



TC07227

Appeal number: TC/2014/06065

COSTS - unreasonable conduct – unparticularised and unsupported allegations of fraud by HMRC in Statement of Case - late withdrawal by HMRC - application allowed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

FIRST CHOICE RECRUITMENT LIMITED

Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S

Respondents

REVENUE & CUSTOMS

TRIBUNAL: JUDGE ALEKSANDER

Application for costs determined on 20 June 2019 on written submissions only

DECISION

1. This decision relates to an application for costs made by the First Choice under Rule 10(1)(b) of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (“Procedure Rules”) on the grounds that party or their representative has acted unreasonably in bringing, defending or conducting the proceedings.
2. This decision has been made “on the papers”, having read First Choice’s application dated 25 September 2018, HMRC’s objection dated 9 April 2019, First Choice’s reply dated 17 April 2019, and HMRC’s letter dated 23 April 2019.
3. References in this decision to a “Rule” are to a Rule of the Procedure Rules, unless otherwise stated.

Background

4. The appeal concerned HMRC’s refusal to direct that First Choice was not liable to pay deductions which (in HMRC’s view) should have been paid under the Construction Industry Scheme. The issues in the appeal were whether First Choice took reasonable care to verify the “gross payment status” of a subcontractor, and whether First Choice’s view that the subcontractor had “gross payment status” was due to an error made in good faith.
5. HMRC’s statement of case was filed on 9 December 2016. The Statement of Case made allegations of fraud, and (in particular):
 32. HMRC contend that the directors of [First Choice], Louise Smith and Martin Campbell were knowing participants in the [name] payroll fraud.
 33. Emails between Martin Campbell, Louise Smith, Victor Shearer and Christopher Azzopardi suggest that [First Choice] were aware of the fraud taking place.
6. HMRC’s documents eventually exchanged with the Appellant contained no emails relating to Louise Smith or Martin Campbell. The only emails contained in HMRC’s evidence confirmed that the Appellant was not aware that the relevant subcontractor did not have gross payment status.
7. The Appeal was set down for a hearing on 20 August 2018, and on 6 August 2018, in accordance with the Tribunal’s directions, First Choice served its skeleton argument. The skeleton raised the following points:
 - (1) That an allegation of fraud has the effect of shifting the burden of proof onto HMRC;
 - (2) HMRC’s pleadings and particulars were inadequate in relation to the allegation of fraud; and

- (3) HMRC's evidence was insufficient to discharge the burden of proof which now rested upon them.
8. On 16 August 2018, HMRC withdrew from the Appeal.
 9. On 25 September 2018, First Choice made an application for costs under Rule 10(1)(b), and applied (if required - as to which see below) for permission to make the appeal out of time, and for dispensation from the requirement to serve a costs schedule under Rule 10(3)(b).

Late Application

10. Initially, First Choice had appointed Francis Clark LLP to act as its representative in the appeal.
11. On 7 August 2018, First Choice sent an email to the Tribunal opposing an application by HMRC that the hearing date be adjourned. The email included a postscript after the sender's signature stating "NB: Francis Clark are no longer acting on behalf of First Choice Recruitment and all future correspondence should be sent directly to the Company." Unfortunately, this postscript was missed by the Tribunal clerk dealing with the correspondence, and the Tribunal's database was not updated. As a result, correspondence from the Tribunal to First Choice continued to be sent to Francis Clark LLP. In November 2018 emails from the Tribunal to Francis Clark LLP were "bounced" and in consequence the Tribunal wrote to First Choice to obtain confirmation as to whether Francis Clark LLP continued to act for First Choice. First Choice confirmed by email on 3 December 2018 that Francis Clark LLP were no longer representing them, and following that email, the Tribunal's database was updated.
12. Because of this error, the Tribunal's letter notifying First Choice of HMRC's withdrawal was sent to Francis Clark LLP, and not to First Choice. Because First Choice had not received any communications since 10 August, they wrote to Francis Clark LLP on 17 September 2018 to enquire about the appeal. Francis Clark LLP replied to First Choice on 19 September 2018 to tell them that HMRC had withdrawn their appeal - Francis Clark LLP had emailed First Choice to tell them this on 17 August, but the email had been sent to an old email address, and the email had bounced.
13. The net effect was that it was only on 19 September 2018 that First Choice became aware that the Tribunal had notified the withdrawal by HMRC.
14. First Choice submit that their application for costs is not out of time because the Tribunal had not served a decision notice on either the Appellant or their properly appointed representative (the appointment of Francis Clark LLP having been terminated by notice on 7 August 2018). Alternatively, they submit that these circumstances provide a reasonable explanation for the delay in filing the application.

15. On 12 March 2019, the Tribunal wrote to the parties notifying them that the costs application be admitted out of time, and that HMRC have 28 days to file their representations.

Failure to include a costs schedule

16. First Choice's application for costs included an application to dispense with the requirement in Rule 10(3)(b) for a costs schedule. This was on the basis that the costs involved are in excess of £22,000, and it was not expected that a summary assessment would be appropriate. First Choice refers to the decision of this Tribunal in *Warren v HMRC* [2017] UKFTT 521 (TC) where such a decision was made.
17. HMRC object to such a dispensation, and referred us to an unpublished decision of Warren J and Judge Hellier in the Upper Tribunal in appeals concerning BMW(UK) Holdings and MG Rover Group, Lloyds Banking Group and Blackhorse, and Standard Chartered and Standard Chartered Bank released on 11 April 2017 (UT/2014/0027, UT/2014/0063, UT/2014/0029 and UT/2015/0038)(the "*BMW(UK)* case"). As the decision has not been published, I set out the Upper Tribunal's reasons in some detail. The decision relates (*inter alia*) to an application for costs made by HMRC following a successful appeal in the Upper Tribunal. Rule 10(1)(a) of the Tribunal Procedure (Upper Tribunal) Rules 2008 gives the Upper Tribunal wide discretion to award costs in appeals from or transferred by the Tax Chamber of the First Tier Tribunal. Rule 10(5)(b) of those Rules requires any application for costs to be accompanied by a schedule of the costs claimed sufficient to allow summary assessment by the Upper Tribunal. In their decision, the Upper Tribunal said:

[6] We do not consider that it is right as a general principle to dispense with a Rule 10 costs schedule, just because the Tribunal considers that a detailed assessment will be necessary. There are cases where a Tribunal might be assisted by a schedule even in cases where a detailed assessment is ordered. Our experience is that in some cases it is possible to decide that a detailed assessment is necessary only once consideration has been given to the schedule, albeit that this is usually so where the party claiming costs seeks a summary assessment and so will, of course, have submitted a schedule of costs.

[7] If it were only the Tribunal which is concerned with the Rule 10 schedule, we can see the force of Judge Berner's view that, where a detailed assessment is to take place, no Rule 10 schedule need be considered (and since it need not be considered, there is no point in delivering one in the first place). We do not think that this will always be correct. There may be cases where the Tribunal will be assisted by knowing the level of overall costs and its breakdown within the categories and amounts (with relevant charging rates) appropriate to a summary assessment. For instance, such information may assist the Tribunal in dealing with some points which would be better dealt with by it than by a costs judge, such as the percentage deduction in a case where it is appropriate to make an order under which the receiving party

receives only a proportion of its overall costs rather the costs of distinct issues.

[8] There may also be cases where it will assist the paying party to have a Rule 10 schedule. For instance, the ability to pitch a sensible offer in settlement (and thus avoid a detailed assessment) may depend upon the amount claimed (with the detail appropriate to a summary assessment) being made available; the Rule 10 schedule provides that information, especially where the expense of carrying out a detailed assessment would be significant.

[9] It is not, in any case, for an applicant for costs seeking only a detailed assessment unilaterally to decide not to provide a schedule. Rule 10 requires it to be provided; a dispensation from that requirement is required and that can only be given by the Tribunal. HMRC's application for costs is therefore defective in not being accompanied by a Rule 10 schedule. They have not applied for a waiver under Rule 7(2) but have simply stated that there is no need to deliver a Rule 10 schedule relying on *Eyedial* (FTC/89/2012 released on 2 December 2003).

[10] Although HMRC's application is defective, we do not consider that should disentitle them altogether from obtaining their costs. We are not, however, willing to waive the requirement altogether. Rather we require the failure to be remedied by the provision of a Rule 10 schedule. If [other parties] were to change its position in relation to the relevant appeals and accept that a Rule 10 schedule fulfilled no real purpose, we are willing to reconsider the decision not to waive the requirement altogether. Otherwise the Rule 10 schedule is to be provided within 21 days from the release of this Order and its Reasons.

18. HMRC submits that in the absence of permission from the Tribunal to dispense with a costs schedule, the application for costs is invalid, and should therefore be refused. HMRC submit that the Tribunal should not exercise its discretion to dispense with the requirement to provide a costs schedule under either Rule 5 or Rule 7(2) in the absence of any good reason given by First Choice. Without any schedule, HMRC is unable to comment on the amount claimed.

Unreasonable behaviour

19. This Tribunal has no general power to award costs. Such power as it has is found in section 29 of the TCEA and Rule 10. Section 29 of the TCEA provides that the FTT has power to determine by whom and to what extent costs of and incidental to proceedings shall be paid, but this power is subject to the Rules.

20. Rule 10 provides:

(1) The Tribunal may only make an award in respect of costs [...] –

[...]

(b) if the Tribunal considers that a party or their representative has acted unreasonably in bringing, defending or conducting the proceedings;

[...]

21. In its decision in *Tarafdar v HMRC* [2014] UKUT 362 (TCC) the Upper Tribunal set out the approach that should be taken where a party withdraws from an appeal. Paragraph [34] states as follows:
 - ... a tribunal faced with an application for costs on the basis of unreasonable conduct where a party has withdrawn from the appeal should pose itself the following questions:
 - (1) What was the reason for the withdrawal of that party from the appeal?
 - (2) Having regard to that reason, could that party have withdrawn at an earlier stage in the proceedings?
 - (3) Was it unreasonable for that party not to have withdrawn at an earlier stage?
22. HMRC say that they withdrew from the appeal in an effort to save time and costs. First Choice's skeleton argument brought to their attention the fact that the burden of proof had shifted to HMRC, and they came to the view that, given this shift, their prospects of successfully defending the appeal were poor.
23. HMRC submit that they could not have withdrawn at an earlier stage, as it was only after receipt of the skeleton that they became aware of First Choice's arguments in respect of this point. HMRC accept that a litigator with experience in matters of fraud may have foreseen such arguments (and acknowledge that HMRC have litigators with such experience - for example in dealing with MTICs). However, it is HMRC's established practice to allocate matters to caseworkers with experience and expertise commensurate with the complexity and issues of each case. Appeals relating to the construction industry sub-contractors scheme are usually straightforward, and are handled by caseworkers who are experienced in litigating such cases, but who have little experience in dealing with matters of fraud or MTIC appeals. In accordance with HMRC's usual practice, this appeal was allocated such a caseworker. HMRC submit that it was entirely reasonable for HMRC to make such an allocation, given that the issues under appeal did not concern fraud.
24. First Choice submits that there is no excuse for HMRC's litigators not to be aware that if they allege fraud, they will have to prove it. It would be an obvious and simple matter for HMRC to instruct its litigators not to allege fraud without seeking advice.
25. Paragraph 33 of HMRC's statement of case refers to various emails evidencing that First Choice's directors had knowledge of a fraud. First Choice submits that whoever drafted HMRC's statement of case would have had to have seen the emails before that allegation could have been pleaded. But in fact, there were no such emails, and the emails that were submitted by HMRC in evidence confirmed that First Choice was not aware of the fraud. First Choice submits that there was no credible evidence upon which the allegation of fraud could have been based (even if it had been pleaded properly) and it should not have been made. HMRC do not challenge any of these submissions in their objections.

26. First Choice submits that HMRC's behaviour was, therefore, unreasonable.
27. Further, First Choice submits that HMRC must have thought that their allegation of fraud could succeed only if they did not have to prove it. This is implicit in HMRC's submission that they withdrew their defence because their prospects of successfully defending the appeal were poor once the burden of proof had shifted. First Choice submits that no reasonable public authority could or would adopt that approach to alleging fraud (or, for that matter, anything else).
28. First Choice also notes that HMRC's only witness statement filed in support of their case was given by Mr McCrossan, "a criminal investigator for the last sixteen years" - and so the suggestion by HMRC that no one with knowledge of fraud had been involved in this appeal was untrue.

Discussion

29. I find that HMRC have been unreasonable in defending and conducting this appeal.
30. HMRC do not challenge the submissions made on behalf of First Choice that the allegations of fraud made in the statement of case were unsupported by evidence. HMRC admit that an appropriately qualified and experienced caseworker would never have made the allegations included in their statement of case.
31. I find that HMRC's conduct in alleging fraud in their Statement of Case, and particularising that fraud by reference to emails which are not produced in evidence, to be egregious. It is unacceptable for a public authority to make allegations of fraud where they have no credible evidence upon which to make even a prime facie case.
32. It is no excuse that the team dealing with the appeal had no experience of dealing with fraud. HMRC should have an appropriate system of supervision and training in place to ensure that their litigators deal with matters in an appropriate manner and in accordance with the law (including the laws of procedure and evidence).
33. If this matter was being managed by HMRC's solicitor's department, HMRC's actions might well amount to serious professional misconduct.
34. The Solicitors Regulation Authority's Code of Conduct requires that solicitors' firms have suitable systems in place for supervising matters, to include the regular checking of the quality of work by suitably competent and experienced people (O(7.8)).
35. The Code of Conduct makes express provisions in relation to the making of allegations of fraud, in particular Chapter 5 sets out the following indicative behaviours:

Acting in the following way(s) may tend to show that you have not achieved these outcomes and therefore not complied with the Principles:

IB(5.7) constructing facts supporting your client's case or drafting any documents relating to any proceedings containing:

(a) any contention which you do not consider to be properly arguable;
or

(b) any allegation of fraud, unless you are instructed to do so and you have material which you reasonably believe shows, on the face of it, a case of fraud;

IB(5.8) suggesting that any person is guilty of a crime, fraud or misconduct unless such allegations:

(a) go to a matter in issue which is material to your own client's case;
and

(b) appear to you to be supported by reasonable grounds;

36. The fact that HMRC alleged in their statement of case that directors of First Choice were parties to emails which suggest that they were aware of the fraud taking place, yet did not produce such emails in evidence, would indicate that there may have been a breach of IB(5.7)(b) and IB(5.8)(b).
37. I find it particularly worrying that HMRC submit that their conduct in this case was entirely reasonable - and therefore (implicitly) that they would not do anything differently in future. I agree with the submission made by First Choice that this raises the prospect that HMRC will continue to make unparticularised and unsupported allegations of fraud in cases before this Tribunal, and do not propose to take any steps to remedy their failings so that this does not recur.
38. HMRC should never have made the allegations of fraud contained in their statement of case. I therefore find that they have been unreasonable in defending and conducting the appeal from the outset.
39. As regards the schedule of costs, I dispense with the requirement for First Choice to produce one.
40. It is important to distinguish the award of costs in the First Tier Tribunal from the award of costs in the Upper Tribunal - and I note that the decisions in the *BMW(UK)* case relate to costs in the Upper Tribunal. In tax appeals before the Upper Tribunal, the Upper Tribunal has wide discretion to award costs, and the normal situation is that the successful party will be awarded its costs - applications for costs are routine. In these circumstances it is understandable why the Upper Tribunal would not want a general practice to develop of waiving any requirement to produce a costs schedule.
41. In contrast, in the First Tier Tribunal, applications for costs are rare. Costs can only be awarded in appeals allocated to the complex track (of which there are very few), or in cases where parties have behaved unreasonably, or in the case of wasted costs. Where it is clear that the amounts involved are likely to be substantial (as will be the case here) and the assessment of costs will be referred to the costs judges at the High Court, and there is no question as to how the costs will be allocated between the parties, it makes little sense for the applicant to

prepare a costs schedule. This falls within the circumstances set out in paragraph 10 of the Upper Tribunal's decision in the *BMW(UK)* case where a costs schedule will serve no real purpose.

42. I note that in this case First Choice did not neglect to include a costs schedule, but instead made an application to dispense with one. In consequence, I find that their application for costs was not invalid, notwithstanding the absence of a costs schedule. If their application to dispense with a costs schedule had been unsuccessful, they would have had to provide one. My directions as to costs set out below provides for assessment by a costs judge if the parties are unable to reach agreement. I have no doubt that First Choice will provide sufficient details to HMRC as to their costs in order to seek and reach agreement if at all possible.

Decision

43. I direct that:
- (1) The Respondents pay the Appellant's costs of and incidental to the appeal and of this application;
 - (2) Such costs to be the subject of a detailed assessment by a costs judge of the Senior Courts Costs Office on the standard basis if they cannot be agreed between the parties within 28 days of the date of release of this decision; and
 - (3) The Appellant is not required to produce a schedule of costs, and the provisions of Rule 10(3)(b) of the Tribunal's procedure rules are disapplied.
44. 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.

NICHOLAS ALEKSANDER
TRIBUNAL JUDGE
RELEASE DATE: 25 June 2019