

Making your excuses

Is HMRC's new manual on reasonable excuse a change in policy, or just another way for HMRC to deny your claim? Antony Greenwood explains all

Five months ago, HMRC updated its manuals on reasonable excuse, with the most notable update being the introduction of a manual dedicated to the question of whether someone can have a reasonable excuse for being ignorant of the law (CH160600).

This has long been a bone of contention between taxpayers, their agents and HMRC. Historically, the question arose predominantly in relation to a failure to notify HMRC of chargeability to tax, or a failure to file a tax return on time.

HMRC would often accept claims for reasonable excuse relating to health and matters outside of the taxpayer's control. However, where the taxpayer simply argued they were not aware of the compliance requirement, HMRC stood by the maxim 'ignorance is no excuse' and denied the appeal.

Reasonable excuse has become a far more crucial argument since the introduction of the Requirement to Correct legislation in relation to offshore matters. It is the only acceptable defence against draconian penalties and so advisers should be making more claims for reasonable excuse than ever before.

The requirement to correct and failure to correct penalties

By way of a refresher, since 30 September 2018 anyone who had not registered to make a disclosure of tax irregularities relating to offshore matters faces 'enhanced' penalties on unpaid tax arising from those irregularities for tax years including, and prior to, 2015/16, unless they have a reasonable excuse for failing to do so.

The minimum penalty for a failure to correct is 100% of the unpaid tax, and HMRC 'demands' (despite having no legislative basis for that demand) a 150% penalty in any case where it considers the disclosure to have been 'prompted'. That is, made in the expectation that HMRC is about to discover the error. As such, there is often far more to be gained from pursuing a reasonable excuse claim in cases involving a failure to correct than for 'ordinary' failures to notify or late filing.

Lack of knowledge

At Buzzacott, we have taken the view that anyone who was unaware of the requirement to correct (or to register to correct) by 30 September 2018 has a reasonable excuse for their failure to correct by that date. Given the (arguably) retrospective nature of the requirement, and the disregard for the usual behaviour criteria (failure to correct penalties make no distinction between someone who took reasonable care and someone who acted deliberately), this would seem perfectly logical. If someone is not aware they have made an error, how can they be expected to correct it and be penalised so heavily for failing to do so?

This argument is actually supported, but unfortunately not explicitly, by the requirement to correct legislation itself. In contrast to reasonable excuse generally, the provisions that relate to a reasonable excuse for a failure to correct (Finance (No 2) Act 2017 Sch 18 Para 23) specify circumstances that will not constitute a reasonable excuse. These are:

- An insufficiency of funds, unless attributable to events outside the taxpayer's control;
- Reliance on another person to do something, unless you took reasonable care to avoid the failure;
- Where an excuse ceased to apply, not remedying the failure without unreasonable delay; and

- Relying on advice where that advice is tainted. This will usually apply in relation to an avoidance scheme, where an adviser connected with the scheme gives advice that leads to an inaccurate return or failure to notify.

Notably absent from this list is ignorance of the requirement itself, raising the issue of Parliament's intention when it enacted the legislation. If Parliament had intended for ignorance of the requirement not to be an excuse it would surely have made that clear when it had the chance.

Our success with arguments for reasonable excuse was initially limited, with HMRC denying the vast majority of claims on the basis that 'ignorance is no excuse'. However, there have been a number of First Tier Tribunal cases in which HMRC has come under fire for its failure to properly publicise new legislation, and its assertions that the information is 'in the public domain' and it is the individual's responsibility to ensure they comply with all relevant legislation.

Following these cases, we took the opportunity to engage in discussion with HMRC regarding its view of reasonable excuse, and the fact it did not accord with that of the Tribunal. We noted additionally that HMRC's own officers do not appear to properly understand the concept, especially as it applies to the failure to correct. In a notable example of this, the HMRC officer concerned sent us a link to the government webpage which related solely to reasonable excuse for the late filing of a tax return.

HMRC's new manuals

HMRC's new manuals were introduced at the beginning of the year, and since then, we have seen an increase in the number of claims for reasonable excuse that have been accepted by HMRC, generally following digital disclosures. Regrettably, the consistency of HMRC's approach is still lacking, with very similar arguments, on similar facts, being accepted in one case and then denied in another.

To put this in context, we had a reasonable excuse claim accepted for a taxpayer who was not aware she had filing obligations, because (putting it simply) she looked after the children and left her husband to deal with their financial affairs. In another case, reasonable excuse was accepted where a taxpayer failed to declare foreign rental income on his UK tax return (which he filed himself), because the accountant that dealt with his overseas filings did not advise him he would also need to declare the rental income in the UK.

Contrast this with two cases where reasonable excuse was not accepted. In one, the individual filed his own UK tax returns and was not aware he had made a mistake until after 30 September 2018, whereupon he then contacted Buzzacott and filed a voluntary and unprompted disclosure. In another, an Italian national believed income that was not taxable in Italy, would also not be taxable in the UK, due to reciprocity within the EU. His other income was paid through PAYE, and so he did not file a tax return. He also discovered his errors after 30 September 2018 and made a voluntary unprompted disclosure.

On the face of it, there is no real difference between these cases. All four amount to a lack of knowledge, and a lack of opportunity to make a disclosure prior to 30 September 2018. However, HMRC appears to draw a distinction between the cases, claiming the latter did not take reasonable care to ensure their tax affairs were correct, and so their lack of knowledge was not reasonable.

Although tax investigations specialists would always expect, and indeed often insist, each case be considered individually and on its own merits, we can see no real distinction between these cases, and this lack of consistency on HMRC's part makes it considerably more challenging to advise clients and manage their expectations. Furthermore, there seems to be a distinct lack of coordination between those teams dealing with disclosures made under the Worldwide Disclosure Facility ('WDF') and teams that deal with formal enquiries and discovery assessments.

In our experience, reasonable excuse claims made under the WDF will generally only be accepted if it can be demonstrated the taxpayer's lack of knowledge was reasonable in the circumstances, and that reasonable lack of knowledge must be in relation to the original error, not the requirement to correct it. However, we have dealt with an enquiry where the case officer specifically asked if the taxpayer was aware of the

requirement to correct, and because we confirmed he was not, HMRC agreed not to charge an enhanced penalty for his failure to correct it.

Conclusion

In our experience, for HMRC to accept a claim for reasonable excuse, due to a lack of knowledge, there needs to be additional factors that can be cited as a reason why the taxpayer was unaware of the error in their affairs.

In cases involving offshore matters, and a failure to correct, HMRC continues to refuse to even address the question of reasonable excuse for the failure to correct itself, concentrating instead on the reason for the original irregularity.

Returning to the original question, this new manual does at least provide confirmation that ignorance can be a reasonable excuse, meaning HMRC has to properly consider the arguments made, rather than simply wheeling out its old maxim. It also gives a good indication as to the conditions that have to be met, allowing tax advisers to form better arguments and better represent their clients.

However, tax advisers should be aware HMRC is most likely to accept a reasonable excuse argument, for a lack of knowledge, where there are other factors which contributed to that lack of knowledge, and more often than not HMRC will simply trot out its new maxim, 'the taxpayer's ignorance was not reasonable'.

The skill of the tax adviser, and their ability to extract all relevant information from their clients to find other factors, and make their ignorance appear reasonable, therefore, comes to the fore.

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- *Antony Greenwood, Manager (Tax Investigations), Buzzacott. Call 020 7556 1475 or email greenwooda@buzzacott.co.uk*