

HMRC – what is a reasonable excuse?

Taxation is complex. In the UK there is evidence of plenty of stick with which to beat the errant taxpayer but very little carrot to motivate taxpayers. The deterrent effect of the numerous penalty regimes is considerable. Conversely, the complexity of UK tax law, especially for business taxpayers, means that the cost of compliance can be considerable and the potential to make mistakes is unacceptably high.

For most penalties which are intended to have a punitive effect, the taxpayer has the protection of the Human Rights Act (ECHR). In particular, the onus lies with HMRC to show that a failure has occurred and that a penalty is exigible.

In direct tax most of the penalties are imposed by the **Taxes Management Act 1970** (TMA 1970). The legislation protects taxpayers from penalties if there is a reasonable excuse.

S 118(2) TMA 1970: For the purposes of this Act, a person shall be deemed not to have failed to do anything required to be done within a limited time if he did it within such further time, if any, as the Board or the tribunal or officer concerned may have allowed; and where a person had a reasonable excuse for not doing anything required to be done he shall be deemed not to have failed to do it unless the excuse ceased and, after the excuse ceased, he shall be deemed not to have failed to do it if he did it without unreasonable delay after the excuse had ceased.

This podcast has been prepared on the basis of the UK legislation which is in force at 31 August 2013. In tax, the law can change with Finance Acts, Statutory instruments and decisions of precedent which includes not only decisions of the British Courts but also the European Courts. The involvement of Human rights in tax legislation is also an area of developing law and quite controversial.

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Many officers within HMRC do not agree that the law on human rights applies to tax penalties. They are wrong in their belief that civil penalties are not within criminal law and protection. But if you are promoting an argument that civil penalties are criminal charges, you need to anticipate argument from many HMRC officers. Especially when small fixed penalties are involved, it will seldom be worth arguing the point as the cost of litigation will far exceed the penalty.

As a starting point, when a tax geared penalty is sought by HMRC, the taxpayer has the protection of article 6(2) ECHR which states:

6(2) Everyone charged with a criminal offence shall be presumed innocent until proved guilty according to law.

The onus lies with HMRC to prove that an offence has occurred. This requires HMRC to show that their systems are such that the taxpayer failed to do something which ought to have been done. The standard of proof is the balance of probabilities but HMRC systems have earned considerable criticism in recent years and any attempt to impose a penalty may fail at the first hurdle.

There is also the question of proportionality.

There are a plethora of cases from the courts and tribunals on what constitutes a reasonable excuse for both direct and indirect tax. Like Balfour's elephant, it is difficult to describe but can be recognized on sight. Reasonable excuse can encompass:

Serious illness but as soon as the person is able to return to work they must respect their fiscal obligations

Death and bereavement

Catastrophe such as fire, flooding, computer failure, record destruction and even reliance on another when there is a reasonable expectation that the reliance was justified.

But what decisions of the court also confirm is that the court will interpret 'reasonable excuse' more reasonably than HMRC have done but they give a high priority to encouraging tax compliance.

Tax is complex and mistakes will occur. If the taxpayer has taken a mistaken but tenable view of the law and has taken reasonable care in deciding their position, such a mistake does not enter the penalty regime. In practice, the problem is producing the evidence that reasonable care was taken. The discipline must be to record the position and leave a clear trail.