[2016] UKFTT 0273 (TC)

TC05046

Appeal number: TC/2015/07191

COSTS – notification by Respondents that not defending proceedings- application by Appellant for costs on ground of unreasonable behaviour by Respondents - application refused

FIRST-TIER TRIBUNAL
TAX CHAMBER

GRAHAM ADDERSON

Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

TRIBUNAL: JUDGE GREG SINFIELD

Application determined on 19 April 2016 on written submissions only.

DECISION

Introduction

1. This decision concerns an application by the Appellant ('Mr Adderson') for an order that the Respondents ('HMRC') should pay Mr Adderson £11,157 in respect of costs in relation to his appeal against assessments which HMRC decided not to defend. The application was made under section 29 of the Tribunals, Courts and Enforcement Act 2007 ('the TCEA') and Rule 10(1)(b) of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ('the FTT Rules').

2. In summary, Mr Adderson claims that he incurred costs in relation to these proceedings as a result of the unreasonable behaviour of HMRC described below. HMRC oppose the application and contend that they did not act unreasonably. For the reasons given below, I do not consider that HMRC acted unreasonably in defending or conducting these proceedings and, accordingly, Mr Adderson's application for costs must be refused.

Background to the appeal

3. There does not appear to be any dispute between the parties about the events leading up to the appeal. The relevant facts may be summarised as follows.

4. In October 2001, Mr Adderson submitted a tax disclosure report, prepared by his then accountants Mapus-Smith & Lemmon, to HMRC (then the Inland Revenue). The report revealed previously undisclosed rental income and reconstructed the accounts for a fish and chip shop, the Downham Fryer, owned by Mr Adderson for the period 1996-97 to 1999-00 and also for a second fish and chip shop owned by Mr Adderson for the years 1998-99 and 1999-00. The tax disclosure report included a Statement of Assets and Liabilities as at 30 September 2001. The turnover included in the report was shown as exclusive of VAT. On the basis of the disclosure report, a contract settlement was agreed with the Inspector of Taxes, Mr Malcolm Garrod, now retired.

5. In 2006, Mr Paul Millions, Inspector of Taxes, opened an enquiry into Mr Adderson's 2004-05 tax return which included profits from the Downham Fryer for the year to 31 August 2004.

6. On 7 December 2007, there was a meeting between Mr Millions and Mr Adderson's representative, Mr Paul Medcalf. The notes record Mr Medcalf's explanation of why Mr Adderson did not want to attend the meeting:

> "Mr Medcalf said that Mr Adderson was still reluctant to see Millions personally. Mr Medcalf explained that Mr Adderson had been subject to the PAYE enquiry that Mr Millions was aware of, Millions' current enquiry, a VAT assurance visit and had recently received a further letter from a different PAYE Audit Office indicating that they wished to review the business again. Mr Medcalf said that, as a result, Mr Adderson was feeling a little persecuted and would prefer not to meet Millions."

7. On 11 January 2008, Mr Millions raised an assessment in respect of the year 2001-02 for £4,350.00.

8. In a letter dated 16 May 2008, Mr Millions referred to the September 2001 disclosure report and stated:

> "… I can advise you that I have spoken to a colleague who deals with VAT liability. The information that they have supplied leads me to believe that Mr Adderson has never declared the VAT liability that ought to have been paid on his fish and chip shop businesses from the date the first of these businesses started to trade until he registered the business in the summer of 2002.
>
> It therefore seems to me that the £96,000 estimated VAT liability shown on the statement of assets at 30 September 2001 has never been paid. My colleague is looking into the possibility of raising the charge now. If this cannot be done then, as the calculations of profit prepared prior to Mr Adderson making the offer which resulted in the £16,000 payment in January 2002 were made on the basis that VAT was to be paid, I will be considering the possibility of re-opening the earlier enquiry on the basis that the calculations of assessable profit were based on the assumption that VAT was to paid when, clearly, it has not."

9. In a letter of 22 October 2008, Mr Millions returned to the subject of the unpaid VAT:

> "My colleagues dealing with VAT advise me that the VAT due from the previous enquiry has never been paid and they are not now able to recover this. The Income Tax settlement negotiated at the conclusion of the previous enquiry was based on VAT exclusive figures and on the assumption that the net VAT due would be paid to HM Customs and Excise.
>
> "As such, I consider that my colleagues dealing with the previous enquiry were misled and I therefore intend to reopen that settlement and seek to negotiate a revised offer with Mr Adderson. I intend to wait until the position with regards to the later years becomes clearer before preparing revised calculations of the additional liability but, as interest will be due on any additional liability, Mr Adderson may wish to consider making a payment on account of any liability now."

10. On 20 January 2009, Mr Millions raised a protective assessment in respect of the year 2002-03.

11. In a letter dated 11 March 2010, Mr Medcalf stated that he had received advice that there was no scope to open up the previous enquiry. Mr Millions responded as follows in his letter of 15 March 2010:

> "Are you prepared to let me have a copy of this advice?
>
> As far as I am concerned the figures presented to my colleagues that formed the basis for the settlement with Inland Revenue were prepared on a VAT exclusive basis (i.e. VAT would be accounted for to HM Customs and Excise).

> Whilst Mr Adderson took the action he was advised to by Mapus-Smith & Lemmon and did register for VAT, the fact remains that, for whatever reason, VAT was not paid over to HM Customs and Excise as anticipated by the agreement reached with Inland Revenue previously.
>
> It may well be that Mr Adderson did not appreciated the consequences of this in terms of the agreement reached with Inland Revenue but I can see no reason why the treatment of this should be any different to a situation where annual financial statements were prepared which originally showed a cumulative VAT creditor of £95,932, which was subsequently not paid over to HM Customs and Excise. In such cases the VAT originally accounted for would be included as additional profit in the year that the business established that they did not need to pay the VAT to HM Customs & Excise.
>
> In my opinion, Mr Adderson has failed to advise either Mapus-Smith & Lemmon, you or Inland Revenue that the VAT he thought he had to pay had not been paid and, as I have now made this 'discovery', I am entitled to re-open the previous enquiry by virtue of Section 29 Taxes Management Act 1970.
>
> If you are unable to agree that Section 29 Taxes Management Act 1970 allows me to reopen the previous enquiry, please let me have your detailed reasons for believing that I am prevented from making a discovery under this section of the Act
>
> If we are unable to reach agreement on this matter then I will have to consider issuing formal assessments for each relevant year and leave Mr Adderson and you to consider your options and decide what you want to do next. If you are not aware of the current procedure for appeals, full details can be found on HMRC's website"

12. In a letter of 14 March 2011, Mr Millions proposed Without Prejudice adjustments to the turnover for the years 1996-97 to 2002-03 in respect of unpaid VAT. He ended the letter:

> "To move matters forward I would like written agreement to or comments on the adjustments I have proposed. I would like this by 11 April 2011 at the latest.
>
> If Mr Adderson is not prepared to agree the adjustments I have proposed I would like to have a meeting with him so that he can explain why, what, if any, of the adjustments he accepts and what he proposes for the adjustments he does not accept.
>
> … The proposals I have made in this letter may be reconsidered if negations break down before an agreement can be reached and formal action needs to be taken so that independent arbitration or adjudication can be implemented to resolve matters."

13. In a letter of 19 October 2011, Mr Millions stated that he intended to seek a penalty under section 95 of the Taxes Management Act 1970 in respect of the assessments he proposed to raise for 1996-97 to 1999-00. He also proposed additional liabilities and interest for the years 1997-98 to 2007-08 totalling £94,215.07.

14. In a letter dated 2 December 2011, Mr Medcalf stated that Mr Adderson was prepared to offer £17,500 to settle any outstanding liabilities.

15. Mr Millions wrote on 29 February 2012 as follows:

> "I have no doubt Mr Adderson believes he fully complied with the instructions given by Mr Garrod. Equally, I have no doubt Mr Garrod would have understood Mr Adderson was going to pay the VAT calculated as being due on the Downham Fryer before he accepted the calculations of additional profit prepared by Mapus-Smith & Lemmon.
>
> … It is unfortunate Mr Garrod did not ensure the VAT had been paid before he, in effect, agreed to relief being given for the VAT which should have been paid when the additional Income Tax liability on the omitted profit from the Downham Fryer was calculated. This certainly would not happen now that the two former departments have merged …
>
> I am not sure why Mr Adderson was under the impression he should advise HM Customs & Excise that he took over the fish and chip shop business in September 2001. There is nothing in the papers I have seen that indicates this was agreed by Mr Garrod. …
>
> Despite my comments above, in the end I believe it is only the actual contract (letter of offer and acceptance) between Mr Adderson and Inland Revenue which is relevant.
>
> As the letter of offer is silent on any requirement of Mr Adderson to notify HM Customs and Excise of his liability to VAT I do not consider that this requirement can be construed as forming part of the contract between Mr Adderson and the Inland Revenue.
>
> The offer Mr Adderson made was based on the assumption that VAT had or would be paid. This clearly did not happen. As I have said before. I am of the opinion I can 'discover' the original agreement was flawed because the offer Mr Adderson made was based on figures of additional Income Tax calculated on a 'net of VAT' basis and VAT was not actually paid."

16. In a letter of 24 May 2012, Mr Millions wrote:

> "I note that Mr Adderson is not about to change his view. Neither am I.
>
> I agree that the letter of offer is silent on the VAT. I would expect it to be. A letter of offer signed today in similar circumstances would still be silent on VAT. The differing legislation does not allow for letters of offer to include any VAT liability.
>
> The letter of offer was a means of settling the Income Tax and Class 4 National Insurance Contribution liability, not the VAT liability. …
>
> Just to make it clear, I am not attempting to collect the VAT which was estimated to be due but to say that, as this VAT was never paid, the calculation of the Income Tax and Class 4 National Insurance liability, included in the letter of offer Mr Adderson submitted, was flawed.
>
> I note you have again not provided details of the instructions given to you when you wrote to HM Customs and Excise on 18 April 2002 to advise

> them the Downham Fryer was taken over by Mr Adderson in September 2001. I will draw my own conclusions from this."

17. In his letter of 5 July 2012, Mr Millions considered how Mr Adderson might have come to register the fish and chip shop for VAT from February 2002:

> "In my opinion this was a conscious decision on Mr Adderson's part and is therefore a deliberate action. As I do not have any evidence that any officer of Inland Revenue, HM Customs and Excise or HM Revenue & Customs was complicit in this decision, I remain of the opinion that I am entitled to recover the Income Tax and Class 4 National Insurance underpaid as a result of this."

18. On 28 January 2014, Mr Millions set out why he believed he was entitled to raise assessments under the extended time limit discovery provisions:

> "… Mr Adderson … made the conscious, and therefore deliberate, decision to advise HM Customs & Excise that the Downham Fryer started trading in September 2001 when he was well aware he had started trading much earlier than that."

19. Following an unsuccessful attempt at Alternative Dispute Resolution, Mr Millions wrote to Mr Adderson on 12 June 2014 and stated that he would formally assess the additional profits for the years 1996-97 to 2002-03. Shortly after this letter was sent, Mr Adderson's adult son died unexpectedly. Mr Adderson asked Mr Medcalf to request a period of grace for the family to grieve. On 25 June, Mr Millions sent a further letter to Mr Adderson correcting a minor error in his letter of 12 June. On the same date he raised and sent the assessments for the years 1996-97 to 2002-03 for income tax and penalties of £23,601.13.

20. Mr Medcalf asked, on behalf of Mr Adderson, for an independent review of the assessments. On 4 August 2014, Mr Millions wrote to Mr Adderson in response as follows:

> "As part of the review process I am required by law to confirm my most recent view of the matter to you personally, although I have sent a copy of this letter to Mr Medcalf. M[y] view remains as set out in my letter of 12 June 2014, as revised by my letter of 25 June 2014 (i.e., Income Tax and Class 4 National Insurance Contributions are unpaid as a result of your decision to advise HM Customs and Excise that your fish and chip shop business in Downham Market started in September 2001 when you were aware it had started in December 1996)."

21. On the same day, Mr Millions also wrote to Mr Medcalf. The letter stated that he accepted Mr Medcalf's letter of 10 July 2014 as a formal appeal against the assessments and penalty determinations for the years 1996-97 to 2002-03 and had arranged for the amounts charged to be held over. Mr Millions also stated:

> "Despite the circumstances you explain in your letter, I am required to write to Mr Adderson personally regarding this and enclose a copy of the letter I have sent to Mr Adderson today.

> "As requested, I will not make any reference to Mr Adderson's son's death in any correspondence sent to Mr Adderson. However, if you consider it appropriate at any time, will you please express my sincere condolences to Mr Adderson."

22. Following a review, Mrs C Warner of Local Compliance Appeals and Reviews in Worthing wrote a letter dated 17 October 2014 to Mr Adderson to confirm that she upheld Mr Millions' decisions in respect of the discovery assessments. In respect of the application of the extended time limit legislation, Mrs Warner wrote:

> "Your accounts had been agreed on the basis that you would contact HM Customs and Excise to inform them you were trading and that you had started in December 1996 and that VAT was due to be paid. However when you instructed your new accountant you appear to have failed to advise him of your earlier trading. This is evidenced by the letter he sent to HM Customs and Excise on your behalf. If P J Medcalf had been aware of the circumstances of your business he would not have advised HM Customs and Excise of the start date being September 2001."

History of the proceedings

23. On 14 November 2014, Mr Medcalf submitted a notice of appeal by Mr Adderson to the First-tier Tribunal ('the Tribunal') by email. The appeal was against HMRC's review decision, dated 17 October, confirming assessments for income tax and penalties of £23,601.13 for the tax years 1996-97 to 2002-03. It appears that the attachments to the email were too large to be accepted by the Tribunal's email system and that no error message was sent to indicate that the notice of appeal had not been received.

24. In September 2015, Mr Millions wrote to Mr Medcalf to inform him that there was no application for an appeal in place. Mr Millions stated:

> "Please therefore let me have a copy of the application to Her Majesty's Courts and Tribunals Service of any acknowledgement from Her Majesty's Courts and Tribunal Service received in return.
>
> If there is no acknowledgement from Her Majesty's Courts and Tribunal Service, please let me know why you or Mr Adderson have not pursued the matter with them.
>
> If I do not hear from you by 2 October 2015, I will shortly thereafter and without further notice, release for collection all the tax, interest and penalties which were postponed pending the hearing of the appeal, on the basis that the statutory review decision is, in the absence of a valid application to Her Majesty's Courts and Tribunal Service, deemed to have been settled by agreement under the provisions of Section 49F(2) and Section 54(1) Taxes Management Act 1970."

25. On 16 December 2015, Mr Medcalf resubmitted the notice of appeal to the Tribunal. In a covering email, Mr Medcalf stated that the notice of appeal had originally been notified by email in November 2014. He explained that he had been told that, because the message exceeded 10 MB, it was not accepted onto the Tribunal's email system and no notice relating to that had been issued. He asked the Tribunal to accept notification of a late appeal.

26. The Tribunal notified the appeal to HMRC by email on 22 December 2015. The email stated that the case had been allocated to the Standard category and that HMRC should provide a Statement of Case to the Tribunal and the appellant within 60 days i.e. by Monday 22 February 2016 (the sixtieth day falling on a weekend).

27. By letter dated 16 February 2016, HMRC notified Mr Adderson's representative, Independent Tax & Forensic services LLP, that, having reviewed the papers relating to Mr Adderson's appeal, they would not be defending the case before the Tribunal. The letter gave the following reasons for HMRC's decision:

> "It is clear from reviewing the papers relating to the recent and the previous enquiries that HM Revenue and Customs do not have a discovery relating to income tax and National Insurance contributions due on the non-payment of VAT. It is clear that Mr Adderson has registered his business Downham Fryer with the VAT office. The problem appears to be that Mr Adderson has possibly failed to pay the VAT that he should have paid, however having spoken to a colleague who has knowledge of indirect tax, I have been informed that it is now too late to request the underpaid VAT."

28. HMRC copied the letter of 16 February 2016 to the Tribunal which acknowledged receipt of it on the following day. Later that month, Mr Millions discharged the discovery assessments for 1996-97 to 2002-03, reducing the additional liabilities and associated interest to nil. In his letter of 24 February to Mr Adderson, Mr Millions stated:

> "I do not propose to go into the detail of why the decision was taken to withdraw from the litigation but I do apologise for any stress and inconvenience caused to you while the matter was under consideration."

29. By emails dated 14 and 15 March 2016, Mr Gary Brothers of Independent Tax & Forensic Services LLP submitted Mr Adderson's application for costs of £11,157 to the Tribunal. The costs related to the preparation of the appeal document by Mr Medcalf on 1 December 2015 and a review of the papers and advice given by Mr Brothers or a colleague as well as the drafting of the costs application between 22 January and 14 March 2016. The letter clearly summarised the basis of the claim and a background note helpfully described the documents and correspondence from which the summary of the background to the appeal set out above is taken. I deal with the submissions made on behalf of Mr Adderson in support of the claim below. HMRC provided written representations in response on 1 April and Independent Tax & Forensic Services LLP provided some further submissions on behalf of Mr Adderson in reply on 13 April.

Legislation

30. Section 29 of the TCEA provides that the Tribunal 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 FTT Rules.

31. Rule 10 of the FTT Rules rule relevantly 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 of proceedings …"

32. Rule 10(1)(a) relates to wasted costs as defined by Section 29(5) of the TCEA Rule. Under that rule, the Tribunal may order a legal or other representative whose improper, unreasonable or negligent act or omission has caused a party to incur costs to meet those costs. Legal or other representative for this purpose is defined as any person exercising a right of audience or right to conduct the proceedings on behalf of a party. That is not the situation in this case and rule 10(1)(a) is not relevant to these proceedings. Rule 10(1)(c) relates to proceedings that have been allocated as a Complex case and is also not relevant to this appeal.

33. In summary, the Tribunal can only award costs in relation to these proceedings if Mr Adderson can establish that HMRC, who did not bring the appeal, have "acted unreasonably in … defending or conducting these proceedings".

Case law on costs

34. The proper approach to be taken in relation to applications for costs on the basis of unreasonable behaviour when an appeal before the Tribunal is withdrawn or not defended has been discussed in a number of cases. The case law was recently summarised by the Upper Tribunal in *Marshall & Co v HMRC* [2016] UKUT 116 (TCC) at [10] – [13] as follows:

"10. The scope of Rule 10(1)(b) has been discussed in this Tribunal in *Catanã v Revenue and Customs Commissioners* [2012] UK 172 (TTC), where Judge Bishopp, at [14], stated:

'Mr Catanã has made a number of points about the phrase "bringing, defending or conducting the proceedings". It is, quite plainly, an inclusive phrase designed to capture cases in which an appellant has unreasonably brought an appeal which he should know could not succeed, a respondent has unreasonably resisted an obviously meritorious appeal, or either party has acted unreasonably in the course of proceedings, for example by persistently failing to comply with the rules and directions to the prejudice of the other side.'

11. The reference to 'the proceedings' in Rule 10(1)(b) is to proceedings before the Tribunal which has jurisdiction of the appeal, whilst it has such jurisdiction. In *Catanã* this Tribunal approved (at [9]) the following statements from *Bulkliner Intermodal Limited v HMRC* [2010] UK FTT 395 (TC):

'….. It is not possible under the 2009 Rules … for a party to rely upon the unreasonable behaviour of the other party prior to the commencement of the appeal, at some earlier stage in the history of the tax affairs of the taxpayer, nor, even if unreasonable behaviour were established for a period over which the Tribunal does have jurisdiction, can costs incurred before that period be ordered. In these respects the principles in *Gamble v Rowe* … remain good law. That is not to say that behaviour of a party prior to the commencement of proceedings can be entirely disregarded. Such behaviour, or actions,

might well inform actions taken during proceedings, as it did in *Scott and anor (trading as Farthings Steak House) v McDonald (Inspector of Taxes)* [1996] STC (SCD) 381, where bad faith in the making of an assessment was relevant to consideration of behaviour in the continued defence of an appeal.'

12. Where HMRC eventually withdraw from a case against a taxpayer, in relation to the pre-2009 costs regime the Special Commissioners held in *Carvill v Frost* [2005] STC (SCD) 2008 that failure by HMRC properly to have reviewed its decision to pursue a claim would be relevant. The Commissioners stated (at [73]):

'Mr Brennan [counsel for the Revenue] told us that it was no part of our role in a costs application to look into the internal workings of the Revenue and examine the nature and extent of an internal review; if the taxpayer has a claim for administrative or other failing then that must be pursued elsewhere. It seems to us, however, at least in the circumstances of this case, that where we are required to determine the reasonableness or otherwise of the Revenue's conduct in pursuing a case from which it eventually decided to withdraw, internal action, such as the adequacy or otherwise of a review of the issues on which the Revenue's case is founded and which is carried out whilst the appeal is within the jurisdiction of this Tribunal, is directly relevant to the findings we are required to make as to the Revenue's conduct.'

13. Again in the context of the withdrawal by HMRC of a case before the FTT, the decision of this Tribunal in *Tarafdar (t/a Shah Indian Cuisine) v Revenue and Customs Comrs* [2014] UKUT 362 (TCC) is relevant. In *Market & Opinion Research International Ltd v Revenue & Customs Comrs* [2015] UKUT 12 (TCC), this Tribunal endorsed (at [18]) the test set out in *Tarafdar* at [34]:

'In our view, 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?'"

Submissions

35. Mr Adderson submits that he should be awarded costs under rule 10(1)(b) because HMRC acted unreasonably in defending or conducting these proceedings. The unreasonable conduct led to the raising of discovery assessments for 1996-97 to 2002-03 which Mr Adderson was required to appeal to the Tribunal and which were withdrawn only a short time after the appeal was lodged. Mr Adderson contends that the following conduct of Mr Millions was unreasonable:

(1) enquiring into every return submitted by Mr Adderson during the previous 10 years;

(2) seeking to reopen earlier issues without jurisdiction;

(3) insisting that he had made a discovery without proper reference to the legislation and case law; and

(4) failing to demonstrate that the insufficiency of tax was brought about deliberately by Mr Adderson as required by section 29(4) and 36(1A)(a) of the Taxes Management Act 1970.

Mr Adderson states that the unreasonable conduct caused him to incur costs in relation to the appeal to the Tribunal.

36. HMRC contend that only matters following the notification of the appeal by the Tribunal should be considered. Accordingly, the alleged unreasonable conduct cannot include the raising of discovery assessments because they pre-date the appeals which initiated the proceedings and are not part of them. HMRC submit that they did not act unreasonably because they reviewed the case within a reasonable time of being notified of the appeal by the Tribunal. As a result of the review, HMRC concluded that there was no discovery and decided not to defend the assessments. HMRC wrote on 16 February 2016 to notify Mr Adderson's representative and the Tribunal that HMRC would not be defending the proceedings. HMRC state that, by withdrawing as soon as they realised that the statutory basis for the discovery assessments was flawed, they acted entirely reasonably.

37. HMRC also note that Mr Adderson's application includes a claim for costs prior to HMRC being notified of the appeal and costs incurred after HMRC had indicated that they would not defend the proceedings. HMRC submit that these costs were not incurred in the conduct of the proceedings.

38. Relying on *Scott and anor (trading as Farthings' Steak House) v McDonald (Inspector of Taxes)* [1996] STC (SCD) 381, Mr Adderson submits in response that bad faith in making the assessments is a relevant consideration when deciding whether to award costs to an appellant. Mr Adderson contends that Mr Millions should have recognised that HMRC had no jurisdiction to raise the assessments at a much earlier stage. Mr Adderson relies, in particular, following as examples of bad faith:

(1) Mr Millions failed to address the issue of extended time limits and the requirement for deliberate conduct until 2014, more than five years after the issue of the discovery assessment was first raised.

(2) Mr Millions raised the assessments despite the lack of grounds for doing so.

(3) Mr Millions refusal to concede the discovery point caused distress to Mr Adderson which was aggravated by the fact that Mr Adderson's son died unexpectedly at around the same time as the assessments were issued.

(4) Although Mr Adderson acknowledges that Mr Millions would not have been aware of his son's death at first, Mr Millions failed to reflect on the case when he did become aware of it.

(5) HMRC's review of Mr Millions's decision to raise the discovery assessments was inadequate.

(6) Mr Millions was aware that Mr Adderson intended to appeal to the Tribunal in November 2014 and his failure to check the status of the case, which was not received by the Tribunal due to the attachments to it being too large, prolonged the life of the dispute.

39. In paragraph 31 of the submissions in response, Mr Adderson states:

> "… HMRC's conduct in the matter of raising the assessments that were the subject of the appeal was wholly unreasonable and there as ample opportunity prior to 16 February 2016 for HMRC to correctly apply the law and come to the opposite conclusion."

Discussion

40. This matter has a long history and I have set it out above because it explains why Mr Adderson feels so strongly that HMRC have behaved unreasonably and that he should be awarded his costs. Unfortunately for Mr Adderson, it is clear from the language of rule 10(1)(b) of the FTT Rules and the case law that the only matters that are relevant to an application for costs of and incidental to proceedings are matters of conduct in relation to those proceedings, ie after the commencement of the appeal. An order for costs under rule 10(1)(b) can only be made if Mr Adderson can show that HMRC has acted unreasonably in defending or conducting the proceedings after the appeal was lodged on 16 December 2015.

41. HMRC's conduct before the commencement of an appeal may be relevant if it shows that defending an appeal is unreasonable e.g. where an assessment was issued in bad faith as in the *Farthings' Steak House* case. Finding bad faith requires much more than a refusal by an inspector to accept that he or she is wrong, even in the face of compelling arguments by the appellant. It is a high hurdle to surmount and requires proof of some egregious conduct. In *Farthings' Steak House*, the Special Commissioner accepted evidence indicating that the investigation had been inspired by the Inspector's desire to get his own back on the taxpayers' accountant. There is no suggestion of any such malice on the part of Mr Millions in this case. In my view, Mr Adderson had wholly failed to show that Mr Millions (or anyone else in HMRC) acted in bad faith.

42. Whether Mr Millions's decision in this case that there was a discovery that enabled him to issue the assessments was wrong is not relevant to the costs application: the purpose of the appeals system is to allow wrong or doubtful decisions to be challenged. The issue is whether, once the proceedings had been brought by Mr Adderson, HMRC acted unreasonably. The reason for the withdrawal of the appeal was, as stated in the letter of 16 February 2016, because HMRC came to the view that there was no discovery. The fact that, once the appeal had been lodged, HMRC reviewed the decision to issue the assessments and withdrew the disputed decision before proceedings had even reached the stage of service of a Statement of Case cannot be said to be unreasonable. I accept that HMRC could have reached that view at a much earlier stage before Mr Adderson had lodged his appeal but that is not the question. The

relevant question is whether HMRC could have decided not to defend the disputed assessments at an earlier stage in the proceedings and, if so, was it unreasonable for HMRC not to have done so and withdrawn from the appeal at an earlier stage than they did. I consider that, taking account of the nature of the issues in the appeal and the intervening holiday period, HMRC could not reasonably have been expected to have reviewed the case and decided not to defend the appeal any sooner than the eight weeks that it took. Accordingly, I do not regard it as unreasonable that HMRC did not notify Mr Adderson and the Tribunal of their intention not to defend the appeal any earlier than they did in this case. It is clear that, unlike in *Carvill v Frost*, there was a rigorous review of the assessments at the time Mr Adderson made his appeal to the Tribunal) and HMRC did not allow matters to drift on but acted promptly to bring the appeal to an end. In conclusion, although I understand the frustration that must be felt by a party to an appeal when the other party repeatedly rejects arguments only to concede them at a late stage, I do not consider that HMRC have acted unreasonably in defending or conducting these proceedings. Accordingly I must refuse Mr Adderson's application for costs under rule 10(1)(b) of the FTT Rules.

Decision

43. For the reasons set out above, the application by Mr Adderson for an order that HMRC pay him £11,157 in respect of costs in relation to his appeal is refused.

Right to apply for permission to appeal

44. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with the Tribunal's 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.

GREG SINFIELD
TRIBUNAL JUDGE

RELEASE DATE: 21 APRIL 2016