6 April 2011, £10 million

Who can claim relief?

Entrepreneurs' Relief is available to individuals and some trustees of settlements, but it's not available to companies or personal representatives of deceased persons or in relation to a trust where the entire trust is a discretionary settlement. Please see below for more information on 'Qualifying conditions' for trustees of settlements.

Claims

Entrepreneurs' Relief must be claimed, either by the individual or, in the case of trustees of settlements, jointly by the trustees and the qualifying beneficiary. You must make a claim to HMRC in writing by the first anniversary of the 31 January following the end of the tax year in which the qualifying disposal takes place that is one year and 10 months from the end of the tax year in which the qualifying business disposal is made. For a qualifying business disposal in the tax year 2014 to 2015 (ending on 5 April 2015) a claim for Entrepreneurs' Relief must therefore be made by 31 January 2017. A claim to Entrepreneurs' Relief may be amended or revoked within the time limit for making a claim.

The Appellant's submissions

Reasonable care

32. The Appellant accepts that he made an error in establishing the correct tax year for declaring the capital gain on the sale of his business, but says that he displayed reasonable care by taking advice - which unfortunately proved to be incorrect.

33. He asserts that the careless error was due to his misunderstanding of information taken from his accountant and HMRC's HS275 guidance document. This information led him to believe that he did not have to pay tax on the capital gain until January 2017. He says:

'I sought professional tax advice from Wilson Henry Chartered accountants based in Liverpool, both prior to and at the time of the sale of business, but due to the final cost of the advice, I closed my relations with them and completed my tax 2014/15 return on my understanding of the ER claim date being January 2017 and [that therefore the net gain should be returned in my 2015/16 return]. I relied heavily on HMRC's HS 275.'

34. With regard to the imposition of the penalty, the Appellant says that he did not knowingly deliver an incorrect 2014-15 tax return or consider the error to be deliberate or deliberate and concealed.

35. The Appellant says that at the time of filing his return in August 2015, there was a dramatic downturn in the oil and gas business immediately causing him stress and anxiety which resulted in a heart condition. Shortly after that he suffered a stroke and was hospitalised. He says that it is clear in hindsight that at the time he completed his return his judgement and ability to collaborate the information he was erroneously relying upon was impaired.

Unprompted disclosure

36. The Appellant says that the disposal of his shareholding in PFH and his intended Entrepreneurs' Relief claim had taken place with the full knowledge of HMRC. He therefore asserts that the error should be considered as an unprompted disclosure. He says that he had spoken with HMRC regarding the treatment of the gain prior to completing the return. When he completed his return HMRC had full knowledge of the sale and approximate details of the

capital gain. Thus any enquiry could not have been ‘prompted’. The investigating officer agrees that he did not *knowingly* deliver an incorrect return or try and deliberately conceal any tax due.

5 37. HMRC display that they had prior knowledge of the share sale in a letter dated 28th January 2016 stating “Information available to HMRC suggests you disposed of your entire shareholding in Primary Fluid Holdings Limited”. He says that information was passed to HMRC during routine PAYE compliance meetings that took place with HMRC several months after the share sale, and that at around the same time he had discussions with HMRC regarding his eligibility for Entrepreneurs’ Relief. His accountants also had discussions with
10 HMRC prior to the share sale.

Disproportionate penalty

15 38. The Appellant accepts that the automatic penalty for careless behaviour is 15% to 30% of the Potential Lost Revenue and that HMRC has applied 15% being the lowest percentage. The investigating inspector reduced the penalty to the minimum on the basis that he “could not have been more helpful”. He therefore asserts that the amount of penalty, at £95,112.79, is too severe and disproportionate given the simple mistake he has made.

20 39. The Appellant acknowledges that HMRC has no discretion in calculating the penalty by applying the set percentage to the potential lost revenue, but asserts that this makes no allowance for the mitigating circumstances and takes no account that the error would have resulted in a corrected return and no lost revenue.

Suspension of penalty

25 40. The Appellant argues that the penalty should be suspended. He has maintained records and completed his own tax returns using advice and guidance from HMRC’s helpline and website. The error can be prevented from happening again if he uses a professional tax advisor to complete his returns.

HMRC’s submissions

30 41. Paragraph 1 Schedule 24 FA 2007 allows HMRC to charge a penalty when an ITSA return contains an inaccuracy which led to an understatement of liability to tax, and this inaccuracy was caused by the careless behaviour of the taxpayer.

42. Paragraph 3 Schedule 24 FA 2007 states that a person is careless “If the inaccuracy is due to failure by P to take reasonable care”.

43. The decision in *Dr David Atkinson v HMRC TC/2015/00534* at paragraph 17 refers to the test applied in *Collis* [2011] UKFTT 588 (TC) which was whether the taxpayer acted as a:

35 *‘...prudent and reasonable taxpayer in the position of the taxpayer in question would have acted’*

44. In *Atkinson*, at paragraph 20 Judge Mosedale states:

40 *‘In my view, a taxpayer does not act carefully if, being largely in ignorance of the applicable law, he simply ‘takes a view’ and claims the relief or expense without taking any steps to verify his entitlement to it.’*

45. HMRC believe that the loss of tax was as a result of careless behaviour. Although the transaction was unfamiliar to the Appellant, he did not obtain professional advice in respect of his personal tax return. The Appellant believed that the gain could be returned on the whole of the consideration at later date when he sold the shares in Flowtech Fluidpower PLC.

5 46. HMRC's Capital Gains summary notes (SA108), explain that the 'Capital Gains summary' pages of the ITSA return need to be completed if 'you sold or disposed of chargeable assets which were worth more than £44,000'. It also states:

10 *'These notes only explain the basic rules as they apply in simple cases. In more complex cases you may need to get professional advice. If you are in any doubt about your circumstances you should ask your tax advisor.'*

47. The reading of these notes should have alerted the Appellant to the fact that the gain was returnable in the 2014-15 tax year. HMRC therefore does not accept that the Appellant took reasonable care to establish when the gain had to be returned.

15 48. It is accepted that the loss of tax which arose in respect of the consideration received in the form of shares in Flowtech Fluidpower PLC was not as a result of careless behaviour. A penalty has not been charged on this part of the gain.

49. The total consideration amounted to £9,886,071. The consideration received not in the form of shares amounted to £6,386,071. This equates to 64.596% of the consideration. The penalty has therefore been charged on 64.596% of the gain, that is £634,085.33.

20 50. The disclosure has been treated as 'prompted'. This is defined by paragraph 9(2) Schedule 24 FA07 as follows.

(2) Disclosure—

25 (a) is "unprompted" if made at a time when the person making it has no reason to believe that HMRC have discovered or are about to discover the inaccuracy, [the supply of false information or withholding of information, or the under assessment], and

(b) otherwise, is "prompted".

51. The Appellant did not alert HMRC to the inaccuracy in the 2014-15 return prior to the enquiry into the return being opened on 28 January 2016.

30 52. The penalty has been charged at the 15% rate. This is the minimum rate for a prompted disclosure where there has been careless behaviour. (Paragraph 10 Schedule 24 FA07).

53. It was found in *HMRC v Hok* TC 2012/UKUT/363 TCC that:

'...it is plain that the First-tier Tribunal has no statutory power to discharge, or adjust, a penalty because of a perception that it is unfair.'

35 54. Paragraph 14 Schedule 24 FA 2007 allows HMRC to suspend all or part of a penalty for a careless inaccuracy. HMRC may suspend a penalty only if compliance with a condition of suspension would help the person avoid becoming liable to further penalties for a careless inaccuracy. HMRC does not consider that in this case there are any special circumstances which would allow a special reduction.

55. The Tribunal may only order HMRC to suspend a penalty if they find that HMRC's decision is flawed (Paragraph 17(4) Schedule 24 FA 2007) -

(4) On an appeal under paragraph 15(3) -

(a) the ... tribunal may order HMRC to suspend the penalty only if it thinks that HMRC's decision not to suspend was flawed, and

(b) if the ... tribunal orders HMRC to suspend the penalty -

(i) P may appeal against a provision of the notice of suspension, and

(ii) the ...tribunal may order HMRC to amend the notice.

(6) In sub-paragraphs (3)(b), (4)(a) and (5)(b), "flawed" means flawed when considered in the light of the principles applicable in proceedings for judicial review.

56. HMRC assert that the penalty is not flawed and the inaccuracy in the Appellant's Self Assessment Return arose from a straightforward error. HMRC have not identified any underlying systemic failure or weakness in record keeping that could be corrected by a specific suspension condition.

57. The Decision in *Eric Eastman v HMRC* TC/05276 at paragraph 31 states:

'But in exercising that discretion HMRC must not only act within the framework of the legislation but must act reasonably in reaching their decision. The jurisdiction of the Tribunal is to review the exercise of that discretion according to the judicial review principles we have outlined above.'

Conclusion

Reasonable care

58. A penalty is chargeable if an individual delivers an incorrect self-assessment return as a result of a careless, deliberate or deliberate and concealed error. The penalty charge is a percentage of the additional amount of tax payable following correction of the inaccuracy. The Potential Lost Revenue in this case was the additional tax due of £981,608.53.

59. An individual is able to show that an error occurred despite taking reasonable care if he took reasonably prudent steps to avoid making an error, and where necessary clarifying the treatment of any unfamiliar transactions by checking this with HMRC or his professional advisors. If such steps are not taken, the error will be said to have occurred because reasonable care was not taken. There is no suggestion here that a deliberate error occurred. The Appellant did not knowingly submit an inaccurate return. However, his error was careless. The Appellant's tax return included a signed declaration to say it was, to the best of his knowledge, complete and correct.

60. The Appellant says he checked his eligibility to claim Entrepreneurs' Relief with HMRC and third parties. He refers to these third parties as financial people, but has provided no evidence to identify those individuals and show that they could be considered to be appropriately qualified professionals. Further, the advice obtained from third parties is not documented and does not appear to have been given in a professional capacity.

61. The steps taken by the Appellant to ascertain his eligibility to Entrepreneurs' Relief did not include establishing the fundamental point, that is, in which tax year the gain should be declared. He assumed the gain would be chargeable in the year the loan was to be repaid and the shares disposed of. This assumption was not made after seeking expert advice. He acknowledges that he could have taken additional steps to establish the correct year and agrees that speaking with HMRC, a suitably qualified advisor or reading more carefully HMRC's guidance notes would have alerted him to his erroneous understanding of the relevant legislation.

62. The Share Sale Agreement was a lengthy complex document. Clearly this was an unfamiliar transaction where the Appellant would not have known, without professional advice how and when the consideration monies would be taxable and precisely how the application of Entrepreneurs' Relief would operate. He did not seek to check this with HMRC or a professional advisor.

63. Although the Appellant may have spoken to HMRC when checking his entitlement to Entrepreneurs' Relief, it is inherently improbable that the advice he received was not to declare the cash and loan elements of the share sale in the year of disposal.

Disclosure

64. There are two forms of disclosure, prompted and unprompted. An unprompted disclosure is made at a time when the person making it has no reason to believe HMRC have discovered or are about to discover the inaccuracy. Otherwise it is prompted. The Appellant did not alert HMRC to the inaccuracies in his returns before the HMRC discovered the inaccuracy and for that reason his disclosure must be regarded as prompted.

65. The Appellant refers to a PAYE inspection carried out by HMRC in August 2015 when he says the share sale was discussed. However the Appellant was not present at that meeting and on that basis, any comments made by his associates would not be considered a 'disclosure'.

Mitigation

66. The penalty range for a careless error is 15% - 30% of the Potential Lost Revenue for a prompted disclosure. The penalty can be reduced from the maximum 30% to the minimum 15% on account of the quality of disclosure. The investigating officer considered that 'the Appellant could not have been more helpful' and therefore reduced the penalty to the minimum 15%.

Suspension

67. Careless penalties are capable of being suspended to encourage and support future compliance by giving the individual an incentive to improve their systems to avoid careless penalties in the future. A penalty can only be suspended where specific conditions can be set which will improve a process or record keeping to prevent future inaccuracies. Conversely, a penalty cannot be suspended where it is not possible to set specific conditions because the same type of error is unlikely to happen in the future.

68. The Appellant proposes that he appoints an agent or other professional agent to submit his future tax returns and that this would be an acceptable suspension condition.

69. As HMRC assert, the error did not occur as a result of a system error. The inaccuracy arose because the Appellant misunderstood the timeframe for declaring the capital gain. This was a straightforward error that was not caused by a systemic problem. HMRC properly concluded that they could not identify a measurable condition i.e. a change to a system or process that could be implemented to prevent a repeat of the error re-occurring in the future. There was very little likelihood of a similar type of inaccuracy occurring again, As HMRC concluded, the Appellant may at some time hold and dispose of shares which could give rise to capital gains, but it is highly improbable that there would be any involving loan notes, shares as consideration and Entrepreneurs' Relief.

70. For the above reasons we dismiss the appeal and confirm the penalty of £95,112.79. We concur with HMRC that the penalty should not be suspended.

71. This document contains full findings of fact and reasons for the decision. 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.

MICHAEL CONNELL
TRIBUNAL JUDGE

RELEASE DATE: 11 SEPTEMBER 2017