CIVIL PENALTIES FOR TAX OFFENCES

by JAMES S. MacLEOD

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SUMMARY

This thesis contains of a review of the law of the three statutory offences of fraud, wilful default, and neglect, in direct taxation, together with an analysis of the consequences of these offences. The study is confined to offences, and their consequences, under the law of income tax, capital gains tax, and corporation tax. Value added tax law has not been considered, except to the extent that it has a bearing on direct taxation.

Taxation is imposed, by statute, on the United Kingdom as a whole, but insofar as they apply to Scotland, the statutes must be construed in accordance with the common law of Scotland, except where the statutes themselves direct otherwise. Accordingly, although the three statutory taxation offences of fraud, wilful default, and neglect are common to both England and Scotland, the application of the law in Scotland may differ to that in England because of the differences in the Scots legal system. This thesis is designed to explain how the law applies in Scotland. The application of the law in England, therefore, is not studied in detail except to the extent that it applies with equal force in Scotland.

Income tax is an old tax, and much of it is better understood with an appreciation of how and why it came to be there. The thesis begins, therefore, with an outline of the income tax administration and penalty code from its origin in Pitt's Act of 1799, and continues with an examination of the reports of the Royal Commissions, Parliamentary Committees, and other factors which have influenced the development of the law to its present state. The three offences of fraud, wilful default and neglect are of comparative recent origin. The words used are barely defined in the legislation itself, but a large, and at times, complex, body of case law has developed giving guidance as to what the words mean. Chapter 2 of the thesis contains an analysis of these offences, and shows how, in practice, the Courts have interpreted the statutory material. Chapter 2 also sets out the powers of the Inland Revenue to make assessments to tax on a guilty taxpayer.

The main consequence of fraud, wilful default or neglect in direct taxation is that the offending taxpayer may become liable to pay interest on overdue tax and a penalty based on the tax lost. These aspects are considered in Chapters 3 and 4. Chapter 4 contains, in addition to a review of the law, a comment on the practice of the Inland Revenue in exercising its jurisdiction in the application of the statutory code.

The final chapter, Chapter 5, contains a review of the remedies open to a taxpayer who is accused by the Inland Revenue of fraud, wilful default or neglect. Such a review is a necessary part of the study, because much of the law on Inland Revenue offences has been developed by the Courts in considering appeals by taxpayers against assessments to tax. Although many of the legal decisions are based on their own facts, and have little value as precedents, much useful information can still be gleaned from a review of the decisions. In addition, Chapter 5 contains a summary of judicial review procedures in both England and Scotland. These procedures exist to provide justice in cases where the statutory appeals procedure is deficient, and judicial review is being increasingly used by taxpayers in situations where administrative discretion has been abused.

The material studied for the purpose of this thesis, apart from the legislation itself, consists of the leading legal decisions on the statutory provisions, together with such commentaries as are available in the major text books on taxation and related subjects. A computer search of U.K. legal decisions back to 1950 was carried out. It will be apparent, however, from the thesis itself, that the application of the law by the Inland Revenue is of considerable importance, and so the study has been influenced by the writer's experience in practice, and includes commentary and material not published elsewhere.

The law is stated at December 31, 1987.

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PREFACE

"Whatever you do in regard to income tax, you must be bold, you must be intelligible, you must be decisive, you must not palter with it."

William Gladstone
Hansard April 18, 1853

"The flotsam and jetsam of a century's legislation have nowhere accumulated into a greater confusion than in the mass of enactments which prescribe penalties for failure to make returns or for the making of incorrect returns or claims."

Quoted from the 1936 Income Tax
Codification Committee. (Cmnd 5131)

"I can give (the House) the assurance asked for..... (T)he Revenue will adhere broadly to the present practice of reasonableness which it has adopted heretofore. If it had not adopted a reasonable practice there would have been great public disquiet and public complaint many years ago."

The Attorney-General,
Sir Reginald Manningham-Buller, Q.C.,
Hansard May 31, 1960

CHAPTER 1

TAX AVOIDANCE AND TAX EVASION

1.01 This dissertation deals with tax evasion and its consequences. Tax lost due to evasion is usually referred to as "back duty". In 1900, in Simms v. Registrar of Probates[1] before the Privy Council, the meaning of the word "evade" was explained in the following way "Everybody agrees that "evade" is capable of being used in two senses; (1) which suggests underhand dealing; and (2) which means nothing more than the intentional avoidance of something disagreeable". In taxation, "evasion" is normally used in the first of these senses, as the 1955 Royal Commission on the Taxation of Profits and Income[2] stated in its Report:- "Tax evasion denotes all those activities which are responsible for a person not paying the tax that the existing law charges on his income. Ex hypothesi he is in the wrong, although his wrongdoing may range from the making of a deliberately fraudulent return to a mere failure to make his return or pay his tax at the proper time. By tax avoidance, on the other hand, is understood some act by which a person so arranges his affairs that he is liable to pay less tax than he would have to pay but for the arrangement. Thus the situation which it brings about is one in which he is legally in the right except so far as some special rule may be introduced that puts him in the wrong".[3]

1.02 Thus the difference between tax avoidance and tax evasion is the difference between right and wrong. The avoider, seeing the possibility of tax being charged on him, takes legal steps to avoid the charge, so that the law produces a liability less than that which it would otherwise have been. The evader, on the other hand, prevents the law from being properly applied, by neglecting or refusing to meet those obligations which have been imposed on him. It may be found, however, that what starts as legal tax avoidance spills over into illegal evasion. For example, a taxpayer may adopt a tax-saving scheme or arrangement which he believes to be legal, but to avoid searching

enquiries from the Inspector, he may be tempted to disguise the true facts. Another example might be where a taxpayer seeks to cure a defect in a tax-avoidance arrangement by back-dating or altering a document. Thus an element of wrongful evasion may find its way into an otherwise lawful course of conduct. In evidence to the Committee on Enforcement Powers of the Revenue Departments[4] (The Keith Committee) a witness put the problem this way:-

> "The taxpayer builds a tax proof castle; if the Inspector could see inside it he would see the weaknesses in the castle's structure, but the taxpayer does all he can to make sure that the Inspector never sees inside it."[5]

Restricting the Inspector's view may amount to evasion.

1.03 The distinction between avoidance and evasion is in principle a clear one. In practice, it is often narrow and blurred. A brief examination of judicial comments on statutory construction and tax avoidance is therefore merited.

In United Kingdom law, tax avoidance is possible because taxation is a pure creation of statute, the statute being construed strictly in determining the scope of the charge. In Attorney-General v. Seccome[6] Mr. Justice Hamilton said, "The burden of proof is upon the Crown. It is for the Crown to bring the subject within the charge. In construing a Taxing Act, the presumption is that the legislature has granted precisely that tax to the Crown which it has described, and no more; and there is no presumption in favour of extending the scope of the Act" Similarly, in the earlier case of Attorney-General v. Sefton[8] Lord Wensleydale said, "However likely it may be that (property) should not be omitted, the subject cannot be taxed unless there are words clear enough to impose taxation. There must be clear words." And in Cape Brandy Syndicate v. IRC[9] Mr. Justice Rowlett said, "..... in a Taxing Act one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax. There is no presumption as to a tax. Nothing is to be read in, nothing is to be

implied. One can only look fairly at the language used."[10] It follows, therefore, that matters of equity, fairness, the mischief against which a section is directed, and presumption or substance, are not matters to which the Courts can direct themselves. In the early case of Partington v. Attorney-General[11] a case on probate and succession duties, Lord Cairns stated that "If a person sought to be taxed comes within the letter of the law, he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be. In other words, if it would be admissible in any statute what is called an equitable construction, certainly such a construction is not admissible in a taxing statute, where you can simply adhere to the words of the statute". It seems that Lord Cairns, a former Member of Parliament who had been both Solicitor General and Attorney General, regarded the "literal approach" to legislation as confined to fiscal statutes. In the same volume of the law reports, in Hammersmith and City Railway Co. v. Brand,[11a] he took a much wider view of the intendment and purpose of the legislation there under review.

1.04 Given that taxing statutes must be construed strictly, it follows that the tax consequences of a transaction must be determined by the form which the transaction takes, and not by any supposed substance which the transaction could have, or might have, taken. Although the preference for form over substance has not always been applied in taxation (see the dicta of Lord Atkinson in Lethbridge v. Attorney-General)[12] the principle was finally settled in favour of the form of a transaction in IRC v. Duke of Westminster.[13] In the course of a celebrated and extensively quoted judgement, Lord Tomlin said "Every man is entitled, if he can, to order his affairs so that the tax payable is less than it otherwise would be, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity."[14] In the Scottish case of Ayrshire Pullman Motors & David Ritchie Ltd v. IRC[15] Lord Clyde was more candid "No man in this country is under the slightest obligation,

moral or otherwise, to so arrange his affairs that the Inland Revenue can put its largest possible shovel into his stores."[16] These rather grudging acceptances of the principle of tax avoidance were echoed by Viscount Simon in Latilla v. IRC in the following terms "There is, of course, no doubt that (taxpayers) are within their legal rights (in avoiding tax) but that is no reason why their efforts, or those of the professional gentlemen who assist them in the matter, should be regarded as a commendable exercise of ingenuity or as a discharge of the duties of good citizenship. On the contrary, one result of such methods, if they succeed, is, of course, to increase the load of tax on the shoulders of the great body of good citizens who do not desire, or do not know how, to adopt these manoeuvres."[17] More recently, judgements of the House of Lords in W.T. Ramsay Ltd. v. IRC,[18] IRC v. Burmah Oil Co. Ltd.,[19] and Furniss v. Dawson,[20] show that although the form of a transaction is to be the basis on which it is taxed, the true form can only be determined by reference to the transaction taken as a whole, and that in particular, where in a pre-ordained scheme or arrangement, a step or steps are introduced which have no commercial purpose other than the avoidance of tax, the Courts are entitled to determine the form of the transaction without regard to these interposed steps.

1.05 Until the true meaning of the Westminster case was explained by the decision in Furniss v. Dawson the only satisfactory way of preventing tax avoidance was by means of legislation. The history of anti-avoidance legislation is relatively short. The phrase "legal avoidance" was first officially used by the 1906 Select Committee, chaired by Sir Charles Dilke. It seems that the 1906 Committee was the first such body to appreciate the extent to which tax law might be manipulated to minimise the tax burden. Asquith[21] considered that nothing could be done about it. "Income tax under the present law, and probably under any improvement they could make in the law could be evaded (sic) to a large extent." Apparently Asquith regarded avoidance and evasion as more or less the same. But Austen Chamberlain[22] saw it rather differently. "Evasion is the illegitimate denial of the tax and avoidance is the legitimate denial of the imposition of the tax. Hon.

Gentlemen spoke of avoidance as if it were the refusal to recognise a moral obligation. I do not think that there is any moral obligation on the part of any taxpayer to pay more taxes than he is legally liable to pay."

1.06 The first anti-avoidance legislation was introduced in 1914,[23] in connection with Excess Profits Duty. The legislation dealt with so-called "artificial transactions" but it seems to have been easily circumvented. The sale of trading stock at contrived prices seems to have been a common and successful arrangement.

1.07 In 1922 following the recommendation of the 1920 Royal Commission on Income Tax (the Colwyn Committee) legislation was introduced to prevent the avoidance of super-tax through the commercially unjustified retention of profits in closely controlled companies.[25] In 1936, a provision was introduced to restrict the avoidance of income tax and super-tax through the use of trusts and settlements.[26] The Finance Act 1936 also contained the first attempt at preventing tax avoidance through the transfer abroad of income-producing assets.[27] However, until the Second World War, relatively low rates of income tax, and the absence of a comprehensive tax on capital gains, meant that there was often little incentive for taxpayers to adopt artificial and complex arrangements to avoid paying tax. With the increase in tax rates during and after the War, and in particular, following the introduction of corporation tax and capital gains tax in 1965, the benefits of tax avoidance grew substantially, and as a result, the trickle of anti-avoidance legislation developed into a flood. It is not difficult to appreciate why this should be so. The tax avoider, anxious to stay within the law although not to pay tax, must accept a degree of disclosure to the Inspector of Taxes. By presenting the tax avoidance symptoms, the taxpayer puts the Inland Revenue in a position to diagnose the malaise in the tax system, and to devise a cure, particularly if the scheme or arrangement is in widespread use, and results in a substantial loss of tax to the Exchequer. Tax evasion is quite different. The evader often volunteers no information, unless forced to do so. It is, of course,

true that tax evasion is likely to be at its worst when tax rates are at their highest, but unlike tax avoidance, it seems that evasion has a long history.

1.08 Income tax in Great Britain was introduced by William Pitt the Younger in 1799, to finance the Napoleonic Wars. The rate of tax was 2 shillings in the £1. Pitt resigned office in 1802, and was succeeded, as Prime Minister and Chancellor of the Exchequer, by Henry Addington who repealed income tax when peace was declared following the Treaty of Amiens. It is clear, however, from the Parliamentary Debates, that the repeal of the tax had been forced on Addington by public demand, and that he himself saw much in its favour.[28] Accordingly, in June 1803, after the resumption of the War with France, income tax was reintroduced, but subject to a number of amendments and safeguards to prevent the widespread fraud and evasion which had characterised Pitt's income tax. Addington's Act is important in a number of respects, in particular, for the introduction of the principle of taxation at source, contained in Section 208 of the Act, which was carried forward, almost unchanged, into Sections 169 and 170 of the Income Tax Act 1952.[28a] In addition, Addington altered Pitt's heads of charge into the five schedules, A to E, which are still in use today. When Pitt succeeded Addington as Prime Minister and Chancellor he retained the new income tax, with a number of amendments, in the Act of 1805, while the final structure of income tax for the remainder of the War was settled by the Act of 1806 which was largely based on the Acts of 1803 and 1805, and which continued in force until income tax was repealed in 1816, when hostilities ceased.

1.09 In 1842, income tax was reintroduced by Sir Robert Peel. Although the 1842 Act was based on the Act of 1806, there were important differences reflecting economic and social developments since the turn of the 19th Century. But the administrative provisions of the 1806 Act were reintroduced, largely unaltered, and so the Act of 1842 is a convenient starting point for a survey of the development of the prevention of tax evasion.

1.10 Income tax evasion had concerned both Pitt and Addington. The 1799 Act was prefaced with these words "We your Majesty's most dutiful and loyal subjects ..... taking notice that the provisions made for that purpose (i.e. taxation) ..... have ..... been greatly evaded, and that many persons are not assessed .....". The references were to the assessed taxes, on items such as clocks and watches, dogs, wigs, and servants, which preceded income tax. These taxes had always been resented. The poet, Robert Burns (1759-1796), himself an excise officer, expressed his disapproval of one such tax in the following fragment, entitled "On Mr. Pitt's Hair-Powder Tax":-

> "Pray, Billy Pitt, explain thy rigs
> This new poll-tax of thine!
> 'I mean to mark the GUINEA pigs
> From the other common SWINE' "

1.10a Pitt's concern to stamp out tax evasion is evident from the explanation he gave Parliament for the introduction of the new tax:-

> "How then, it will be asked, is evasion and fraud to be checked? Knowing the difficulty of guessing what a man's real liability is, I do not think that the charge of fixing what is to be the rate ought to be left to the Commissioners. It would ..... be most acceptable ..... to make it the duty of a particular officer, as surveyor, to lay before the Commissioners such grounds of doubt as may occur to him on the amount of the rate at which the party may have assessed himself".[29]

1.10b The Acts of 1799 and 1803 both contained penalty provisions, and these were reproduced in Peel's Income Tax Act of 1842. But although the penalties for evasion were severe, they had little effect because of the absence of administrative provisions to support them. Thus the Surveyor of Taxes could impose a penalty in a case of fraud, but was virtually powerless to collect it.

1.11 In 1851 a Select Committee under William Hume M.P. met to consider, inter alia, income tax evasion, and what should be done about it. The Committee was charged with the duty of collecting evidence of evasion, and making recommendations. The Committee certainly collected evidence, and concluded that there was widespread evasion of income tax under Schedule A. The Clerk to the London General Commissioners stated, in evidence, that "(taxpayers) seemed to have ascertained what sum will pass (under Schedule A) and are content to go on with it". It seems that the Committee had little grasp of evasion under Schedule D, and in any event, although it identified the problem, it was unable to come up with any solutions. It therefore presented Parliament with all the evidence which it had collected, and left it at that. An appreciation of Schedule D evasion might have escaped the grasp of the 1851 Committee, but it did not escape the Board of Inland Revenue. The Board's Report of 1870 covering the years from 1856 to 1869, referred to a case where Schedule D profits of £6,500 were returned, but the true profit was £32,000, and another case where the reported profit of £190,000 was £60,000 understated. Yet no effective steps were taken to deal with the problem.

1.12 There was another Select Committee, the Hubbard Committee, in 1862. This Committee was primarily concerned with income tax differentiation, although other matters were also before it, including tax allowances for depreciation of plant and machinery. Income tax evasion was also considered and the Committee concluded that it was widespread and that something should be done about it. But the Committee could not decide on what should be done, and seems to have had some difficulty in separating the question of evasion from the other matters under consideration. One member, Sir Stafford Northcote, criticised the proposals for tax depreciation as defective, and stated "the plans which are under consideration might, if adopted, increase rather than reduce the mischief (of evasion)".[30] His statement was never published in the official report. Nevertheless, some of the deficiencies highlighted by the 1862 Committee were eventually dealt with. The Taxes Management Act 1880 consolidated and improved the machinery and administration of income tax. At that time, the General

Commissioners were responsible for making most assessments, and the 1880 Act gave the surveyor power to correct errors within four months from the end of the year of assessment. In addition, provision was made to rectify omissions by means of a surcharge made within 12 months of the year end. These powers were, of course, hopelessly inadequate to deal with cases of serious evasion, particularly where fraud had to be established. This aspect was recognised in the next review of evasion, by a Departmental Committee under the Chairmanship of Mr. C.T. Ritchie, M.P., which reported in 1905. The Committee took evidence, inter alia, from Mr. Stoodley, Secretary to the Board of Inland Revenue, and seems to have adopted many of the suggestions which he made. The Committee recommended that:-

1. Penalties should be imposed for failing to make a return, when asked to do so. The existing penalty code was almost powerless to deal with this weakness.

2. The existing penalty of £20 plus three times the tax due should be changed, to differentiate between fraud, and errors due to ignorance or carelessness.

3. The period during which assessments could be made to recover lost tax should be increased to three years, and

4. There should be more frequent prosecutions for fraud, and the names of guilty taxpayers should be published, together with details of their cases.

The Finance Act 1907 incorporated all these recommendations, except the one about publishing the names of tax evaders.[31]

1.13 In 1911, the Inland Revenue, in its battle against evasion, received support from an unexpected source. Section 5 of the Perjury Act 1911, (which did not apply in Scotland) enabled prosecutions to be made against individuals who submitted false income tax returns, and made false claims. The Perjury Act was the basis of most public

prosecutions for tax fraud up to the Second World War. It is still available to the Revenue, although prosecutions are now usually made under the Theft Act 1968. The Theft Act defines a number of offences for the purposes of English law, including theft and fraud. It is an English Act and may only form the basis of criminal prosecution in England. It is to be observed that although the Theft Act abolished the crime of "cheating" in English law, the crime was retained by Section 36 of the Act in relation to taxation offences, and was the basis of the criminal charge in the recent English case of R. v. Mavji,[31a] a case on VAT fraud.

The nearest Scottish equivalent to the Perjury Act is the False Oaths (Scotland) Act 1933. Section 2 of the Act created a statutory offence of (a) making a false statutory declaration and (b) making a false statement in any "abstract, account, balance sheet ..... report, returns, or other document". The penalty is a fine and/or imprisonment. According to Gordons Criminal Law 2nd Edition para 48-23, the 1933 Act is not used if the offence falls under another statutory provision, or constitutes perjury at common law.

1.14 In 1918, the Income Tax Act 1842, and subsequent Acts, were consolidated into a new Income Tax Act. The 1918 Act extended to 239 Sections and 7 Schedules. Part 5 of the Act dealt with Administration, Part 6 with Assessments, Part 7 with Appeals, and Part 8 with Collection. Unlike modern Acts, there was no penalty code as such; instead, the penalty provisions were scattered throughout the Act. They may be summarised thus:-

A - MONETARY PENALTIES

1.15 1. Section 107 of the 1918 Act, consolidating Section 55 of the Act of 1842, imposed a penalty on "A person who neglects or refuses to deliver, within the time limit in any general or particular notice, or wilfully makes delay in delivering a true and correct list, declaration, or statement, which he is required under this Act to deliver ....." For this offence, the

General Commissioners had power to impose a penalty of up to £20 plus three times the tax with which the taxpayer ought to have been charged. In an action before the Court, however, the penalty was limited to £50, and if the taxpayer could show that he was not liable to tax, no penalty could be imposed.

2. Section 126, consolidating, inter alia, Section 63 of the Taxes Management Act 1880, provided that "If the surveyor discovers that a person liable to tax has not been charged in respect thereof ..... he may, at any time within three years after the expiration of the year of assessment for which that person ought to have been charged, surcharge, to the best of his judgement, the person liable, to the amount which ought to have been charged for that year". However, Section 127 provided that if a person surcharged made a complete and accurate return within 10 days of the notice of surcharge, and the surveyor was satisfied with the return, the surcharge was to be withdrawn, while Section 129 provided for an appeals procedure by which, if he was successful, the taxpayer could have the surcharge quashed. In practice, therefore, a surcharge could not be effectively made in the absence of fraud.

3. Section 146, consolidating Section 127 of the 1842 Act, as amended by Section 23 of the Finance Act 1907, empowered the General Commissioners to impose a penalty where tax which ought to have been charged under Schedule D had not been charged due to an omission from a "statement or schedule" of the taxpayer. The maximum penalty was three times the tax with which he ought to have been charged, and could be made within three years of the end of the relevant year of assessment. However, no such charge could be made if the taxpayer could satisfy the Commissioners that the omission did not proceed from any "fraud, covin, art, or contrivance, or any gross or wilful neglect".

4. Section 100, which consolidated Section 52 of the Act of 1842, as amended by Section 22 of the Finance Act 1907, was the

section which imposed on a taxpayer the obligation to make an income tax return when required to do so, and whether or not he was chargeable to tax. But the penalty imposed on a person who failed to comply with the section but was not liable to tax was limited to £5 for any one offence.

B - FALSE RETURNS

1.16 1. Section 107 of the Act, which has previously been described, was concerned not only with the failure to make a return, but also with the making of a false return. The penalty for each offence was the same. The phrase used in the section - "failure to make a true and correct return" - was considered in Lord Advocate v. A.B.[32] and Attorney-General v. Till.[33] Attorney-General v. Till was an English case about whether the requirement to deliver a return meant a requirement to deliver a return which was true and correct. In a lengthy judgement, the House of Lords decided that it did, and that the person who made a return which was incorrect was in the same position, as regards a penalty, as someone who failed to make a return at all. The leading judgement was delivered by the Lord Chancellor, who attached "great importance to the rule that unless penalties are imposed in clear terms they are not enforceable". In finding for the Revenue, his Lordship not only reversed the decision of the Court of Appeal, but confirmed the judgement of the Court of Session in the earlier case of Lord Advocate v. A.B. (sub.nom. Lord Advocate v. Sawers).[32] An interesting historical feature of the Scottish case is that it was brought, not in terms of tax legislation itself, but under Section 22 of the Inland Revenue Regulation Act 1890, by way of information placed before the Lord Ordinary in the Outer House. The decision of the Lord Ordinary was reclaimed (appealed) to the First Division of the Inner House, where the Lord President confirmed the Lord Ordinary's finding. The taxpayer then elected, in terms of Section 6 of the Exchequer Court (Scotland) Act, for trial by jury, but the Lord Ordinary found that since he had a discretion over the procedure

to be adopted, and since in practice over many years, Revenue cases had been heard by a Judge without a jury, the taxpayer's application for trial by jury should be refused. A note at the end of the case states that within a few days, the taxpayer settled with the Revenue.

2. Section 132, which consolidated Section 178 of the 1842 Act, provided that "Where a person who ought to be charged with tax, as directed by this Act, is not duly assessed and charged by reason that he has:-

(a) fraudulently changed his place of residence or fraudulently converted, or fraudulently released assigned or conveyed, any of his property or,

(b) made or delivered any statement or schedule which is false or fraudulent, or,

(c) fraudulently converted any of his property ..... in order not to be charged for the same or any part thereof, or

(d) been guilty of any falsehoods, wilful neglect, fraud covin art or contrivance whatsoever ....." -

he was to be assessed and charged three times the amount of the charge which ought to have been made upon him. The section also provided that if any charge had been made which was less than the amount due, the penalty was to be treble the amount of the difference. Section 132 also provided that any person who "wilfully aids, abets, assists, incites, or induces another person to make or deliver a false or fraudulent account, statement, or declaration ....." was to be liable to a fixed penalty of £100 for every offence.

C - FALSE CLAIMS FOR RELIEFS OR ABATEMENT

1.17 The principal statutory weapon here was Section 30 of the 1918 Act, consolidating Section 166 of the Act of 1842. The Section applied where a person, in making a claim for any "exemption abatement or relief" (subsequently amended by the Finance Act 1920 to "allowance or deduction"), was guilty of any fraud or contrivance, or made a fraudulent claim, the penalty being £20 plus three times the tax chargeable on all his income. A person wilfully aiding or abetting anyone to commit such an offence was liable for a fixed penalty of £500. There was no power to mitigate either penalty, which was imposed by the Court.

1.18 If this summary of the 1918 Act provisions does anything, it shows that even before the days of sophisticated income tax law, the penalty code was already in a hopeless mess. Other parts of the tax system, for example the taxation of life insurance companies, were also piecemeal and inadequate. Income tax evasion was a major cause for concern. Ever since the Ritchie Committee of 1905, therefore, there had been calls for a thorough review of all aspects of income tax. In 1919, a Royal Commission on Income Tax, chaired by Lord Colwyn,[34] was set up. It reported in 1920. The Colwyn Committee had an immense impact on the tax system, and until well after the Second World War, it was the point of reference for any serious discussion on tax reform.

1.19 In framing its recommendations on the prevention of tax evasion, the Colwyn Committee seems to have been much influenced by the evidence presented, on behalf of the Board of Inland Revenue, by Mr. E. Stanford London, CBE, a Deputy Inspector of Taxes. The line taken by Mr. Stanford London was that the penalty provisions were designed to have a deterrent effect, and that such an effect could not be achieved unless

(a) the penalty code was seen and understood as a code of punishment, and,
(b) it was seen to be effective.

The Committee adopted many of Mr. Stanford London's proposals and made the following recommendations:-

1. that the existing three year time limit for penalty proceedings should be increased to six years

2. that the High Court should be able to impose the same penalties as could be imposed by the Commissioners

3. that penalties for false returns made by a company should be capable of being charged on the company or on its directors, and that where penalties were imposed on a partnership, any partner should be capable of being charged

4. that it should no longer be possible for a taxpayer to purge the offence of an incorrect return, by making a correct one, and

5. that the penalty for aiding or abetting the making of a false return should be increased.

1.20 The first of the Colwyn Committee's recommendations to be enacted was contained in the Finance Act 1923. Section 23(1) of the 1923 Act said that proceedings for the recovery of any fine or penalty incurred under the Income Tax Acts in relation to income tax, charged for the year 1920-21 or any subsequent year, could be commenced at any time within six years next after the date on which it was incurred. Sub-section (2) of Section 23 enacted that the penalty in Court proceedings, under Section 107 of the Income Tax Act 1918, should be increased to the same penalty as was exigible in proceedings before Commissioners. And finally, Section 23(3) increased to £500 the penalty for aiding and abetting another person to make or deliver a false or fraudulent return, etc.

1.21 The next important alteration to the administrative and penalty code came in 1927. Section 43 of the 1927 Act, the forerunner of Section 7 of the Taxes Management Act 1970, laid on taxpayers an obligation, when required to do so by the Inspector, to make a return

of all sources of income, and of the amount derived from each source. The section also provided that the penalty provisions regarding the delivery of lists, declarations, statements, and other information should apply to Section 43. Section 19 of the Finance Act 1939 was also concerned with notices and information, by placing on employers the obligation to make a return of emoluments and other sums paid to employees.

1.22 1942 was a watershed in the Revenue's fight against tax evasion. Until then, the Revenue time limit of six years in making an assessment had the effect that, where fraud or evasion had been committed over a long period, the Revenue could get tax for only the immediately preceding six years of assessment. From the point of view of the Revenue, therefore, Section 33 of the Finance Act 1942 was a major step forward, because it provided that, in respect of the fiscal year 1936/37 and subsequent years, assessments could be made at any time, for the purposes of making good any loss of tax attributable to fraud or wilful default committed by or on behalf of any person. The time limit of 1936/37 ensured that the legislation was not retrospective. In addition to extending the time limit for assessment, Section 33(2) provided that proceedings for the recovery of any penalty connected with such an assessment could be commenced within three years from the final determination of the amount of tax covered by the assessment. Tax payable under such an assessment was finally determined when the assessment could no longer be varied by the Commissioners or the Court, and any objection to the making of an assessment was to be made by way of an appeal.

1.23 Section 35 of the 1942 Act was a further weapon in the Revenue's anti-evasion armoury. This section provided that where a person engaged in a trade, profession, or vocation, failed to deliver a statement of profits or gains, or where such a statement was delivered, but was regarded as incorrect, the Revenue could serve on that person a notice requiring him to deliver his accounts to the Inspector, and where these accounts have been audited, to provide a copy of the auditor's certificate; and to provide the Inspector with all books

documents and accounts in his possession or power relative to his trade, profession or vocation. Where a person failed to comply with such a notice without a reasonable excuse, he was to be liable to a penalty of £50, plus £50 for every day during which the offence continued after judgement had been given against him. The section was strengthened by giving Commissioners power to issue precepts ordering the production of the matters specified in the section, and empowering the Inspector to take copies or extracts from any books or documents which were made available. The Finance Act 1942 had thus enacted a recommendation of the Colwyn Committee made more than 20 years earlier. But it was not without criticism in Parliament. Clauses 32 to 34 took up more Parliamentary time than any other single topic in the 1942 Finance Bill. The Attorney-General, in answering criticisms, admitted that existing procedures were vulnerable, but maintained that the taxpayer's protection was adequate - the power was vested in the Board of Inland Revenue, not the Inspector, and so the Inspector could only act with Board approval. In the light of the recent case of I.R.C. v. Rossminster[36] such assurances might well be regarded by some as having a somewhat hollow ring.

1.24 The final change of importance in the penalty code, before the law was consolidated in 1952, came in 1947, when Section 8 of the Finance (No. 2) Act of that year made provision for statutory interest on overdue tax, at the rate of 3%, where tax remained unpaid for more than three months after the due date for payment. It will be observed that the tax had to have been assessed before interest was due. The idea of "default" interest on tax lost due to tax evasion was not considered until 1960.

1.25 The Income Tax Act 1952 was a consolidation of the 1918 Act and subsequent Finance Acts. The Act of 1952 was, in a sense, a catalyst whereby the existing system, with its roots firmly in the 1842 Act, was prepared for the radical, and far reaching, changes which were to come. Many of these changes were recommended in the reports of another Royal Commission on Taxation, the Radcliffe Committee[37] of which the final two volumes were published in 1954 and 1955. The Radcliffe Committee was charged with a wide-ranging enquiry into all

aspects of the existing income tax system, and so it was inevitable that some consideration was given to tax evasion. The Committee rightly concluded that the key to preventing tax evasion was a good system of information about taxable income, and so it recommended that every taxpayer engaged in a trade, profession or vocation should be obliged to keep elementary business records, and that accounts submitted to the Inspector in support of an income tax return should form part of the return. The Committee also recommended an extension of the power of the Inspector to examine business records, and said that this power should also cover the examination of private records, where these had a bearing on income tax liabilities. On penalties, the Committee found itself "in something of a quandary" (para. 1070) since it was plain from the evidence taken, and from the work of the Income Tax Codification Committee, that the penalty code was complex and confusing, yet the Board of Inland Revenue considered that the penalty sections "though they contain some dead wood and overlapping, ... work satisfactorily in practice". (para. 1069). Accordingly, the Committee found itself unable to make specific recommendations, but it made a number of general recommendations including:-

(a) the restructuring of the penalty code to avoid confusion and overlap,

(b) the extension of the time limit for assessment on deceased taxpayers, where tax has been lost due to fraud, wilful default or neglect, to a period of six years from the date of death, the assessments to be raised within three years of death, and,

(c) a sharper distinction between fraud where intent to deceive was present, and lesser offences involving carelessness or negligence.

1.26 The Radcliffe Report was a milestone in the development of the modern tax system. Another milestone, although a somewhat embarrassing one for the Revenue, was the decision of the House of Lords in I.R.C. v. Hinchy,[38] where a retired civil servant who had omitted to return interest of £18.30, found himself liable for a penalty of £438.72. The case is discussed in more detail in Chapter 5. It was plain, following

the Hinchy case, that something was seriously wrong with the penalty provisions, any doubts being dispelled by the caustic comments of their Lordships in the House. The Finance Act 1960 therefore introduced an entirely new, and modern, penalty code. The 1960 Act swept away the somewhat antiquated language of the 1952 consolidation, and provided for three offences; fraud, wilful default, and neglect. The 1960 Act also upgraded the fixed penalties for offences, and ensured that tax-geared penalties were based on the tax lost, and not on the taxpayer's total liability, which is what had emerged from the Hinchy case. In addition, the new law differentiated between the offences, by prescribing heavier maximum penalties for fraud and wilful default than for the less serious offence of neglect. The existing Revenue power to mitigate penalties was retained.

1.27 The income tax machinery provisions and the new penalty code were consolidated, first in the Income Tax Management Act 1964, and again, in the Taxes Management Act 1970. Since 1970 there have been three legislative changes of importance. First, in 1975 the provisions governing the payment of interest on overdue tax, and the payment of tax under appeal, were changed, to ensure that taxpayers could not obtain a financial advantage merely by delaying the settlement of an outstanding appeal. Next, there were a number of administrative changes in 1984, to ensure that "delay cases" and non-contentious appeals are heard by the General Commissioners and not by the Special Commissioners. Finally, the Revenue were given new powers of entry and search in the Finance Act 1975. These powers were subsequently used by the Revenue against Rossminster Bank Ltd. and a number of its directors. In consequence of the Revenue's behaviour, the Bank unsuccessfully sought a Judicial Review of the way in which the Revenue had operated the relevant legislation.[36] Shortly after that unsuccessful application, the Revenue announced that criminal proceedings were not to be taken against the Bank or any of its directors and as a result, the Bank raised an action for damages against the Revenue. That action has not yet been heard by the Courts. However, the considerable disquiet caused by the attitude of the Revenue in the Rossminster[36] case, led to the appointment of a Committee, the Keith Committee, to review the powers of the Revenue

Departments. The Keith Committee reported in 1983 and its recommendations, or some of them, may become law in due course. Some of the recommendations on value added tax are already in force.

1.28 Until such time as the Keith Committee recommendations reach the Statute Book, the Taxes Management Act 1970 is the point of reference for any analysis of the administrative provisions of the income tax system, and of the penalties exigible for tax offences. A brief examination of the structure of the 1970 Act serves to round off this historical survey of the development of the system, and to introduce the later chapters of this dissertation.

1.29 It is self-evident that no direct tax system can operate without procedures for identifying those persons who are liable to pay tax, and obtaining from them sufficient information for their tax liabilities to be calculated. Parts II and III of the Act of 1970 contain 22 sections which (a) impose on taxpayers the obligation to notify the Revenue if they are liable to tax; (b) require taxpayers to make returns of income and capital gains, when asked to do so by the Inspector; and (c) require from certain third parties information about income and gains received by others. Failure to comply with these provisions is examined in Chapter 2, in the context of fraud, wilful default and neglect.

1.30 In addition to finding out who is liable to pay tax, a good tax system must ensure that the tax due is properly calculated, and that taxpayers know what they are due to pay, and when they must pay it. Taxpayers who have been wrongly assessed must have a right of appeal. Part IV of the 1970 Act is concerned with the assessing procedure; with the time limits for assessments; and with appeals against assessments, and other remedies open to taxpayers. The appeals procedure itself is dealt with in Part V, while Part VI is concerned with the collection and recovery of outstanding tax. Chapter 2 deals with assessments to tax so far as relevant to this dissertation, while Chapter 5 deals with appeals and other remedies.

1.31 Default interest and pecuniary penalties are dealt with in Parts IX and X of the Act. Part IX deals with interest on overdue tax, including interest on tax not properly or timeously assessed due to fraud, wilful default, or neglect. Part X deals with penalties. The civil offences of fraud, wilful default, and neglect, are discussed in Chapter 2. Default interest is dealt with in Chapter 3, and penalties in Chapter 4.

CH. 1

1. 16 LJPC 56
2. Cmnd 9474
3. ibid para. 1016
4. Cmnd 8822
5. ibid para.
6. (1911) K.B. 688
7. ibid, pp 702-703
8. (1865) 11 H.L. Cases 257
9. 12 T.C. 358
10. ibid p.71
11. (1869) L.R.4 H.L. 100

11a. (1869) L.R. 4 H.L. 171

12. (1907) A.C. 19 pp 26 & 27
13. 19 T.C. 490
14. ibid p.520
15. 14 T.C. 754
16. 14 T.C. p763
17. 25 T.C. p117
18. 54 T.C. 101
19. 54 T.C. 200
20. 55 T.C. 324
21. H.H. Asquith M.P. (1852-1928) Prime Minister 1908-1916
22. (1863-1937) Foreign Secretary 1924-1929
23. F.A. 1914 S.16
25. F.A. 1922 S.21
26. F.A. 1936 S.21
27. ibid S.18
28. (1967) B.T.R. 177 and 271

28a. Now T.A. 1970 SS 52 & 53

29. H.H. Monroe Q.C. "Intolerable Inquisition?" Stevens 1981 p7
30. Quoted in evidence to the Colwyn Committee, 1920
31. It seems that, originally, offenders names were published. See English Economic History by C.R. Foy, Heffer & Co. 1948 pp74-75

31a. 1986 STC 508

32. 3 T.C. 617
33. 5 T.C. 440
34. Cmnd 615
36. (1980) STC 40
37. Cmnd. 9474
38. 38 T.C. 625

CHAPTER 2

FRAUD, WILFUL DEFAULT, AND NEGLECT

2.01 Of the three civil offences of fraud, wilful default, and neglect, only one - fraud - is a crime, and only one other - neglect - is statutorily defined in the Taxes Management Act 1970. That definition says that "neglect" means negligence, or a failure to do something which the Taxes Acts require a taxpayer to do,[1] except that failure is not neglect if the taxpayer has a reasonable excuse for the failure, and puts it right within a reasonable time after the excuse has ceased.[2]

FRAUD

2.02 In the absence of a statutory definition of fraud for taxation purposes, it is submitted that the civil offence of fraud and the crime of fraud have the same characteristics, except that the standard of proof needed to establish the crime is the higher - criminal - standard of "evidence beyond reasonable doubt".

2.03 The crime of fraud, in Scots law, is a crime at common law. In this respect, it is fundamentally different from the English crime, which is the subject of an elaborate statutory framework continued in Sections 16 to 20 of the Theft Act 1968 which codified, and amended, the English common law. This difference raises an immediate problem. It is clear that if a taxpayer in Scotland is charged with the crime of fraud, he will be tried according to Scots procedure, and his guilt or innocence will be determined according to the law of Scotland. But what is the position of a taxpayer against whom the Revenue allege fraud before a hearing in Scotland of the General or Special Commissioners? Tax statutes apply to the United Kingdom as a whole. Is, therefore, a taxpayer likely to find himself being criminally prosecuted under one set of rules, but subject to a different, civil, code of law for the same offence? The writer considers that the answer to this question is "no". In Scotland, Scots law must apply to both

the civil and criminal offences. So the Commissioners, in dealing with a case of alleged fraud in Scotland, must apply the principles of Scots law. Questions of jurisdiction, as between England and Scotland, may be relevant in criminal prosecutions for tax fraud. In civil cases, jurisdiction is likely to be determined by the place of residence of the taxpayer as determining the place where Commissioners hear the appeal. In the case of a criminal prosecution, however, there may be a conflict where, for example, a fraud is started in England and finished in Scotland. In Laird v. H.M. Advocate, a fraud was performed partly in Scotland partly in England, against an English company. The High Court of Justiciary,in Scotland, held that since the main, and originating act took place in Scotland, the Scottish Courts had jurisdiction to hear the appeal.[2a]

2.04 There is nothing unusual in finding that fiscal statutes, drafted by reference to English Law, have a different meaning or different application in Scotland. In 1905, in L.A. v. Countess of Moray,[3] Lord Dunedin said "It is useless not to recognise the fact that (revenue) statutes are usually framed by draftsman but little conversant with the forms and requirements of (the law of) Scotland" In these circumstances the Scottish Courts must apply the law of Scotland to the words used.

2.05 In Scots law, the crime of simple fraud is the crime of deception or false pretence which is linked to, or causes, a practical result, and it is fundamental that the falsehood should have been perpetrated with the intent of causing the result. The absence of intent breaks the link between the two essential elements of the crime. McDonald's "Treaties on the Criminal Law of Scotland" (1867 at page 52) expresses that principle the other way round, as a definite practical result brought about by false pretences. The false pretences need not, however, be positive acts. Silence can, in circumstances, be fraudulent where, for example, a person has a duty to disclose information which he fails to do. This was the basis of the charge in a leading case on fraud in Scotland, Strathern v. Fogal,[4] where a landlord fraudulently evaded the payment of rates by omitting information from a return sent to the local assessor. The facts in

Strathern closely parallel the deliberate failure to make, or the omission of information from, returns for tax purposes. Fraud may also exist where a person makes an innocent statement which is subsequently found to have been false, but which is not corrected. Section 97 of the 1970 Act says that, in relation to the civil offence, such conduct amounts to negligence. But it may amount to a fraud at common law. Dr. Gill, in his thesis "The Crime of Fraud - A Comparative Study"[5] cites H.M. Advocate v. Livingston[6] in support of the proposition that fraud exists where a person knew that the disclosure of facts would lead another to act otherwise than he did and otherwise than the accused wished him to act. In Livingston the accused was a bankrupt, who ordered goods on credit without disclosing that he was a bankrupt, and in full knowledge that the goods bought could not be paid for.

2.06 It does not seem settled as to whether an opinion can be an element in fraud. An essential feature of the crime seems to be that there has been a fraudulent act. But Dr. Gill has expressed the view that an opinion, if not honestly held, could amount to misrepresentation. He cites H.M. Advocate v. Pattison,[7] in which a deliberately false opinion on the value of stocks was held to be relevant in a fraud charge, to support his proposition. For example, if a taxpayer claims relief for a trading loss, he may be obliged to demonstrate to the Inspector that the business which sustained the loss has been carried on commercially and with a view to profit, in terms of Section 170 of the Taxes Act 1970. That involves in part at least an opinion. If the taxpayer falsely represents to the Inspector that he expects the business to make a profit when he believes that it will never be profitable, is that fraud? It would seem that the short answer to the question is "Yes", but even if it were "No" it is unlikely that the short answer on its own would have satisfied the Inspector, and answers to further enquiries might involve falsehood amounting to fraud.

2.07 The decision in Adcock v. Archibald[8] shows that the practical result which is necessary to establish fraud is sufficiently wide that any result whereby the dupe has been prejudiced will be sufficient. For practical purposes, fraud in taxation will usually result in a loss

of tax to the Crown. If there is no loss of tax, there can be no tax-geared penalty, although there may be a fixed penalty. But if there is no loss of tax, may not there still be a practical result whereby the taxpayer is guilty of fraud? In Geddes[9] a man was charged with pretending to be a police officer, and asking drivers to produce their driving licences. The charge stated that the accused did "fraudulently induce them to do acts which they would otherwise not have done". Clearly, the persons duped suffered no economic loss, and no lasting prejudice except inconvenience. Nevertheless, the Crown Office thought that there was sufficient prejudice to mount a charge of fraud. It would seem, therefore, that a person who fraudulently submits wrong information to the Revenue which does not affect his tax liability, may nevertheless be guilty of fraud. However, a leading modern authority, Gordon's Criminal Law,[10] 2nd Edition, suggests that in practice a person is unlikely to be accused of fraud if the practical result does not include economic loss, or at least some measurable prejudice.

2.08 The essential feature of fraud in taxation, and the reason why it is so difficult to prove, is that the Revenue must show, in a civil case, that on the preponderance of probabilities, the result which was obtained by the dishonest conduct was the result which the taxpayer intended his conduct to bring about. In Cullens Trustees v. Johnstone[11] the Lord President said at page 937 "When you are considering whether, in making the statement, he acted fraudulently, you must go into his mind and purpose and intention and see whether his mind was in that corrupt, and I would almost say guilty, state when he made these statements. If it appears upon clear evidence, circumstantial it may be, that there were no reasonable grounds to believe the statements or that he did not believe them to be true and if it appeared that in making them he had a fraudulent purpose to deceive ..... that will be sufficient. But they must be pregnant circumstances, because, I must repeat to you again, that the law in no case presumes fraud - in no doubtful matter does the law lean to the conclusion of fraud. Fraud is a thing that must be clearly and conclusively established." It follows, therefore, that intent to deceive involves two questions of fact; the accused's belief as to the

truth, or honesty, of what he asserted or did, and his intention as to the belief of the dupe. The first part of that test is quite clearly a subjective one. In the English case of Derry v. Peek[12] Lord Herschell adopted the following formulation for fraud, incorporating an essentially subjective test:- "Fraud is proved where it is shown that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, that is careless whether it be true or false". His Lordship then qualified his use of the word "recklessly" by saying that it might be fraud because "for one who makes a statement under such circumstances can have no real belief in the truth of what he states". Recklessness may therefore be evidence of the subjective intent to deceive. Recklessness or carelessness, however, do not constitute an element in fraud unless they are of such a degree as to lead to the conclusion that there was indifference to the truth. Moreover, this deliberate recklessness, or, at the least, indifference to the truth, must have been perpetrated with the intention of deception. The intent, or mens rea is the crucial element.

2.09 In the practical circumstances of income tax it is not difficult to see the Inland Revenue's problem in establishing that a taxpayer is guilty of tax fraud. If, for example, profits are understated, or items of income or expense are wrongly classified, or trading stock or work-in-progress is wrongly valued, or provisions are wrongly calculated, the result may well be an underdeclaration of taxable income. But to establish fraud, the Crown would have to show that the errors were deliberately, or at the very least, recklessly made with the intention of evading tax, and in practice, that may be difficult. It may be made easier if a pattern can be established. Even then, however, false accounts may have been produced to deceive a bank, or shareholders, or partners, or an estranged spouse. The deception of the Inland Revenue, in these circumstances, would be incidental to the purpose of the pretence. Alternatively, it may be easier to establish fraud in a case where it can be shown that the only person who could have been deceived was the Inspector of Taxes where, for example, false wages books are kept with a view to the underdeclaration of income tax under PAYE, or false self-employed sub-contractors certificates are produced, or where there is evidence

of collusion between two or more parties and only the Revenue could suffer. The case of L.A. v. Keay[13] was a prosecution of an accountant who falsified the accounts and tax computations of clients with the result that their tax liabilities were fraudulently reduced. The accountant obtained no benefit from these frauds, some of which were unknown to his clients. He was found guilty, and sentenced to a term of imprisonment. In that case, the accused had pled guilty to the charge of fraud perhaps because he could suggest no possible purpose for the fraudulent entries in the accounts and statements, except the deception the Inland Revenue. More recently, in December 1986, the former champion jockey Mr. Lester Piggott was arrested on a warrant which alleged that he had made a false statement to the Inland Revenue about his tax affairs. Press reports have suggested that he had given the Inland Revenue wrong information about certain bank accounts, and that the Revenue had alleged that this wrong information had been deliberately given to evade taxation.

2.10 In view of the importance of mens rea or intent to the charge of fraud, and the difficulties experienced in establishing it, it is not difficult to envisage certain facts and circumstances which are more indicative of fraud than others. The Revenue gave evidence to the Keith Committee[13a] that three-fifths of all cases of suspected fraud referred by tax districts to the Enquiry Branch were regarded as serious, because the amount of tax lost was likely to be in excess of £20,000 and there were other factors suggesting that the taxpayer had intended to deceive the Revenue. These "other factors" included:-

a. the fact that the taxpayer under enquiry was a professional adviser in tax matters,

b. evidence of collusion between the taxpayer and others to defraud the Revenue,

c. evidence of forged documents intended to deceive the Revenue,

d. the fact that the taxpayer had denied that there were irregularities, and the Revenue had proof that there were,

e. the fact that the taxpayer had completed a "certificate of disclosure" or a "statement of assets" which he alleged to be true and which was subsequently found to be materially wrong,

f. that one offence was followed by another offence, and,

g. that the fraud was exceptionally large or ingenious.

2.11 The statistics for prosecutions show that most successful convictions were for frauds under the sub-contractors tax deduction scheme (about 100 a year on average, over the past five years) with successful prosecutions for false accounts being, on average, no more than 40 a year for a similar period.[14] These statistics perhaps reflect the very difficult hurdles which the Revenue have to surmount in establishing fraud as a criminal matter, and in particular, the strict requirement of corroboration in Scots law.

WILFUL DEFAULT

2.12 In practice, there is no difference in taxation between the civil offence of fraud and the civil offence of wilful default. The Revenue's powers to make assessments to recover tax lost due to fraud and wilful default are the same, and the same penalties are exigible where fraud or wilful default are established. Moreover, the two offences are not mutually exclusive. In Frederick Lack v. Doggett[15] back duty assessments were made on a company, on the basis that expenditure by a director and principal shareholder must have come from undisclosed company profits. The Commissioners and the High court found for the Revenue. On appeal to the Court of Appeal, the taxpayer contended that the findings of facts by the Commissioners pointed to fraud, and that accordingly, the taxpayer could not be guilty of wilful default. The Court held that fraud and wilful default were not mutually exclusive, and that the Commissioners had not erred in law in finding that wilful default had been established.

2.13 The Taxes Acts contain no definition of "wilful default" for taxation purposes. The phrase has been considered, however, in the

context of other legislation. In City Equitable Fire Insurance Co. Ltd.[16] Mr. Justice Romer said, in the High Court:- "But if an act or omission amounts to a breach of his duty, and therefore to negligence, is the person guilty of wilful negligence? In my opinion, that question must be answered in the negative unless he knows that he is committing, and intends to commit, a breach of his duty, or is recklessly careless in the sense of not caring whether his act or omission is or is not a breach of duty." That definition was quoted by Mr. Justice Wilberforce in Wellington v. Reynolds[17] as a reasonable working definition of wilful default in taxation. In considering the word "recklessly" Mr. Justice Wilberforce said:- "No doubt, if one considers the word "recklessly", some adjustment may have to be made in relation to the particular duty which is cast upon a taxpayer as compared with the particular duty cast upon a director or an auditor of a company; but it is clear that what I have to find is some deliberate or intentional failure to do what the taxpayer ought to have done, knowing that to omit to do so was wrong. What the taxpayer's duty was, in such a case as this, was to make a true and correct return in relation to income tax to the best of his judgement and belief; so that is what I have to consider here".

2.14 The term "wilful default" has been considered in the context of Section 30 of the Trustee Act 1925. It has been held that the phrase in that section implies either a consciousness of negligence, or breach of duty, or recklessness in the performance of a duty. In a case on earlier English trust law,[18] wilful default by a trustee was held to be the wilful failure to do something which ought to be done, as distinguished from doing something which ought not to be done. It must not be assumed, however, that wilful default in taxation, is limited to a deliberate failure to do something required to be done. Any error recklessly or carelessly made will amount to wilful default, if the recklessness or carelessness amounted to a disregard for the truth.

2.15 In practice, there may be no obvious and meaningful distinction between the civil offence of fraud and the civil offence of wilful default, but it seems clear that wilful default is something

less than fraud. In Barney v. Pybus[19] Mr. Justice Wynn-Parry said, "Prima facie a man must be presumed to intend the results which naturally flow from what he does. Prima facie, therefore, the conclusion ought to be that he deliberately refrained from making any returns of income over that period, in which case he was guilty of fraud or at least of wilful default." In a later case, Brown v. IRC[20] the Special Commissioners found that the taxpayer had deliberately omitted, from his tax returns, dividends received by his wife, knowing that for tax purposes they should be included. In the High Court, Mr. Justice Stamp said:- "It seems to me the Special Commissioners are perfectly right in holding as they did hold, that Mr. Brown in omitting to make proper returns in respect of his income was, if not guilty of fraud, at least guilty of wilful default".

2.16 Given that wilful default is less than fraud, what is the difference? It is submitted that the difference is that it is not necessary to establish that there was intent to deceive in wilful default. So the man who prepared wrong accounts to deceive his partners does not defraud the Revenue, but if he submits them to the Inspector knowing that they are wrong, he is certainly guilty of wilful default.

NEGLECT

2.17 For taxation purposes, neglect is defined in Section 118 of the 1970 Act as "negligence, or a failure to give any notice, make any return or produce or furnish any document or other information required by or under the Taxes Acts". There is a saving in Section 118(2) which provides that "for the purpose 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 Commissioners or officer concerned may have allowed; and where a person who has a reasonable excuse for not doing anything required to be done he shall be deemed not to have failed to do it if he did it without unreasonable delay after the excuse has ceased." The saving does not apply to the requirements to make returns for corporation tax purposes, within Section 10(1) of the 1970 Act.

2.18 Negligence and wilful default are mutually exclusive. In Day v. Williams[21] the General Commissioners found that the taxpayer was guilty of "neglect tinged with wilful default". The High Court found that the taxpayer was guilty of neglect only, and not of wilful default.

2.19 The definition of "neglect" in Section 118 is in two parts. The second part, neglect through failure, implies an objective test. A taxpayer who fails that test is guilty of neglect, unless he can show either that he was allowed extra time to do what the Taxes Acts required, or that he had a reasonably excuse for his failure. A taxpayer may obtain extra time to do something required by the Acts by asking the Inspector or other officer for it. Alternatively, he may be able to establish that the Revenue have tacitly given him extra time to complete a requirement. In one unreported case before the Special Commissioners, on interest under Section 88 of the Taxes Management Act 1970, a taxpayer had failed to report a capital gain within the time provided for by the Act. Instead, he submitted business accounts from which the gain was omitted. When it was discovered that the gain had been missed from the accounts, the Revenue were told, but did not raise assessments. The income tax return was then lodged, even later than the late-reported gain. Some time after that, the Inspector maintained that the gain (but nothing else) had been reported late and that interest was due under Section 88 of the 1970 Act. The Special Commissioners held that the Inspector's application for an interest certificate should be refused. By accepting, without comment, the late return, the Revenue had tacitly given extra time for the late reported gain.[22]

2.20 Where a taxpayer seeks to avoid a charge of neglect through failure, on the grounds that he was given extra time by the Revenue, the onus is on him to show that extra time was given. So also with the defence of "reasonable excuse". In practice, most arguments about "reasonable excuse" arise in connection with Revenue claims for interest under Section 88 of the Taxes Management Act 1970. Since applications for interest certificates under Section 88 are not capable of appeal beyond the Commissioners, none of the Commissioners decisions

are reported. The phase "reasonable excuse" appears, however, in Section 15(4) of the Finance Act 1985, in connection with value added tax, and has been considered by VAT Tribunals in that context. The decisions show that what is or is not a "reasonable excuse" is largely a question of fact and impression for the appellate Tribunal. One principle seems to have emerged, however, that ignorance of the law should not be taken as a reasonable excuse for value added tax purposes.[23] It is submitted that such an unqualified principle is too broad. For example, the reason for the ignorance of the law may itself be a reasonable excuse where, for example, a taxpayer asks the Revenue of Customs for an explanation of the law, and the explanation given is wrong. On the other hand, it would not be a reasonable excuse, it is submitted, for a taxpayer to know that he may have legal obligations, but make no effort to find out what they are.

2.21 Actionable negligence has four main characteristics. First, there must be some act, or a failure to act, which is voluntary, in the sense that the taxpayer could have done otherwise than he did. Second, the act or failure to act must have caused some harm or loss. Next, it must have been reasonably foreseen that the act, or failure, would cause the harm or loss. Finally, the person whose act or failure caused the harm or loss must have had a duty of care to ensure that the loss or harm did not arise, and the standard of care which he exercised must have fallen short of the standard of care which a reasonable man would have adopted in the circumstances.[24]

2.22 Applying these principles to taxation disputes, it is plain that the first three are of little practical relevance. Obligations under the Taxes Management Act 1970 are statutory obligations. If a taxpayer fails to meet his obligations, and as a result tax is not assessed, or not fully and timeously assessed, there has been a loss to the Crown and it must be reasonable to foresee such a loss arising. It also seems indisputable that there is a duty on a taxpayer to comply with his obligations with reasonable care. The law cannot, of course, expect the taxpayer to do what is impossible, but he is expected to do the best he can.[25] But when one reaches the last of all the characteristics, namely the idea of the "reasonable man", difficulties

may be encountered. The reasonable man is a central feature of actionable negligence. In Muir v. Glasgow Corporation[26] Lord Thankerton said: "In my opinion it has long been held in Scotland that all that a person can be held bound to foresee are the reasonable and probable consequences of the failure to take care, judged by the standard of the ordinary reasonable man." The reasonable man has been described as "The man who takes the magazines at home and in the evening pushes the lawnmower in his shirt sleeves".[27] He is not to be credited with anything more than a pedestrian sort of mind. He is not expected to deal with the unusual. Not for him the luxury of intuition, and he is not expected to take a leap in the dark.[28] In Muir, Lord MacMillan said[29] that the standard of foresight of the reasonable man should be judged by eliminating the personal equation. He was not, therefore, to be considered as over apprehensive or over confident. Accordingly, it would seem necessary to exclude those characteristics which the taxpayer in question might display and to attempt to define those characteristics which, on average, should be displayed.

2.23 It is submitted, however, that the required standard of care cannot be determined in a vacuum. Income tax returns vary in complexity. It may be assumed, therefore, that the more complicated the tax return, the more likely that the reasonable or average man would seek professional help in preparing it and, conversely, a taxpayer who employs professional help in the preparation of his tax return, although not thereby excused of his duty to take care, may nevertheless, by that very action, have shown that he is anxious to do what is right. The contrast is, therefore, between the careful man and the careless man. The careful man may well be in the habit of carefully preserving the information needed for his tax returns; of ensuring that his returns are completed and lodged within good time; and if he employs professional help with his returns, of ensuring that after they have completed, there are no obvious mistakes in them. In an unreported case before the Special Commissioners,[30] income tax returns prepared on behalf of a taxpayer contained errors arising from wrong information obtained from stockbrokers. The taxpayer was found guilty of negligence because he admitted that, on receiving the

completed tax return from his accountants, he signed it without reading it. Had he read the return, it is unlikely that he would have spotted the mistake but the Commissioners held that the reasonable man would read his income tax return before he signed it. This would suggest that the reasonable man would not seek to "second guess" his professional adviser, but, nevertheless, he must take reasonable steps to ensure that the adviser has produced an accurate return.[50a] When an adviser has been negligent, the effect of Section 97(2) of the 1970 Act is that the taxpayer must pay any penalty, but it is not clear that he is liable for default interest on the tax lost under Section 88.[31]

2.24 Like wilful default, negligence is very much a question of the impression gained by the appeal Commissioners. It is submitted that a simple mistake will not amount to negligence unless the Revenue can show that it was coupled with carelessness, or that there was a pattern of such mistakes which in general indicated a falling short of the standard of care which the average taxpayer would employ in relation to his tax affairs.

TIME LIMITS FOR ASSESSMENTS

2.25 Section 34 of the Taxes Management Act 1970 provides that an assessment to tax may be made at any time in the six years after the end of the chargeable period to which it relates. Any objection to an assessment on the grounds that it has been made out of time is to be made by way of an appeal. Where, however, the Revenue are able to establish that tax may have been lost due to fraud, wilful default or neglect, assessments to recover the tax so lost may be made outwith the normal six year period. Section 36 of the 1970 Act provides that were any form of fraud or wilful default has been committed by or on behalf of any person in connection with tax, assessments to recover the tax attributable to the fraud or wilful default may be made at any time. Section 36 has its origin in Section 33 of the Finance Act 1942, which provided that no assessment could be made for any fiscal year before the year ended April 5, 1937, and although that date no longer appears on the statute, the Revenue have never sought to make assessments for years earlier than 1936/37. In practice, of course, that time limit is

now of academic interest, since it would involve the Revenue in investigations stretching over fifty years.

2.26 It is to be observed that out-of-time assessments under Section 36 can be made to recover tax loss due to fraud or wilful default only. If, for example, tax has been lost due to fraud or wilful default in a year outwith the normal six year period, but, for the same year, some other item of income, which was properly returned, was never assessed, the assessment under Section 36 cannot extend to tax on that income.

2.27 Out-of-time assessments on individuals to recover income tax or capital gains tax lost due to neglect are dealt with in Section 37 of the 1970 Act. The law is not straightforward. First, before there can be an assessment to recover tax lost due to neglect more than six years after the year for which the assessment is to be made, the Revenue must establish that within the normal six year period an assessment has been made to recover tax lost due to fraud wilful default or neglect. A year for which such an assessment has been made is referred to in Section 37(1) as the "normal year". Section 37(3) then provides that, where there is a "normal year", assessments to recover tax lost due to neglect may be made for any of the six years ending with that normal year, but the assessments must be made by the end of the year of assessment following that in which the tax due under the assessment for the "normal year" has been finally determined. For example, if during the fiscal year ended April 5, 1987, the Revenue establish that a taxpayer had been guilty of wilful default in the fiscal year ended April 5, 1975 and had been guilty of neglect in the year ended April 5, 1976, an assessment could be made under Section 36 to recover the tax lost due to wilful default, but no assessment could be made for the following fiscal year to recover the tax lost due to neglect. If, on the other hand, in the year ended April 5, 1987, the Revenue discover that a taxpayer has been guilty of fraud, wilful default or neglect in the year ended April 5, 1983, and had been guilty of neglect in the year ended April 5, 1977, an assessment to recover the tax lost due to neglect in 1976/77 could be made in terms of Section 37, provided that it is made not later than the end of the year

of assessment following that in which the tax payable for 1982/83, due to wilful default, had been finally determined. An assessment is made when it is signed by the Inspector, and not when it is issued to the taxpayer.[32] An assessment is determined when thirty days have expired from the date in which it was made, without there being an appeal, or, if there is an appeal, on its determination by the Commissioners, or 30 days after the date on which any appeal has been settled by agreement between the Inspector and the taxpayer in terms of Section 54 of the 1970 Act.

2.28 Where an assessment to recover tax lost due to neglect has been made for one of the six years before the "normal year", these six years being referred to as the "earlier years", the Inspector may apply to the General of Special Commissioners for leave to make assessments to recover tax lost due to neglect in any of the six years which end with the beginning of an "earlier year" for which a neglect assessment was made. In addition, leave may be given to make an out-of-time assessment, on the grounds of neglect, where the assessment for the "earlier year" was one of a number of assessments made to recover tax lost due to fraud or wilful default under Section 36, provided that the latest assessment is for a year ending not more than six years before the end of the "normal year", and the other assessments made under Section 36 were for earlier years in sequence. The key in understanding this complex provision is that assessments under Section 37 can only be made for the purpose of recovering tax lost due to neglect. Assessments for fraud or wilful default are covered not by Section 37, but by Section 36. Were it not for Section 37(5), therefore, the Revenue could go back for six years before an "earlier year" provided that the earlier year was a year of assessment for neglect, but not if it was a year for assessment for fraud or wilful default. Section 37(5) caters for this anomaly. It is to be observed, however, that an isolated assessment to recover tax lost due to fraud or wilful default is not enough for Section 37(5) purposes. The assessment for fraud or wilful default which triggers the right to make earlier assessments under Section 37(5), must be one of a number of assessments, made <u>seriatim,</u> the latest of which, apart for the one for the "normal year" ended within six years before the end of the

"normal year", the next, if any, ended not more than seven years before the end of the "normal year"; and so on for earlier assessments.

2.29 The essential point in Section 37(5) is that the assessment referred to in Section 37(6) must be "one of a number" of assessments. There must therefore be at least two such assessments, each made to recover tax lost due to fraud or wilful default, although one might be for the normal year itself. However many assessments there are, they must be sequential, and the latest (other than one for the normal year) must be for a year which ends within six years before the end of the normal year.

2.30 Section 38 of the 1970 Act modifies Section 37 in relation to partnerships. For Section 38 to come into operation, there must first have been an assessment of the kind described in Section 37(1), that is, an assessment to make good a loss of tax due to fraud, wilful default or neglect for a "normal year", and the person assessed must have carried on a trade, profession or vocation in partnership with some other person or persons. Where these conditions are met, assessments to recover tax lost due to neglect within Section 37 may be made on:-

(a) The person in default, that is, the person who is guilty of neglect.

(b) Any person who, at any time in the year for which the assessment is made, was in partnership with the person in default.

(c) Any person, who, at any time in the normal year, was in partnership with the person in default, and,

(d) Any person who, at any time in the normal year, was in partnership with a person who had been in partnership with the person in default at any time in the year for which the assessment was made.

2.31 It is to be observed that Section 38 is not confined to partnership income. The section is therefore of wide application, since it is capable of affecting individuals who were "partners of partners of defaulting partners" and who may be wholly ignorant of the neglect, and even of the person who has alleged to have committed it. There are, however, two important modifications to Section 38. First, sub-section (3) provides that the assessment within Section 37 may be made "not only on the person on default but on any person ...." It would appear, therefore, that assessments within Section 38 must be joint assessments. It is not possible, it seems, for the Revenue to abandon the assessment on the person in default, and assess instead someone who had been his partner. Given that assessments on two or more persons must be joint assessments, Section 38(5) then provides that the assessment within Section 37(1) cannot include any income or gains of any innocent partner, nor can the tax be recoverable from such an innocent partner. The effect of sub-section (5), therefore, is that interest and penalties are calculated only on the tax lost due to neglect, and the liability does not become the several liability of any former partner within Section 38(3). Nevertheless, it would appear that the liability is a joint liability of the partnership, and can be recovered as such.

2.32 Neglect by a company is dealt with in Section 39 of the 1970 Act. In substance, Section 39 is no different from Section 37, except to the extent that modifications are needed because companies are assessed on profits for periods of account, and not for fiscal years.

2.33 The general time limit for assessments on the executors of a deceased person is that any assessment, no matter its purpose, must be made no later that the end of the third year next following the year of assessment in which the deceased died. Difficulties in the interpretation of the phrase "next following" are considered in paragraph 412 in connection with penalties. Except in cases of fraud, wilful default or neglect, the normal time limit of six years will apply, so that an assessment made in the third year following the year of death can only extend to income or gains for the three years before the year in which death occurred. But Section 40(2) modifies this rule

where assessments are made to recover tax lost due to fraud, wilful default or neglect. In such a case, the Commissioners may give leave for assessments for any of the six years of assessment ending not earlier than the year in which death occurred, provided that the assessment or assessments are made before the end of the third year next following the year of assessment in which the deceased died.

2.34 It will have been observed that assessments to recover tax lost due to fraud, wilful default, or neglect outwith the normal six year period may only be made with the leave of a General or Special Commissioner. The sections envisage two types of leave being necessary. First, there is leave for assessments to recover tax lost due to fraud or wilful default within Section 36; for assessments under Section 37 to 39 for any of the six years ending before the "normal year"; and for assessments on personal representatives to recover tax lost due to fraud, wilful default or neglect within Section 40(2). Leave for these assessments is governed by Section 41 which, by its terms, does not give the taxpayer any right to be present at the application for leave, or to have his views heard. This apparent injustice was considered by the English High Court in Perlberg v. Varty[33] when it was confirmed that the proceedings for leave under Section 41 are administrative proceedings only, and that the taxpayer's presence is not permitted by the Section itself. In that case, the Court considered that there was no injustice, because the taxpayer would have an opportunity to appeal against the assessments, and so to have his case considered by the Commissioners. Section 41(2) provides that a Commissioner giving leave to make the assessments shall not take any part in any subsequent appeal hearings on these assessments. Despite this apparent safeguard, however, the Section can work against taxpayers, as was shown in the recent case of R. v. Special Commissioners ex.p. Stipplechoice Ltd.[34] when an application was successfully made for a judicial review of the circumstances in which leave to make out of time assessments, within Section 41, was granted.

2.35 Next there are two instances where a taxpayer may be present, and give evidence, at a hearing of an application by an Inspector for leave to make an out of time assessment. These circumstances arise

when in terms of Section 37(5) or Section 39(5), leave is sought to make assessments to recover tax lost due to neglect for any of the six years before the "earlier year" referred to in these Sections. In these cases, the taxpayer is permitted to be present when the Inspector makes his application, and is entitled to be heard by the Commissioners.

INLAND REVENUE ERRORS

2.36 What is the position of a taxpayer who, having complied with all the provisions of the Taxes Acts on returns, etc, finds that he is asked to pay less tax than he ought, because of an Inland Revenue error? For example, an amount of income, properly and timeously returned, may not be assessed: an assessment may be raised in the wrong amount, because something has been omitted, or due to a simple error of arithmetic: an item of expense may be allowed more than once: or an income tax repayment may be wrongly calculated and too much may be repaid.

2.37 It is submitted that the obligations on a taxpayer under the Taxes Management Act 1970 do not include an obligation to point out to an Inspector of Taxes that an amount of income or gain, properly returned, has never been assessed. The duty to make an assessment rests with the Inspector of Taxes, and so a taxpayer cannot be guilty of any offence if the Inspector fails to do his job. The same position would follow, it is submitted, if the Inspector raises an assessment for an amount which is too low, provided that full returns have been made. No default or neglect can be alleged against someone who accepts the assessment, and pays the inadequate tax demanded. This should be contrasted with the situation which arose in Amis v. Colls[35] where a taxpayer who had failed to make proper returns accepted estimated assessments which he knew were too low. In that case, the Court held that the taxpayer was guilty of wilful default.

2.38 It is submitted that the situation may be different if a taxpayer makes a claim for relief which, subsequently, he discovers to be wrong. In that case, he is obliged to correct the false claim,

otherwise he may be guilty of negligence in terms of Section 97 of the 1970 Act. It is to be observed that the negligence arises, not by having made the claim, but having failed to correct it once it is known to be wrong.

2.39 It is not uncommon for the Inland Revenue to make a repayment of tax in excess of the correct amount which is repayable. In these circumstances, any interest (called repayment supplement) on the repayment will also be wrong. Before 1982, the Revenue had only a limited power to recover such over-repayments of tax. The legislation itself was inadequate, and there was no power whatever to recover overpayments of repayment supplements. Moreover, a civil action through the Courts for recovery of the amount was unlikely to succeed. Court actions to correct such mistakes are not competent unless the mistakes are of fact. In Taylor v. Wilson's Trustees,[36] the Court of Session held that an arithmetical error in the calculation of tax was an error of law, and on the basis of this judgement, it is difficult to see how any mistake in taxation could be anything other than an error of law. A taxpayer in such a position, of course, could offer to repay the amount of the excess, but if he does not, is he guilty of any offence? It has been suggested that the Theft Act 1968 created a category of crime of "stealing by finding", and that a taxpayer who knowingly keeps an excessive tax repayment might be guilty of such a crime. But the Theft Act is an English Act. It has no counterpart in Scotland, where the crime of theft, which is a common law crime, is the dishonest taking by one person of the property of another, without the owner's consent. It is submitted that by keeping an excessive repayment of tax, a taxpayer cannot be guilty of the Scots crime. It is this aspect which, it is understood, the Theft Act sought to change in England, but which remains unchanged in Scotland. It is submitted, however, that the position might be different if the Inspector had agreed the amount of the repayment of the taxpayer and then paid more than the agreed amount. In the case of Robert Potter,[37] fraud was established where a person tried to exploit an innocent error made by a bank clerk in the person's favour. But in that case it was beyond doubt that the accused and the Bank both knew what the correct amount was.

2.40 It is also submitted that by keeping an over-repayment of tax, a taxpayer is not guilty of fraud. First, there can be no deception if the taxpayer has complied with all the provisions of the Taxes Act, and submitted true and correct returns. In addition, without some evidence of misrepresentation or deception, it is difficult to see how the Revenue could ever sustain an argument that there was intent to deceive. Finally, it seems that there is no offence under the Taxes Management Act 1970, because every such offence presupposes that the taxpayer either failed to do something required by the law or did something which was wrong, either wilfully or carelessly.

CH. 2

1. TMA 1970 S.118(1)
2. TMA 1970 S.118(2)
2a. 1985 SLT 198 (see also "Jurisdiction and Criminal Law in Scotland and England" Juridical Review Dec. 1987 p.179
3. (1905) AC 501
4. 1922 SLT 543
5. Unpublished Ph.D. Thesis, University of Edinburgh 1976
6. 15 R 48
7. (1901) 3 Ad. 420
8. 1925 J.C. 58
9. 1963 Unreported
10. 2nd Ed. W. Green & Co. 1978 para. 18-19
11. 1865 3M 935
12. (1889) 14 A.C. 337
13. 1985 unreported
13a. Cmnd 8822 Ch.9 para.11
14. ibid Ch.9 para.15
15. 46 T.C. 524
16. 1925 Ch.D. 407
17. 40 T.C. 209
18. Re Stevens (1898) 1 Ch. 162
19. 37 T.C. 106, p.110
20. 42 T.C. 583
21. 47 A.T.C. 459
22. IRC v. McDonald Lockhart 1981 unreported
23. See eg. Rhodes v. CCE London Tribunal 1986/25 (unreported)
24. See e.g. Dorset Yacht Co. v. Home Office (1970) A.C. 1004
25. Moschi v. IRC
26. 1943 SC (HL) 3. at p.8
27. Hall v. Brookland (1933) K.B. 205 at p.224
28. McColl v. McAuley & Noble 1962 SLT (Notes) 3
29. 1943 SC (HL) 3 at p.10
30. IRC v. McDonald Lockhart 1981 unreported

30a. In L.B. Laboratories Inc. v. Mitchell 39 Californian Reports 56. an accountant was successfully sued for damages by a client when tax returns had been submitted late, to the Internal Revenue Service. But in Trent and Sons Ltd. v. Price Waterhouse & Co. (1935 unreported) a taxpayer failed in an action to recover penalties paid to the Revenue, on the grunds that the taxpayers own moral turpitude was the basis on which penalties had been paid. See further R.W.V. Dickerson "Accountants and the Law of Negligence". Canadian Institute of Chartered Accountants 1966.

31. see para 3.14

32. Honig v. Sarsfield (1986) STC 246

33. 48 T.C. 14

34. 1985 STC 248

35. 39 T.C. 148

36. 1974 SLT 298

37. (1844) 2 Brown 151

CHAPTER 3

DEFAULT INTEREST

3.01 The Crown's right to interest on overdue tax is contained in Part 9 of the Taxes Management Act 1970. Although the 1970 provisions originated in 1960, when the tax code for interest and penalties was substantially recast, interest on overdue tax as a statutory right was first introduced in 1947. Prior to that time, the Revenue had to sue for recovery of interest on tax lost due to fraud or neglect.[1]

INTEREST ON OVERDUE TAX

3.02 Until 1975, tax which had been assessed was not overdue unless it was not paid from the later of the due date for payment, and 30 days after the day on which the assessment had become final and conclusive. The law is contained in Section 86 of the Taxes Management Act 1970. If, therefore, the Inspector failed to raise the appropriate assessment before the normal date for payment had been reached, no interest could be charged provided that the tax was paid within 30 days of the assessment, once it was issued, having become final and conclusive. And if the assessment was appealed against, so much of the tax as was in dispute was not due and payable until 30 days after the appeal had been settled, either by agreement under Section 54 of the 1970 Act or by the Commissioners. Because of the many opportunities afforded by the legislation for taxpayers to delay paying tax without incurring an interest charge, new rules, amending Section 86 were introduced by the Finance (No. 2) Act 1975 to enable the Revenue to collect interest on tax which had been assessed, even where there was an appeal not yet determined. Section 86 does not, however, apply until an assessment has been raised.

DEFAULT INTEREST

3.03 Where an assessment has been raised to make good a loss of tax due to the taxpayer's fault, Section 86 of the Taxes Management Act 1970 does not apply. Instead, Section 88 directs that interest is to

apply from the date when the tax lost would have been payable if the assessment had been raised before the normal payment date. These dates are set out in sub-section (5), the appropriate date being used in calculating the interest charge, notwithstanding that it was a non-business day within the meaning of Section 92 of the Bills of Exchange Act 1882. The taxes to which Section 88 applies are income tax, corporation tax and capital gains tax. Section 88 does not apply to advance corporation tax or to income tax on annual payments and interest paid by companies, collection of which is governed by Schedule 20 to the Finance Act 1972. Instead, Section 87 charges interest when payment of these taxes is overdue.

3.04 Section 286 of the Taxes Act 1970 provides that where a close company, otherwise than in the course of a money-lending business, makes a loan or advances any money to an individual who is a participator of the company, the company is to be assessed to an amount equal to 27/73rds (the current rate of advance corporation tax) of the loan or advance. It is to be observed that although the amount which is assessed is tax which is due for payment within fourteen days after the issue of the notice of assessment, it is neither corporation tax, income tax, nor advance corporation tax. Section 286 sets out a number of situations in which the charge to tax is not to apply, as well as defining other transactions which are to be treated as within the scope of the section. The Inspector's right to obtain information about transactions within Section 286 is contained in paragraph 19(5) of Schedule 16 to the Finance Act 1972, which allows a request for information to be incorporated in a return of distributions received and paid. In practice, it is on this return that a loan to a participator would be declared.

3.05 Where a close company fails to make a return of a loan or advance within Section 286, Section 109 of the Taxes Management Act 1970 says that the due date of payment of the tax, for the purposes of default interest under Section 88, is to be April 1st following the date on which the loan or advance was made. Thus if, due to fraud, wilful default, or neglect, a close company fails to report a loan or advance made to a participator who is an individual, Section 88

interest can be charged on the amount which ought to have been paid to the Revenue calculated from April 1st following the date when the loan was made. Before the law was changed by the Finance Act 1986 the interest charge continued even if, before the company gave notice of the loan, the loan was repaid, because although Section 286(5) provided that the close company could claim a repayment of the tax paid if the loan or advance was itself repaid, that repayment could only be made after the tax had been assessed, and this could not happen if the loan or advance was never reported to the Inspector. In practice, the Revenue did not take the point, and it has now been rectified by the 1986 Act, so that default interest cannot be charged for any period after which the loan has been repaid.[2]

3.06 In order to show that interest is due under Section 88, the Revenue must prove that:-

1. the taxpayer was guilty of fraud, wilful default, or neglect;

2. tax was lost to the Crown as a result of that fraud, wilful default, or neglect, and,

3. the interest has been charged on an assessment made to make good that loss of tax.

3.07 The meaning of "fraud, wilful default, or neglect" has already been discussed.[2a] The phrase "loss of tax" was considered by the Court of Appeal in Knight v. I.R.C.[3] In that case, following a back duty enquiry, assessments on the profits of a cattle dealer were confirmed in the figures advanced by the Inspector, based on capital statements prepared by him. The assessments were for the four fiscal years ended April 5, 1956, and were all raised by the Inspector in 1955. The taxpayer contended that these assessments had not been made to make good a loss of tax, because they had been made within the normal six year period for making assessments, and that a loss of tax could not arise unless the normal six year period had expired. The Court in dismissing the taxpayer's appeal, held that the phrase "loss of tax" meant tax which had not been assessed because the taxpayer had either

failed to make a return, or had not made a correct return. In a later case, R. v. Holborne Commissioners (ex parte Rind Settlement Trustees),[4] the taxpayers, a solicitor and two accountants who were trustees of a settlement, were late in making returns of income and chargeable gains. When pressed to do so by the Revenue, the trustees made payments to account of approximately one-third of the tax ultimately found due. On appeal to the Queens Bench Division the trustees contended that the tax had not been lost, but had merely been delayed; but the Court rejected that contention, holding that tax was lost within the meaning of Section 88(1) where payment was delayed for an unreasonable period, as a result of the taxpayer's fault.

3.08 It is, of course, not sufficient for the Crown to show that there has been a loss of tax. It must also be shown that the loss was due to the fraud, wilful default, or neglect of the taxpayer, and that the assessment which charges the tax on which interest is claimed was made for the purposes of making good that loss. In J.O'Mullan & Co. v. Walmsley[5] estimated assessments to income tax, made in the absence of accounts, were confirmed by the Special Commissioners, who found that the taxpayer had been guilty of neglect. On appeal to the High Court in Northern Ireland, it was contended that it was for the Crown to establish that the assessments had been made for the purposes of making good a loss of tax, that no evidence had been led by the Inspector to show the purpose for which the assessments had been made, and that accordingly, the Special Commissioners erred in law in reaching their conclusion. The Court decided in favour of the taxpayer, holding that in the absence of evidence of the purpose of the Inspector in making the assessments, the assessments could not be said to have been made for the purpose of recovering tax lost due to the fraud, wilful default, or neglect of the taxpayers. As a result of the O'Mullan decision, which decided that the test of the purpose of the assessment was a subjective test, it became the practice of the Revenue to state, on the face of the assessment or in correspondence, that the assessment had been made for the express purpose of recovering tax lost due to fraud, wilful default, or neglect. However, six years later, the Chancery Division held, in Thurgood v. Slarke[6] that the test to be satisfied was not a subjective test, but the objective test of what the

assessment achieved. If, therefore, tax had been lost due to fraud, wilful default or neglect and the assessment did in fact recover that tax, or part of it, then the assessment had been made for the purposes of recovering the tax so lost. The Crown must, however, do more than merely show that an assessment includes tax which has been lost due to fraud, wilful default, or neglect. It must show that the assessment was made for the purposes of recovering that tax. If, therefore, an estimated assessment is made in amounts greater than those shown on the return and that assessment is increased by agreement, or on appeal, to include tax which has been lost, due to fraud wilful default or neglect, interest under Section 88 cannot be charged unless the Inspector can show that at the time when the original assessment was made, fraud wilful default or neglect where known or suspected. To overcome this difficulty, the Revenue may make estimated assessments for tax lost due to fraud wilful default or neglect while earlier estimated assessments, not so made, are still under appeal. The recent case of Duchy Maternity Ltd. v. Hodgson[7] shows that the Inspector is entitled under Section 29(3) of the 1970 Act, to issue a discovery assessment when an existing assessment is still under appeal.

3.09 Section 88(4) gives the Board of Inland Revenue power to mitigate interest due under Section 88, whether before or after judgement, and entitles it to stay or compound proceedings for the recovery of interest. In practice, this sub-section is used where a taxpayer agrees that interest is due under the section. The procedure, which is more fully described in the context of penalties, is for the taxpayer to make an offer in settlement of the tax and the interest, in return for which the Revenue undertake not to assess the tax or to take proceedings for the interest. Where, however, the taxpayer disputes the Revenue's entitlement to interest under Section 88, the Revenue will be obliged to take proceedings against the taxpayer to recover the interest due. The provisions for the collection and recovery of tax, contained in Part 6 of the Taxes Management Act 1970 are extended, by Section 69, to interest on overdue tax, charged under Part 9. There is no time limit for the commencement of proceedings for recovery of interest.

3.10 The evidence which the Collector of Taxes needs to recover interest charged under Section 88 is a certificate by the General or Special Commissioners that the tax, or some of the tax, charged by an assessment carried interest under the section. To obtain such a certificate, the Inspector or the Board of Inland Revenue must apply to the General or Special Commissioners and at the hearing of the application, the taxpayer (or the personal representatives of a deceased taxpayer) is entitled to be heard. No application for a certificate of interest under Section 70(3) is competent unless the assessment in question has become final and conclusive. This principle is based on the decision of the Attorney General of the Irish Free State v. White,[8] which was approved by the House of Lords in I.R.C. v. Hinchy.[9]

3.11 It is somewhat surprising, given the radical nature of the new interest and penalty provisions introduced in 1960, that the relevant clauses of the 1960 Finance Bill received so little attention in Committee. Clause 52 of the Bill (now Section 88 of the 1970 Act) was afforded only the briefest comment by the Economic Secretary to the Treasury, Sir Anthony Barber who said, in relation to certificates of interest, "The certificate will be evidence of the facts stated, but not conclusive evidence. It will be open to the taxpayer, if he wants, to question this procedure in any Court proceedings." Just what the Economic Secretary meant by this statement is far from clear, but if he meant that the taxpayer could appeal against a certificate of interest he was to be proved wrong. In R. v. General Commissioners of Income Tax for Holborne (exp. Rind Settlement Trustees),[10] the Court confirmed that since the hearing for a certificate of interest was an application, and not an appeal, neither the taxpayer nor the Revenue had any right to demand that the Commissioners state a case for the opinion of the Court. This means that the decision of the Commissioners on an interest certificate is final and conclusive, although it may be possible for the taxpayer to have manifest procedural defects examined by means of a judicial review. Alternatively, if the taxpayer could show in proceedings that the interest certificate was not a true record, the onus would fall on the Crown to establish that the interest shown on the certificate was payable.

3.12 Although an application for a certificate of interest under Section 70(3) of the Taxes Management Act 1970 may be made to either the General or the Special Commissioners, it is understood that the Board of Inland Revenue does not consider that the taxpayer has any right in terms of Section 46 of that Act, to elect as to which body of Commissioners the application should be made. The Board's reason for this view is that Section 46 applies to appeals and proceedings; Section 70(3) on the other hand refers to an application, which is therefore outwith the scope of Section 46. It is considered that this view is correct.

3.13 It seems to be Revenue practice to apply for a certificate of default interest to the Commissioners to whom any appeal against the relevant assessment was made, or in the absence of that appeal, to the General or Special Commissioners as the Board of Inland Revenue may direct, although a request from the taxpayer to have the application made to a particular body of Commissioners is often acceded to.

There are no time limits for applying for an interest certificate.

AGENTS

3.14 It is known that the Inland Revenue take the view, that where a taxpayer has been assessed to recover tax lost due to fraud, wilful default, or neglect, that taxpayer is the person who must pay the default interest, notwithstanding that some other person may well have been guilty of the fault which resulted in interest being due. It follows, therefore, that the Revenue do not normally consider neglect by the taxpayer's agent (e.g. his accountant or solicitor) as a good defence against Section 88.

3.15 It seems that the Revenue have three main reasons for this view. First of all, it is maintained by the Revenue that the phrase "any person" in Section 88 includes a third party acting on behalf of a taxpayer; secondly, the Revenue contends that a solicitor or accountant who prepares income tax returns for the taxpayer is that taxpayer's alter ego; and thirdly, attempts may be made to show that a

taxpayer is vicariously liable for the actions of an accountant or solicitor who acts for him in his income tax affairs.

3.16 The use of the word "agent" to describe a person who prepares income tax returns for others may be misleading. "No word is more commonly or constantly abused than "agent"" - Lord Henshill in Kennedy v. De Trafford.[11] Much of the law on agency is concerned with mercantile agency, where two parties contract with one another through an agent or agents. That relationship, it is submitted,is not relevant to taxation, because the dealings between a taxpayer and the Revenue are not contractual but statutory. The overriding rule of construction of taxing statutes is that they must be interpreted by reference to the words of the Acts, and the onus is clearly on the Revenue to show that the legislation, by its terms, imposes the tax or duty on the subject. Mr. Justice Rowlatt's famous comments in Cape Brandy Syndicate v. IRC,[12] which are quoted in paragraph 1.03, are an early example of the principle. In a later case, Potts' Executors v. I.R.C.,[13] Lord Simond said "It was finally urged that, if this appeal is allowed, an easy way of evading tax will be open to the taxpayer. This is an argument which is of no weight whatever. The question is: What is the fair meaning of words in a taxing Act?". If these principles are applied to Section 88 it is clear that, by its terms, no concept of agency can be imputed except by reference to the phrase "any person". It is submitted, however, that that phrase cannot have its literal meaning otherwise the taxpayer could be prejudiced by the actions or failure of persons totally unconnected with him. If, as seems reasonable, the phrase "any person" is to be restricted, then it is submitted that what it means is "any taxpayer". That meaning would give the sub-section some consistency with the head-note of the section itself,[14] which refers to tax lost "due to the taxpayer's fault". In addition, it would be a meaning consistent with the structure of the section which encompasses income tax, corporation tax and capital gains tax. This is in contrast with the legislation on penalties, in part 10 of the Taxes Management Act 1970, where separate sections are required for income tax and capital gains tax, on the one hand, and corporation tax, on the other, and where, by Section 97(2), accounts submitted on behalf of a taxpayer are to be treated as submitted by him unless he can show that they were

submitted without his consent or connivance. Against this view is the decision in Mankowitz v. Special Commissioners[15] where the taxpayer was held liable for penalties due to the continued delay of his accountant in submitting tax returns. But in that case, the taxpayer knew full well that his accountant was unsatisfactory and did nothing about it, and it seems from the judgement that the Court considered that the taxpayer's failure to find a more satisfactory accountant was itself default. In an earlier case, Clixby v. Pountney[16] the General Commissioners found, in relation to penalty proceedings under Section 47 of the Income Tax Act 1952, that while the taxpayer himself was not guilty of wilful default, his accountant had been guilty. The relevant legislation imposed a penalty on a taxpayer where fraud or wilful default had been committed on his behalf. On appeal to the High Court, the taxpayer contended that he could not be liable for any penalty unless it could be shown that he had known of, or had been a party to, fraud or wilful default committed on his behalf. The taxpayer's contentions were decisively rejected, the Court holding that the words "on his behalf" were not confined to situations where the taxpayer had knowledge of the fraud or wilful default committed by an agent. The decision is of particular interest because the judgement includes commentary on the development of this branch of the law, from Section 125 of the Income Tax Act 1918 to Section 33(1) of the Finance Act 1942, which by its terms, rendered a taxpayer guilty of fraud, wilful default or neglect committed on his behalf. Counsel for the taxpayer emphasised that the introduction of the words "on behalf of" showed that the previous legislation could apply only to fraud, wilful default or neglect committed by the taxpayer himself and not, for example, by an agent acting for him. Although the analysis presented by the taxpayer's Counsel is not fully discussed in the judgement, there is no doubt that the taxpayer failed primarily because the plain meaning of the phrase "on behalf of" included acts of an agent whether or not the taxpayer was aware of them. It is the absence of express words in Section 88, linking the taxpayer and his agent, which suggests that the guilt or fault of an agent of which the taxpayer himself is completely innocent, does not render the taxpayer liable to default interest.

3.17 Revenue contentions that an accountant or other person preparing income tax returns is the alter ego of the taxpayer and that the taxpayer is vicariously liable for the default of his professional adviser really amount to the same argument, and can be dealt with together.

There is no direct authority for the application of the principles of vicarious liability to taxation, and so the analysis must be made by reference to other branches of the law.

3.18 The general rule in Scots law is that a fault or delict binds the perpetrator only, so that a person cannot be held responsible for the actions of another. The underlying principle here is that fault or culpa requires intent and the intention of one person cannot be imputed to another. There are, however, important exceptions to this rule. The exceptions fall into two main categories. First of all, strict responsibility may be imposed on a person by statute so that if an offence is committed, the person upon whom statute lays the responsibility cannot avoid it in any circumstances. For example, strict responsibility normally applies to offences under the Road Traffic Acts, so that if a person commits a road traffic offence, he is guilty irrespective of the reason or circumstances which caused the offence. It is submitted that the doctrine of strict responsibility has no application to taxation obligations, because fraud, wilful default, or neglect all involve some degree of fault, or at least carelessness. This involves a degree of intent, either intent to deceive, as in fraud, or a lack of interest in ensuring that the law is complied with, as in wilful default or negligence. Intent, or lack of it, is irrelevant in cases of strict responsibility. Vicarious responsibility is similar to strict responsibility, in that the person responsible need not have had any guilty intent - if he had, he could be held liable as art and part in the actions of a third party, and therefore his accomplice. Vicarious responsibility is therefore concerned with situations where conspiracy or complicity are not alleged.

3.19 Vicarious responsibility exists in private as well as public law. An employer is vicariously liable for the actions of his employee acting in the course of that employment, even although in breach of his duties. Thus in Lloyd v. Grace Smith & Co.[17] the managing clerk of a solicitor defrauded a client in the course of a property transaction. The Court of Appeal held that the solicitor was vicariously liable for the fraudulent conduct of his employee. Vicarious liability can also arise in actions of an agent on behalf of a principal, although in Scots law, it has been held that not all principals are vicariously liable for the actions of an agent.[18] Given that an accountant or other person, preparing an income tax return for a taxpayer is not his employee, and is unlikely to be his "agent" except in a very loose sense, the question of vicarious responsibility must be approached on general principles. In the leading case of Mousell Bros. Ltd v. London & North Western Railway,[19] Atken J. said that in applying vicarious liability in the absence of express statutory words, the Courts must have regard "to the object of the statute, the words used, the nature of the duty laid down, the person upon whom it is imposed, the person by whom it would in ordinary circumstances be performed, and the person upon whom the penalty is imposed". Two aspects of this judgement are striking, in the context of Section 88. First of all, the express words of the Section imply no vicarious liability, particularly when they are contrasted with other sections which specifically link the fault of an agent to that of the taxpayer. Secondly, the person who would in ordinary circumstances complete a tax return, is the taxpayer himself. Relatively few income tax returns are completed by accountants or others on behalf of taxpayers.

3.20 Finally, since offences dealt with in this thesis are often "quasi-criminal", cases involving vicarious responsibility in quasi-criminal situations are probably most helpful. A recent case on vicarious liability under Section 134 of the Road Traffic Act 1960, G. Newton Ltd. v. Smith,[20] demonstrates the limitation of the concept in quasi-criminal cases. The legislation made it an offence for the holder of a public service vehicle licence "wilfully or negligently" to fail to comply with the conditions of the licence. The accused company held a public service vehicle licence which required it to use a

specified route for its vehicles. A driver employed by the company wilfully took a different route, and the accused was convicted of wilfully failing to comply with the terms of the licence. The grounds for the conviction were that the duty was laid on the company, no penalty was provided for the employee, and that any contravention would normally be committed by an employee. It seems, however, that if the driver had negligently taken the wrong route, no conviction would have been made. The case seemed to closely mirror many of the practical situations in which Section 88 is applied and seems to support the argument that a taxpayer is not vicariously liable, on general principles, for at least the negligence of a person engaged by him to complete tax returns, in circumstances where it would not be unreasonable for him to rely on the competence of that person to do so.

CH. 3

1. Chapter 1 para 1.24
2. F.A. 1986 S.42, Introduction to clarify the point following conflicting decisions by the General and Special Commissioners
2a. See chapter 2
3. 49 T.C. 179
4. 49 T.C. 656
5. 42 T.C. 573
6. 47 T.C. 130
7. 1985 STC 764
8. 38 T.C. 666
9. 38 T.C. 625
10. 49 T.C. 656
11. (1897) A.C. 80
12. 12 T.C. 358
13. 32 T.C. 211
14. The head-note is not an aid to construction - Chandler v. D.P.P. (1964) A.C. 763 per Lord Reid at p.789.
15. 46 T.C. 707
16. 44 T.C. 515
17. (1912) A.C. 716
18. see Mair v. Wood 1948 S.C. 83
19. (1917) 2 K.B. 836
20. (1962) 2 Q.B. 278

CHAPTER 4

PENALTIES

4.01 Penalties for tax offences may be either fixed, that is of a fixed upper monetary limit, or tax-geared, that is, based on the amount of tax lost. A tax geared penalty is often imposed in addition to a fixed penalty.

4.02 The present penalty code can be traced to the origins of income tax. Section 197 of the Income Tax Act 1842 provided that where a Schedule D assessment had been made in excess of the income returned by the taxpayer, or where the Commissioners had discovered that income had not been fully assessed to tax, a penalty of £20 plus three times the tax charge could be imposed, unless the taxpayer could show to the satisfaction of the Commissioners that the omission did not "proceed from any fraud covin art or contrivance or any gross or wilful neglect", the words quoted having themselves been taken from the Act of 1799. The Commissioners were also empowered to impose a penalty not exceeding three times the amount of tax with which a taxpayer should have been charged if he neglected or refused to deliver a "statement or schedule".

4.03 Maximum penalties of treble the tax which ought to have been charged remained on the Statute Book until 1960. The change to the present system was as a result of the decision of the House of Lords in I.R.C. v. Hinchy.[1] Mr. Hinchy, a retired Officer of Customs & Excise, returned Post Office Savings Bank interest of £18.30 when the correct amount of interest credited to his account for the relevant year was £51.29. The Crown's claim to a penalty was based on the words of Section 25(3) of the Income Tax Act 1952, which stated that the amount due by the taxpayer should be "treble the tax which ought to be charged under this Act", plus a fixed penalty of £20 and, of course, the tax itself. The decision of the High Court was that the penalty due was £20. In the Court of Appeal, it was held that the penalty was £62.75. The House of Lords, however, decided that the penalty due was £20 plus treble Mr. Hinchy's total tax liability for the year, giving a combined

liability of £438.72. The Crown had urged that this interpretation of the phrase had been applied ever since it had been used in a tax statute. There was, however, some doubt as to when the words were first used. Lord Radcliffe thought that the first use had been in Section 181 of the Income Tax Act 1805, although he alluded to the possibility of the Act of 1799 as having been the source. Lord Reid and Lord Keith both referred to the origin of the phrase in the earliest of the Income Tax Acts. In fact, the phrase was first used in Section 92 of the Income Tax Act 1799. What is interesting, however, is not so much the origin of the section as the fact that the original words could never have resulted in the interpretation put by their Lordships on Section 25 of the Income Tax Act 1952 which led to a result so absurd that the law was amended by the Finance Act of the same year. Section 92 of the 1799 Act provided that the penalty exigible should be "double the amount of the charge which ought to have been made on such person (if no such charge shall have been made), and if any such charge shall have been made which shall be less than the charge which ought to have been made on such person, then such person shall be assessed and charged for the purposes of this Act over and above such former charge, double the amount of the difference between the sum with which such persons shall have been charged and the sum with which he ought to have been charged". The effect of the 1960 amendments, which form the basis of the present penalty code, was therefore to bring the law into line with what it had been when income tax was first introduced over 150 years earlier.

PENALTIES FOR FAILURE

4.04 The law provides for both fixed and tax-geared penalties where a taxpayer has failed to meet a requirement of the Taxes Acts. Section 7 of the Taxes Management Act 1970 requires every person who is chargeable to income tax for any year of assessment, and who has not made a return of his income or gains for that year, to give notice to the Inspector that he is so chargeable. The notice must be made within one year after the end of the year of assessment, and failure can result in a penalty not exceeding £100. Section 10 of the 1970 Act contains a similar obligation in relation to corporation tax while

Section 12 applies these provisions to capital gains tax. The obligation of a taxpayer to give notice of liability to tax was introduced in 1942. Before then, two forms of notice were in force, both dating from the Income Tax Act 1842. The first was a general notice under, latterly, Section 98 of the Income Tax Act 1918. This was usually referred to as the "Church Door" notice, because it was affixed to the local church door or other public place. The other notice, under Section 99 of the 1918 Act, was a particular notice incorporated in the income tax return form. On consolidation Section 99 found its way into Section 115 of the Taxes Management Act 1970.

4.05 Part 3 of the Taxes Management Act 1970 requires certain persons to make returns of income paid to, or to provide information about, third parties. The provisions deal with, inter alia, fees and commissions paid to third parties, employees' emoluments, and interest paid or credited by banks. In some cases, fixed penalties may be charged by virtue of the section which imposes the requirement or responsibility. But for many of the provisions, Section 98 provides for a penalty not exceeding £50 plus £10 for each day after the failure has been declared an offence by the Court or by the Commissioners. Where the failure was due to neglect or wilful default, the penalty is a maximum of £250, while in the case of fraud, it is a maximum of £500. Fixed penalties under Section 98 are not to be imposed for failure to comply with a notice where the failure is remedied before penalty proceedings are commenced. However, because of the structure of Section 98, it is not always possible to avoid a penalty by putting right a failure before penalty proceedings start. The reason is that the relieving sub-section (3), applies only to returns which are required on notice from the Inspector, such returns being set out in the first column of the Table at the end of Section 98. The second column of the Table refers to measures under Acts and Regulations for which returns are required without notice. A failure, for whatever reason, to furnish a return under the second column results in a penalty, whether or not the failure is put right before penalty proceedings are commenced. In practice, a common offence under Section 98 is a failure, by an employer, to make a return required under Section 204 of the Taxes Act 1970. Section 204 provides for the collection of tax

from wages, salaries, and other emoluments of employed people under the "pay as you earn" system. Section 204(2) permits the Board of Inland Revenue to control the PAYE system by means of Regulations, the principle such measure at present in force being the Income Tax (Employments) Regulations 1973. Regulation 30 of the 1973 Regulations requires an employer, at the end of each fiscal year, to make a return in respect of each employee of the amount paid to that employee in that year, together with the income tax deducted from it. These returns are required to be made not later than fourteen days after the end of the fiscal year. Where such a return is incorrect, (because, for example, the employer has failed to treat as an emolument a reimbursement of expenses not covered by a dispensation,) the obligation imposed by Regulation 30 will not have been met. If the error is discovered subsequently, for example, as a result of a PAYE inspection, a penalty will be due under Section 98 in respect of that incorrect return, even if the return was made innocently and a correct return is made before penalty proceedings start. It is the view of the Revenue that Regulation 30 requires separate returns to be made in respect of each employee so that if returns for all employees are incorrect, the maximum penalty for innocent error is £50 per employee, or £10 a day, for each employee, after the date on which the Commissioners have declared that an offence has occurred. This is the basis on which the Revenue can claim very large penalties for PAYE offences. It is, however, to be observed that the nature of the PAYE procedure does not allow for interest under Sections 86 or 88 of the 1970 Act to be charged on overdue tax.

4.06 Section 53 of the Taxes Management Act 1970 permits the Commissioners to award penalties summarily in connection with offences under Section 51 or 52, notwithstanding that proceedings for the recovery of penalties have not been commenced. Section 51 gives the Commissioners power to obtain information from an appellant in a tax appeal, including books, accounts, and other documents, being information needed to determine the appeal. The section also permits an Inspector or other Officer of the Board to take copies of any information which the Commissioners have requested. The information is to be obtained by a notice served on the taxpayer or other party to the

appeal (but not the Inspector) and the maximum penalties are set in Section 98(1) and (2). Section 52 is concerned with evidence, and provides for the amount of a summary penalty against a person who, after being duly summoned, neglects or refuses to appear before the Commissioners, or refuses to take the oath, or refuses to answer questions concerning the appeal. The obligation is not, however, imposed on an agent or employee of the taxpayer who cannot be obliged to answer any question to which he objects. The maximum penalty for an offence under Section 52 is £50.

4.07 Sections 93 and 94 of the Taxes Management Act 1970 provide for both fixed and tax-geared penalties for offences of failure resulting in loss of tax. Section 93 deals with a taxpayer's failure to comply with a notice served on him under Sections 8 or 9 of the Taxes Management Act 1970 or Section 39(3) of the Taxes Act 1970. Sections 8 and 9 of the Taxes Management Act 1970, as extended by Section 12 of that Act deal with returns of income and chargeable gains. Section 39(3) of the Taxes Act 1970 empowers the Board to obtain returns of total income from a husband or a wife in a case where they have elected for separate assessment. Section 94 is concerned with failure to comply with Section 11, that is, with failure to make corporation tax returns.

4.08 It is to be noted that a failure under Section 7 is covered neither by Section 93, nor by Section 95 (which deals with incorrect returns made fraudulently or negligently). This produces the odd result that failure to notify the Revenue of chargeability gives rise to a fixed penalty of £100 only, whereas a taxpayer who tells the Inspector that he is chargeable to tax, but fails to send in a return, may be liable to a much higher penalty, based on the tax due.

4.09 Where the taxpayer's failure to comply with a notice is not a prolonged failure, the penalty is not tax geared. Section 93(1) provides that in the first instance the penalty payable for failure is to be a maximum of £50 plus £10 for each day during which the failure continues after it has been so declared by the Commissioners or the Court. The taxpayer can avoid the fixed penalty in one of three ways:-

(a) If, in the course of proceedings to recover a penalty, the taxpayer can show that he had neither income nor chargeable gains to be included in his tax return, the penalty cannot exceed £5 (S.93(7)).

(b) In terms of Section 118(2) a taxpayer will not be regarded as having failed to comply with a notice served on him within the time allowed by the notice, if he can show that the Revenue allowed him extra time to comply with the notice, or that he had a reasonable excuse for his failure and put the failure right without unreasonable delay after the excuse has ceased. This defence is more fully discussed in the chapter on Fraud, Wilful Default and Neglect.

(c) If, before proceedings commence, the taxpayer puts right the failure, the Revenue cannot obtain penalties under Section 93(1).

4.10 Where the failure continues after the end of the fiscal year following that during which the notice was served Section 93(2) says that the penalty payable is to be a maximum of £50 plus the total amount of the tax charged on income or chargeable gains which were omitted from the return, and which are assessed after the end of the year next following the year of assessment in which the notice was served. In the case of a taxpayer who has died, the tax-geared penalty is calculated by reference to tax assessed on the deceased's personal representatives. A taxpayer cannot avoid a tax-geared penalty under Section 93(2) by putting his failure right before penalty proceedings start. It is to be noted that the penalty is based on the tax which "is assessed". Such an assessment would normally be made after allowing any reliefs or deductions to which the taxpayer may be entitled. The recent case of Khan v. First East Brixton General Commissioners[1a] shows that the assessment can only be reduced by reliefs to which the taxpayer is entitled when the assessment is made. In Khan the taxpayer objected to a tax-geared penalty on the grounds that he had another business which had sustained a loss, and that it might be possible to reduce the assessment by carrying back the loss under Section 30 of the Finance Act 1978. The taxpayer's contention was dismissed. Tax was payable on the due date after the making of an

assessment. The fact that a future claim might reduce the assessment was irrelevant.

4.11 The decision in Moschi v. Kensington General Commissioners[2] shows that the obligation under Section 93(1) is not simply an obligation to send back the income tax return form which the Inspector has issued. It is an obligation to comply with the requirements of Section 8, that is, to make a return of income and gains computed in accordance with the Income Tax Acts and specifying each source of income and gain and the amount from each source. In Moschi, the taxpayer delivered forms of return in which he had inserted in four places, the words "not yet finally ascertained", and against "Dividends Already Taxed" the words "not exceeding £5" without specifying any source. The Court upheld the findings of the Commissioners that the taxpayer had not complied with his requirements under Section 93(1) and that that was a failure within the meaning of the section.

4.12 For the Crown to obtain a tax-geared penalty, it is not sufficient for the Inspector to show that there has been failure; he has to show that the failure continued beyond the end of the year following that in which the notice was served. Since income tax return forms are normally issued early in the fiscal year, this means that the taxpayer will, in practice, have almost two years within which to complete his requirements under Section 8 without the risk of incurring a tax-geared penalty. The Inspector must also show that the assessment by reference to which the tax-geared penalty is calculated was made after the end of the year next following that in which the notice was served. The phrase "year next following" will have different meanings, depending on whether "next" governs "following", or "following" governs "next". The word "next" is an abbreviation of the word "nearest".[3] The phrase "year next" could, therefore, signify the nearest year before or the nearest year after a particular year. Thus if "next" governs "following" then the "year next following" must be the nearest year following a particular year, that is, the immediately following year. It would follow, therefore, that if a notice was issued in the fiscal year 1980/81 then the "year next following in the year of assessment in which the said notice was served", within Section

93(2)(b) would mean the year 1981/82. But if this interpretation is correct, is creates an inconsistency with the opening words of Section 93(2) which refer to a failure continuing "after the end of the year of assessment following that during which the notice was served". That year must be the immediately following year, that is, in the example given, 1981/82 and the effect would be that the "following" year and the "next following" year would be the same year. It is submitted that that cannot be so. Apart from the inconsistency, the only support for treating "following" as governing "next" is to contrast it with the "next before" year. It is submitted that no penalty could ever be based on an assessment issued after the end of the year next before the year in which the notice was served because that interpretation renders the section meaningless. It is therefore submitted that the word "next" governs "following" so that the "year next following" is the year after the following year, that is, two years from the year in which the notice was served. If this view is correct, it means that, in the example given, a tax-geared penalty in respect of failure to comply with a notice issued in 1980/81 could only be based on an assessment issued after the end of 1982/83, being the year next following 1980/81.

4.13 It is believe that the opinion expressed in the previous paragraph is not shared by the Revenue. The Revenue view seems to be that the phrases "next following" must be contrasted with "next before". Therefore, according to the Revenue, the "next following year" is merely the next year. This interpretation accords with the explanation given, in the Committee debates on the 1960 Finance Bill, by the Solicitor-General, Sir Jocelyn Simon. But the Solicitor's analysis was confined to what is now Section 93(2)(b) of the 1970 Act. Sub-section (2) was not fully analysed, and the relationship between the "following" year, and the "next following" year, was not considered.

4.14 Section 93 deals with returns for income tax or capital gains tax. Section 94, on the other hand, is concerned with corporation tax. Under that section, a company's failure to deliver a return, after having been served with a notice to do so, gives rise to a penalty of

£50 plus £10 a day for each day after which the failure has been so declared by the Court or the Commissioners but, as in Section 93, this penalty may be avoided if the failure is put right before penalty proceedings start, or if, in terms of Section 118(2), the company can show that it was given extra time, or had a reasonable excuse for its failure. If the company can show that it had no profits to be included in a return, the penalty is not to exceed £5. If the company's failure continues after the end of two years from the date on which the notice was served the penalty is a maximum of £50 plus the total amount of corporation tax charged on assessments based on the profits which should have been returned but were not, and made after the end of the two year period. The clear words of Section 94(2), in imposing a tax-geared penalty on a company, are inconsistent with the suggested interpretation of "next following year" in Section 93(2). It is to be observed, however, that while Section 93(2) refers to the "following" and the "next following" year, Section 94(2) deals, quite simply, with a two year period and so there is nothing, it is submitted, in Section 94(2) which is an aid to the construction of Section 93.

PENALTIES FOR INCORRECT RETURNS

4.15 Where a taxpayer, fraudulently or negligently, delivers an incorrect return for income tax or capital gains tax purposes, when required to do so by notice under Section 8 or 9 of the Taxes Management Act 1970 (or Section 39(3) of the Taxes Act 1970) or makes an incorrect return or declaration in connection with a claim for relief from income tax or capital gains tax, or submits incorrect accounts in connection with an income tax or capital gains tax liability, Section 95 of the 1970 Act provides for a maximum penalty of £50 plus the amount of the difference between the income tax or capital gains tax payable for the "relevant years of assessment" and the amounts which would have been payable for those years if the returns or accounts had been correct. In the case of fraud, the penalty is a maximum of £50 plus twice the difference for the "relevant years". The relevant years of assessment are the year of assessment in which the return or accounts were submitted, any preceding year of assessment, and the "next following" year of assessment. It is thought that the

phrase "next following" in this context means the immediately following year, that is, the year in which the returns or accounts are submitted to the Revenue. The Revenue are thus protected against possible difficulties if income is assessed in a year other than that for which a return or accounts are submitted. For example, special rules apply in the first year of a source of income assessable under Schedule D Cases 1 to 5, whereby income for the first fiscal year of the source forms the basis of assessment for the first three fiscal years.[4] A return showing income from a new source taxable under Cases 1 to 5 of Schedule D would normally be delivered to the Revenue not earlier than in the year following that in which the source arose. Since the "relevant years of assessment" include the year immediately following that of the delivery of the return, then each of the first three years of assessment of the new source will be within the scope of Section 95, should the return or accounts be incorrect due to fraud, wilful default or negligence.

4.16 Section 96 provides for tax-geared penalties on companies or bodies corporate liable to corporation tax, in respect of incorrect returns, statements, or accounts made fraudulently or negligently. The penalty is a maximum of £50 plus the difference between the corporation tax payable by the company for the accounting period or period covered by the incorrect returns, statements, or accounts and the amounts which would have been payable if the returns or accounts had been correct. In the case of fraud, the maximum penalty is £50 plus twice the difference in tax.

4.17 Sections 95 and 96 deal with returns or accounts submitted "fraudulently or negligently". In R. v. Havering Commissioners (ex parte Knight)[5] the Court concluded that that phrase included wilful default. Lord Justice Russell[6] said "It would be, in my view, quite absurd to hold under Section 95 that it embraces a careless breach of duty - that is to say negligence, but not a careful breach of duty - that is to say wilful default". The Court did not reach a conclusion, however, on whether wilful default was implied as part of fraud, or as part of negligence. The important point here is that the maximum penalty for fraud is £50 plus twice the excess tax, whereas for

negligence, the penalty is a maximum of £50 plus the excess tax itself. It is understood that in practice the Revenue do not seek penalties in excess of the amount of the tax on the difference except in cases where fraud is alleged.

4.18 It is submitted that the word "negligently" implies negligence and not mere neglect. This distinction is important because the definition of "neglect" in Section 118(1) encompasses both negligence and failure. The restricted interpretation must follow, it is submitted, because Sections 93 and 94, on the one hand, and Sections 95 and 96, on the other, are mutually exclusive, in that a taxpayer cannot be accused of having fraudulently or negligently submitted incorrect returns or accounts when he failed to submit them at all. However, the border line between a submitted return which is incorrect due to an omission, and a failure to comply with Sections 8 and 11, is a narrow one. The obligation under Section 8 is to make a complete return of income and gains showing each source, and the amount from each source, separately. The obligation under Section 11, in relation to corporation tax, is to make a return of "profits" that is income computed by reference to each source (and the amount of each source), chargeable gains or allowable losses, and charges on income to be deducted from profits. A person who fraudulently or negligently submits a return which is wrong fails to comply with his obligation to make a return, as described in Section 8 and 11. He is therefore guilty under both sets of provisions. It seems, however, that the correct position is this. If the taxpayer has not sent back his income tax return, the appropriate penalty sections are Sections 93 and 94. If he has sent back an incomplete return showing entries against particular items "to be agreed" or "figures to follow" then he has failed to comply with the obligation under Section 8 or 11, and once again Sections 93 and 94 are the appropriate penalty sections. But if he has submitted an income tax return or accounts showing income or gains from particular sources which are wrong due to fraud, wilful default or negligence, then the appropriate penalty sections are Sections 95 and 96. The question to be asked is, therefore, has information been supplied? If the answer is "Yes" but it is wrong, then incorrect returns have been submitted. If the answer is "No"

because no income or gains were shown, then there has been a failure to comply with the requirements to make a proper return.

ASSISTING IN MAKING AN INCORRECT RETURN

4.19 Section 99 imposes a penalty not exceeding £500 on any person who assists in or induces the making or delivery, for any purposes of tax, of any return or accounts which he knows to be incorrect. When the predecessor of Section 99 was introduced, by the Finance Act 1960, doubts were expressed in Parliament on its efficacy, and, in particular, as to its interaction with the penalty provisions for fraud. The Attorney-General, Sir Reginald Manningham-Buller, clearly regarded the Section as of limited application, and in particular, expressed the view that he could imagine no case where, for example, Section 99 would be applied to a guilty accountant, where a prosecution for fraud was an alternative.

Almost 20 years later the Attorney-General's assertion was to be proved wrong.

4.20 The phrase "for any purposes of tax" was considered in Lord Advocate v. Ruffle,[7] the only reported case on this section. Mr. Ruffle, a chartered accountant, was the auditor of a company in the printing industry. It was the company's practice to value stock-in-trade, for the purposes of its annual accounts, at the lower of cost or market value, but to disregard the last few stock sheets in any year, so that the total trading stock shown in the account was valued at a figure below the lower of cost or market value, the minimum valuation acceptable for taxation purposes. When this practice came to light, the Revenue brought an action against the auditor under Section 99, on the grounds that he had assisted in the preparation of accounts for the purposes of tax which he knew to be incorrect. In fact, Mr. Ruffle did not submit the accounts of the company, or computations of tax liabilities, to the Inland Revenue, as this was done by the company's own staff. The Court of Session therefore decided that no penalty was payable by Mr.Ruffle, on the footing that, although he had assisted in the preparation of accounts which he knew to be incorrect,

he had not done so for the purposes of tax. Lord Jauncey in the Outer House said that the clear intention of Parliament was that tax must have been the sole or one of the purposes for the making of the accounts. The fact that accounts were used for the purposes of tax was not sufficient.

4.20a A further weakness in Section 99 is that it is limited to "returns and accounts", and not to other information. This weakness may, however, be more apparent than real, since the section would presumably extend to information given in support of a return or accounts. Nevertheless, it would appear that the wording is not as comprehensive as it might be.

4.21 Despite the limitations on Section 99, as explained in the Ruffle case, the section is still a formidable one which the Revenue will use when circumstances warrant it. Lord Jauncey seems to have been misinformed by Revenue Counsel who said that Ruffle was the first occasion on which the Revenue sought to enforce the section, or the previous enactments of it. It is understood that the Revenue regularly bring cases under Section 99 before the General or Special Commissioners. The reason is that an award of a penalty against a person under Section 99 entitles the Revenue, in terms of Section 20A(1)(b) of the Taxes Management Act 1970 to take possession of documents or other information relating to any of his clients. Moreover, the scope of the section is wide. There is no need for the Revenue to show that the incorrect accounts produced a loss of tax, because the penalty under Section 99 is not tax-geared, and the standard of accuracy needed to produce "correct" accounts might well be higher than the standard normally implied by accounts showing a true and fair view. Thus, for example, the omission or mis-classification of an item not material by reference to accounting standards might well be an error of sufficient size to give rise to an offence under Section 99.

PARTNERSHIPS

4.22 Section 152 of the Taxes Act 1970 says that income tax on the profits of a trade or profession carried on by two or more persons in partnership is to be computed and stated jointly, and a joint assessment on partnership profits is to be made in the partnership name.

4.23 In Income Tax Commissioners v. Gibbs[8] the Revenue, following a change in the partnership of a firm of stockbrokers, assessed the old firm and the new firm as two separate taxing entities. The House of Lord upheld the Revenue's approach. Lord MacMillan said[9] "Justification is thus not wanting for the view.....that for taxing purposes a firm is treated as an entity distinct from the persons who constitute the firm". Other decisions which emphasise this principal include Reynolds & Gibson v. Crompton[10] and Watson & Everitt v. Blunden.[11] A contrary view was, however, expressed by Lord Denning in Harrison v. Willis Brothers,[12] as follows:- "It is suggested that for taxing purposes a partnership firm is treated as an entity distinct from the persons who constitute the firm but I do not think that this is correct.....the partnership firm is not an entity for taxing purposes or any other purposes. Its name is simply a convenient way of describing the persons who constitute the firm."[13] Lord Denning's comments, however, were obiter comments in a case which was concerned with the complex question of the machinery of assessment following a back duty enquiry into the affairs of a two-partner partnership where one of the partners had died. It is not, therefore, thought to overturn the view expressed in the Gibbs case. In a very recent case on partnerships, MacKinlay v. Arthur Young McClelland Moores & Co.[13a] the Court of Appeal upheld a finding of the Special Commissioners, that expenditure incurred by a partner in relocating to another office, was wholly and exclusively incurred for trading purposes, on the footing that the firm was an entity separate from the partners. The case will go to the House of Lords. It therefore seems clear that in England, for the special purposes of income tax, a partnership is a separate unit of assessment, and the partners are jointly liable for the tax of the firm. In Scotland, a partnership is a recognised legal entity for

all purposes. In Mair v. Wood[14] Lord President Cooper said[15] "It is fundamental to the Scots law of partnership that the firm is a legal persona distinct from the individuals who compose it. ..... Partners are, of course, liable jointly and severally in a question with a firm creditor for the obligations of the firm.....the partners being in substance guarantors or cautioners for the firm's obligations and each being entitled on the payment of a firm debt to relief pro rata from the others".

4.24 The legal position of partners and partnerships in relation to taxation is subject to a special rule in Section 118(3), concerned only with the Revenue's power to make out of time assessments for neglect, and for penalties within Part 10 of the Taxes Management Act 1970. Section 118(3) provides that in Scotland as well as England, tax charged on such an assessment is to be treated as an assessment on the partners, as though the tax charged by the assessment was charged on and payable by them. This seems to convert the liability for penalties under Part 10 into a joint liability of the partners themselves.

4.25 In England as well as Scotland, the partners in a firm may become liable to penalties for failure or for rendering incorrect returns or accounts due to fraud, wilful default or negligence. A failure to comply with a notice under Section 9, that is a notice served on the first-named or precedent acting partner, affects all the partners, since that obligation is to make a return under Section 8 on all the partners' behalf. Any resultant penalty charged under Part 10 will therefore be by law a joint liability of the partners of an English firm, and by Section 118(3) a joint liability of the partners of a Scottish firm. The same position would seem to apply to an offence under Section 95. It is thought to be impossible for a partner to avoid a penalty under Section 95 by maintaining that another partner submitted false accounts, because one partner, acting on behalf of a firm, acts as an agent for all the partners.[14a] In addition, Section 10 of the Partnership Act 1890 provides that where, as a result of a wrongful act or omission by a partner acting in the ordinary course of the firm's business, a penalty is incurred, the firm is liable for that penalty to the same extent as the partner who was responsible for the

unlawful act or omission. Default interest under Section 88 is a joint liability in England, and a joint and several liability in Scotland, because the interest forms part of the assessment and the liability therefore forms part of the liability for the tax itself. Despite the legal position, it is Revenue practice in back duty settlements, to ensure that the partners are jointly and severally liable for the amount offered in settlement.

4.26 In practice, it would seem equitable to allocate penalties among partners according to their respective shares of the partnership tax on which the penalty was charged. But it is by no means certain that this is correct. There appears to be no reason why a penalty, or interest on overdue tax, should not be treated among the partners as a partnership expense and allocated according to profit sharing ratios. Section 10 of the Partnership Act 1890, provides that the firm is liable for any penalty incurred by any partners in performing the duties of partnership. In these circumstances, it would seem to be the firm which meets the penalty, and not the partners as individuals.

RECOVERY OF PENALTIES

4.27 Unlike default interest under Section 88, which is "carried" by the assessment to make good the tax lost, the procedure for the recovery of penalties is separately provided for in Section 100 of the Taxes Management Act 1970.

Section 100 permits an Inspector to commence penalty proceedings before the General Commissioners for a penalty under Section 93(1) or 98(1) that is, for failure. The maximum penalty which can be so obtained under Section 93(1) is £50. Penalty proceedings, in all other cases governed by Section 100, may only be commenced by order of the Board of Inland Revenue. Proceedings are to be instituted either in the name of an officer of the Board or, in Scotland, in the name of the Lord Advocate, and may be commenced before the General or the Special Commissioners or before the High Court or, in Scotland, before the Court of Session as Court of Exchequer in Scotland. An application to the Commissioners for an award of a penalty is by way of information in

writing to the Commissioners who may summon the taxpayer to appear before them. Any penalty awarded is to be collected in the same way as though it were tax charged by an assessment. The Commissioners or the Court may award penalties, whether fixed or tax-geared, for less than the maximum amount. This differs from default interest, where the Commissioners have no power to mitigate the full amount due.

4.28 A penalty awarded summarily under Section 53 is due and payable as though it were tax charged in an assessment, notwithstanding that proceedings for its recovery have not been commenced.

4.29 Where a person has died, penalty proceedings which could have been taken again him when he was alive, may be commenced, or continued, against his personal representatives. Any penalty awarded is a debt due from the deceased's estate. The relevant legislation is contained in Section 100(5) of the 1970 Act and clarifies doubt created by the decision of the Court of Appeal in A-G v. Canter.[16] In that case, a taxpayer who was liable to penalties under Section 30 of the Income Tax Act 1918, died before penalty proceedings were commenced. Although the Court held that the Revenue could commence penalty proceedings against the deceased's executors, some emphasise was placed by Sir Wilfred Greene M.R. on the fact that the penalties were, in that case, fixed. Section 100(5) now makes the position clear that penalty proceedings against personal representatives of a deceased's taxpayer can be commenced whether the penalties are fixed or tax-geared.

4.30 In penalty proceedings, the evidence needed by the Commissioners or the Court of the tax charged, is an assessment or assessments which are final and conclusive.[17] This means that proceedings are premature until the relevant assessment has become final and conclusive, as was confirmed in the Irish case of A-G v. White.[18] It is, however, open to the Commissioners to determine an assessment, and immediately thereafter, to award penalties in respect of that assessment.

4.31 The decision of the Commissioners in penalty proceedings under Section 100 may be appealed against by either party on a question of

law, and by the taxpayer against the amount of any penalty awarded. Appeals are to be heard by the High Court, or in Scotland, the Court of Session as Court of Exchequer. The Court has no power to vary the award of a penalty in an appeal on a question of law - the Court must either set the decision aside, or confirm the amount of the penalty awarded by the Commissioners. Where the taxpayer appeals to the Court against the amount of a penalty, the Court has the power to confirm the decision, or to increase or reduce the amount of the penalty.

4.32 The procedure for an appeal against the summary award of penalties under Section 53 differs from an appeal under Section 100. It seems that either party may under Section 53 appeal against the Commissioners decision to the High Court, or in Scotland, the Court of Session as Court of Exchequer. There is, however, no reference to an appeal on a point of law in Section 53, which merely provides that the decision of the Commissioners may be confirmed or reversed, and that the penalty may be reduced or increased.

4.33 Appeals against assessments to tax, are by way of a case stated for the opinion of the Court. Appeals against the award of penalties under Section 53(2) was considered by the English High Court in the recent case of Q.T. Discount Food Stores Ltd. v. Warley General Commissioners.[19] In that case, the taxpayer company had failed to comply with notices under Section 51 and had summary penalties awarded against it by the General Commissioners. Mr. Justice Vinelott, in a lengthy judgement discussing the company's appeal, drew a distinction between appeals under Section 100(6), which are restricted to questions of law and the amount of a penalty, and appeals under Section 53(2), which were not so restricted. The Judge confirmed that except where appeals are restricted to questions of law, the Court is not precluded from considering the evidence of the parties. Applying this principle to appeals under Section 100(6) it would appear that the Court can only consider the law in the context of the evidence admitted or proved before the Commissioners. In Salmon v. General Commissioners for Havering[20] Lord Donovan, in the Court of Appeal, said in relation to a

Section 100(6) appeal "Finally, we are asked to mitigate the penalty on the grounds that domestic expenditure met out of cash receipts - in other words met out of the till - had been grossly over-estimated. Speaking for myself I find it quite impossible even to embark on that enquiry. This depends on evidence, upon going into facts and figures, and it is not for us to do that. One can see this jurisdiction being exercised in a case where plainly something has gone wrong, but for myself I am not in that position with regard to this domestic expenditure nor could I put myself in that position without conducting some sort of accountancy investigation, which it is not the function of this Court to conduct." So an appeal under Section 100(6) proceeds in broadly the same way as an appeal by Case Stated, that is, on the law, including the conclusions in law drawn from the facts found. An appeal under Section 53(2) is, however, quite different. Under the Rules of the English Supreme Court Order 55 Rule 7(2) an express power is given to permit an appeal by way of rehearing, except where the statute provides otherwise. The English Court therefore decided in Q.T. Discount that the findings and reasons of the Commissioners are to be treated as evidence which can be challenged by either party. If the primary facts found by the Commissioners are challenged, the rules of the English Supreme Court permit further evidence to be adduced in such manner as the Court directs. It is submitted that the position in Scotland would be the same.

4.34 Appeals by taxpayers against the quantum of penalties awarded have only rarely been successful. In Taylor v. Bethnal Green General Commissioners[21] penalties of £1,198.55 imposed by the Commissioners for "gross negligence" in failing to make proper returns were reduced to £1,000 by the Court, on the basis, so it seems, that the taxpayer had a life policy which was likely to yield £987. In Stableford v. Liverpool General Commissioners,[22] penalties were sought from a taxpayer, under Section 93(1), in respect of his failure to make returns of income for the two years ended April 5, 1980. The taxpayer did not appear, nor was he represented, before the General Commissioners who awarded penalties against him of almost £2,000. On appeal to the High Court the taxpayer stated that he was an undischarged bankrupt and that the Inspector had agreed not to press him for any return for the period up

to April 5, 1978. No returns had, in fact, been submitted for 15 years. Mr. Justice Vinelott, who described the case as "wholly exceptional", decided that the Inspector's failure to explain the circumstances of the case had misled the Commissioners, who had awarded a penalty which was excessive. The penalty was therefore reduced to £100, with additional costs of £250. The authorities show, however, that the amount of penalties awarded will only be interfered with if the Court can be satisfied, as in the Stableford case, that the Commissioners were not justified in reaching the conclusion which they reached. Fresh evidence may, of course, be put forward,[23] but if the Court proceeds on the Commissioners note of findings, it is unlikely that it will feel justified in varying the award previously given. A recent example is Sen v. IRC[24] where penalties of less than the maximum were imposed by the Commissioners. Although the Court regarded the penalty imposed as lenient, the amount payable was not varied. The general principle which the Court should adopt when considering the quantum of a penalty was stated by Vinelott J. in Lear v. Leek General Commissioners[24a] when he said that the Court should only interfere with an award when the penalty was plainly disproportionate to the possible fault. In the recent case of Broat v. Wells General Commissioners[24b] Scott J. said that it was desirable that a uniform approach to penalties should be adopted by Commissioners in different parts of the country. The judge compared Lear,[24a] with Willey v. IRC[24c] to illustrate differing approaches of different Commissioners. It is submitted, however, that differences will always occur, unless legislation is introduced to restrict the discretion open to Commissioners.

MITIGATION OF PENALTIES

4.35 The term "back duty" is applied to tax lost due to fraud, wilful default or neglect, and a "back duty settlement" is the amount which a taxpayer offers the Revenue, in consideration for the Revenue not taking formal proceedings against for the recovery of tax, interest and penalties. The Revenue's power to mitigate penalties is contained in Section 102 of the Taxes Management Act 1970 and gives the Board complete discretion to mitigate a penalty, or entirely remit it before

or after judgement, and to "stay or compound" any proceedings for the recovery of a penalty. Section 88(4) gives the Board similar powers in relation to default interest. The great majority of back duty cases are settled in this way, by negotiation, between the taxpayer, or his professional adviser, and an Inspector on behalf of the Board. In serious cases, an Inspector from the Revenue's Enquiry Branch will have carried out the investigation, and will negotiate with the taxpayer on the Board's behalf. Normally, the Inspector will ask the taxpayer to complete a Certificate of Disclosure certifying that he has made a complete disclosure of all information relevant to his taxation affairs. In R. v. Hudson,[25] a taxpayer who had submitted a Certificate of Disclosure which he knew to be wrong was held to be guilty of fraud.

4.36 The power of the Revenue to reach informal settlements with taxpayers in back-duty cases was considered in the English High Court in A-G v. Johnstone.[26] In that case, a taxpayer who had entered into a voluntary agreement with the Revenue for a voluntary settlement, following a back-duty enquiry, failed to meet the final two instalments of the settlement. In giving judgement in favour of the Crown, Mr. Justice Rowlatt described the Revenue's practice which was based on Section 222 of the Income Tax Act 1918 (now Section 102 of the Taxes Management Act 1970) as "An extremely beneficial and merciful practice to the parties" which enabled taxpayers "To put their cards on the table and make arrangements with (the Revenue) to pay something in respect of the penalties on account of the injustice which they have inflicted on the other taxpayers....." More recently, the question of the Board of Inland Revenue's right to reach compromises with taxpayers was considered by the House of Lords in IRC. v. National Federation of Self Employed & Small Businesses Ltd.,[27] a case concerning the Board's right to grant a general tax "amnesty" to individuals employed in the printing industry where there was clear evidence that PAYE irregularities had occurred. The House decided unanimously in favour of the Crown, emphasise being laid on the wide discretion placed by Parliament on the Board of Inland Revenue, by the Inland Revenue Regulation Act 1890 and the Taxes Management Act 1970 to make such arrangements as were necessary for the good management of the taxes under the Board's jurisdiction.

4.37 The final monetary settlement will consist of a composite sum which the taxpayer offers the Crown in exchange for immunity from prosecution, immunity from penalty and interest proceedings, and an undertaking by the Board that he will not be assessed to the tax. The form is drafted in such a way so as to ensure that, when it is signed, it is binding on the taxpayer as a debt due under contract. In A-G v. Midland Bank Executor & Trustee Co. Ltd.[28] the Bank, as executor of a taxpayer who had died, attempted to repudiate the terms of such a contract entered into by the taxpayer while he was still alive. It was held that the Bank, as executor, were bound by the contract which the deceased had made.

4.38 The Board does not normally mitigate default interest except in cases of financial hardship, or where the application of Section 88 produces a manifestly unjust result. But in evidence to Lord Keith's Committee on Inland Revenue Powers, the Board made it plain that there is scope for substantial mitigation of penalties, depending on the circumstances of each case. In informal settlements, penalties sought never exceed the amount of the tax due. From this, the following "discounts" can be expected:-

(a) For disclosure a discount of up to 20%. If the disclosure by the taxpayer is immediate when challenged by the Inspector and no material facts are withheld, the full discount of 20% can be expected, the discount being reduced to 5% where disclosure has been piecemeal. If the taxpayer denies the irregularities, but they are confirmed by the Commissioners, or where the Revenue are forced to complete an investigation to prove that irregularities exist, no discount for disclosure will be given. At the other end of the scale, it is understood that the Revenue will accept a discount of 30% in a case where the taxpayer has volunteered information regarding irregularities in his tax affairs.

(b) An abatement of up to 40% can be secured for co-operation by both the taxpayer and his agent in the course of an investigation. Co-operation consists of a willingness to provide all information requested by the Revenue, quickly and efficiently.

(c) An abatement of up to 40% can be obtained depending on the size and gravity of the offence. The amount of tax lost is one factor. Other factors include the way in which the irregularities occurred - whether they amounted to negligence or carelessness, or whether profits were deliberately omitted from returns or accounts. Substantial omissions over a long period, the use of false records, or deception, will substantially reduce the amount of the abatement.

4.39 By publishing its practice in relation to the mitigation of penalties, the Revenue may have exposed itself to a claim that it has exercised its discretionary powers unfairly. Judicial review may lie against an Inspector who fails to give due weight to the mitigating factors described above.[29] Thus an Inspector who offers to accept a voluntary monetary penalty may have difficulty in contending for a higher amount should the case go to Commissioners. It is even possible that, as a matter of natural justice, such a list is ultra vires, although the National Federation case suggests otherwise.

4.40 A further point arises, in this connection, from the fact that, under Section 88(4) and Section 102, it is for the Board and not the Inspector, to exercise discretion. If, therefore, the Board never hears of a decision to impose default interest, or a penalty, it cannot exercise its discretion. That failure may be an abuse of administrative power.

TIME LIMITS FOR RECOVERY OF PENALTIES

4.41 Strict time limits for the recovery of penalties are contained in Section 103 of the Taxes Management Act 1970.

The general rule in Section 103(1) is that proceedings for recovery of a penalty may be commenced at any time within six years following the date on which the penalty was incurred. It is to be observed that there is no reference to fiscal years - the time limit is six calendar years from the actual date of the penalty being incurred. The legislation is silent on when a penalty is incurred. It is thought that it will be incurred on the date, or at the time, when the relative

offence was committed, that is, in relation to a failure, the latest time when the statutory obligation could have lawfully been completed.

4.42 The normal time limit for the recovery of penalties is extended in two situations. The first situation is where a penalty is sought in connection with a loss of tax due to fraud or wilful default. In that case, penalty proceedings may be commenced at any time within three years from the final determination of the amount of the tax covered by the assessment, that is when the assessment can no longer be varied on appeal to the Commissioners, or by an order of the Court.[29a] The second extension of the normal recovery time limit is where an assessment for a chargeable period is made within six years of the end of that chargeable period. In that case, proceedings may be commenced within three years from the final determination of that tax. However, the tax so charged must not include any tax lost due to neglect which has been assessed, with leave from the Commissioners, outwith the normal six-year time limit by virtue of Sections 37, 39, or 40(2). The effect of these provisions, therefore, is that the Revenue have three years in which to commence penalty proceedings in relation to tax lost due to fraud or wilful default, no matter when the offences took place, but they cannot recover a tax-geared penalty due to neglect, if the neglect took place more than six years before the date when the relevant assessment was raised. The three years time limit in cases of fraud etc. was considered by the Court of Session in Carco Accessories Ltd. v. I.R.C.[30] In that case the company paid tax on estimated assessments of tax far short of the actual profits earned. After an enquiry, the Revenue raised additional assessments in amounts which the company agreed were due. But the Inspector, in correspondence, made the additional assessments conditional on statements of the directors' personal assets. The Court confirmed the Commissioners findings that that agreement was not final. Penalty proceedings could therefore be commenced.

4.43 Section 100(5) permits penalty proceedings to be taken against the personal representatives of a deceased person who has incurred a penalty. The extended time limit in Section 103(2) does not, however, apply to these proceedings. If the Revenue seek to recover a

tax-geared penalty from personal representatives, they must, of course, have a valid assessment which has become final and conclusive. Section 40, which has already been discussed, permits assessments to income tax or capital gains tax to be made on the personal representatives of a deceased's person within the three fiscal years following that in which the individual died. The period prior to death for which assessments may be raised is extended by Section 40(2) where tax has been lost due to fraud, wilful default or neglect. But Section 103(4) provides that a penalty based on tax recovered by virtue of Section 40(2) is to be left out of account in determining the Revenue's powers to recover a penalty from personal representatives. The position therefore seems to be that penalty proceedings against personal representatives must be commenced within six years of the date when the offence was actually incurred, with the proviso that if the penalty is tax-geared it will be necessary for the Revenue to produce a valid assessment which has become final and conclusive.

4.44 Where a fixed penalty is imposed under Section 99 of the 1970 Act, or a person who assists in the preparation of accounts for the purposes of tax which he knows to be wrong, only the six year time limit for penalty recovery can apply, unless the Revenue can show that the person has committed fraud or wilful default.

Ch. 4

1. 38 T.C. 625
1a. (1986) STC 331
2. (1980) STC 1
3. see Booth v. Vickars 13 L.J.C. 147
4. Taxes Act 1970 SS 117, 120, & 123
5. 49 T.C. 161
6. ibid p.175
7. 1979 S.C. 371 Lord Jauncey went as far as to give the Parliamentary Draftsman a few hints on how to correct the section's weaknesses.
8. 24 T.C. 221
9. ibid p.248
10. 33 T.C. 288
11. 18 T.C. 402
12. 43 T.C. 61
13. ibid p.73
13a. 1988 STC 116
14. 1948 SC 83
14a. See Cox v. Hickman (1860) 8 HLC 628. For a contrary view, which is incorrect, in the writer's opinion, see "Partners, back duty and death" by A.F. Newhouse 1976 BTR 353
15 ibid p.86
16. 22 T.C. 422
17. T.M.A. 1970 S.101
18. 38 T.C. 666
19. 1982 STC 40
20. 45 T.C. 77
21. 1977 STC 44
22. 1983 STC 162
23. Campbell v. Rochdale Commissioners 50 T.C. 411
24. 1983 STC 415
24a. 1986 STC 542
24b. The Times, Feb. 14, 1987
24c. 1985 STC 56
25. 36 T.C. 561

26 10 T.C. 758

27. 1981 STC 260

28. 19 T.C. 136

29. See R v.Inspector, ex parte Lansing Bagnall Ltd. 1986 STC 41 and Ch.3

29a. TMA 1970 S.118(4)

30. 1985 STC 518

CHAPTER 5

APPEALS AND OTHER REMEDIES

5.01 Although many disputes on back-duty matters are settled by agreement between the Revenue and the taxpayers, not all of them are. In the absence of an agreement, the Inspector will raise assessments to tax, and it may well be that these assessments will cover fiscal years outwith the normal six year period. In due course these assessments may have to be adjudicated on appeal to the General or Special Commissioners. The appeals procedure is therefore a pertinent one for the purposes of this study.

5.02 The appeal code is contained in Part V of the Taxes Management Act 1970. The legislation provides for appeals to be heard, in the first instance, by either the General or the Special Commissioners of Income Tax. Some matters, usually on complex provisions of the law, can be heard only by the Special Commissioners. A few matters are confined to the General Commissioners. But the great majority of appeals can be heard by either the General or the Special Commissioners, although as a result of legislation introduced in 1984, disputes for which there is a choice of jurisdiction go first to the General Commissioners, unless the taxpayer elects otherwise, and the General Commissioners and the Inspector agree that the appeal should be heard by the Special Commissioners.[1]

5.03 The General and Special Commissioners exercise very considerable judicial power over taxpayers' affairs. This power flows from Section 50(6) of the 1970 Act which provides that "If on an appeal, it appears to the majority of the Commissioners present at the hearing, by examination of the appellant on oath or affirmation, or by other lawful evidence, that the appellant is overcharged by an assessment, the assessment shall be reduced accordingly, but otherwise every such assessment shall stand good". Sub-section (7) permits the Commissioners to increase the amount of an assessment, where they consider it appropriate to do so. The main consequence of Section 50(6) is that it places on the taxpayer the onus of showing that an

assessment to tax is too high. That onus may only be discharged by the testimony of the taxpayer himself, or by other lawful evidence. But the power in Section 50(7) to increase the amount of an assessment shows that the Commissioners are not judges, deciding which of two parties to an appeal should succeed. Instead "they are merely in the position of valuers whose proceedings are regulated by statute to enable them to make an estimate of the taxpayer's liabilities for the years in question".[1a] In modern practice, however, the quasi-judicial role of Commissioners has developed to the point that they are now closer to being judges than valuers, mainly because their administrative duties, including the making of assessments, are now carried out by the Inspector.

5.04 There is no doubt that, by placing the onus of discharging an assessment on the taxpayer himself, the legislation has conferred a considerable advantage on the Inspector. Like so much in income tax, this advantage has it origins in history. Originally, the General Commissioners existed, not only to hear appeals against assessments in dispute, but to make the assessments themselves. The function of the Inspector, or the surveyor as he was known until 1922, was administrative, and included the collection of information on which the Commissioners could base their assessments. This arrangement had the effect of offering some protection to the taxpayer against the overzealous Inspector, because at that time, the appeals procedure was less well developed than it is now. It was not until 1964 that the last remnants of the original arrangements were abolished, leaving Commissioners' hearings as the surviving part of what was once a two-part process, namely the making and the determination of assessments. It is for this reason that an assessment once made "stands good" unless the taxpayer can show that it is excessive, and so by accident, the Inspector has therefore inherited a very real advantage. A second aspect of procedure, arising from history, is the nature of the evidence needed to determine an appeal. Originally, in the absence of a return, the Commissioners had to make assessments according to the best evidence available. As a result, the words in Section 50(6) "Where ..... it appears to the Commissioners ..... by ..... lawful evidence". do not restrict the Commissioners to hearing

lawful evidence put forward by the parties to the appeal. In Forestside Properties (Chingford) Ltd. v. Pearce[2] the Commissioners took into consideration facts not advanced by either party, and this practice was upheld by the Court on the footing that this local knowledge was the equivalent of judicial knowledge. It is for this reason that General Commissioners are selected from local people of standing, with knowledge of business and local affairs. The Scottish system of written pleadings, with an appeal based on a Closed Record from which the parties cannot then depart, has no place in appeals to Income Tax Commissioners. At the same time, however, Commissioners are a quasi-judicial body. They are bound by the rules of natural justice, and if their conduct infringes these rules, either party may petition the Court to have the wrong righted. This aspect is dealt with later in this chapter.

5.05 The end product of an appeal to Commissioners against an assessment to tax is the Commissioners' determination. Section 56 of the 1970 Act provides that, immediately after the determination of an appeal by the Commissioners, the taxpayer or the Inspector may declare that he is dissatisfied with the determination as being wrong in point of law, and, within 30 days thereafter, he may require the Commissioners to state a case for the opinion of the Court. Section 56(4) directs that the Stated Case is to contain both the determination, and the facts on which it is based. An examination of the Stated Case procedure therefore gives valuable insight into the operation of the General and Special Commissioners' Hearings.

5.06 It may be said that the two functions of the Commissioners are to find facts, and to draw conclusions from the facts so found. In back duty cases, Commissioners' conclusions are often no more than a matter of credibility. Thus in Jacobs v. Eavis[3] the taxpayer maintained that a deposit of £40 in his bank account represented betting winnings. In their Stated Case, the Commissioners declared that they did not consider this explanation as satisfactory. In another case, Frowd v. Whalley,[4] the taxpayer, a grocer, sought to explain low personal drawings in his accounts by maintaining that his diet consisted of unsaleable meat, cracked eggs, and the trimmings from

the bacon machine. The Commissioners refused to believe him, and the Court held that they were entitled to do so. In cases such as these it seems unnecessary for the Stated Case to say whether the evidence was accepted or rejected. It is enough for the Commissioners to say whether the taxpayer had discharged the onus on him.

5.07 Although many back duty cases are simply cases of credibility, not all of them are. Cases arise where Commissioners, having accepted certain facts as proved, are then obliged to draw inferences from these facts. These inferences may be factual inferences, often referred to as secondary facts, as opposed to the primary facts which are led in evidence. For example the question as to whether a transaction of purchase or sale is an adventure in the nature of a trade is a matter of law, but it is essentially a secondary fact based on the primary facts of how and why the transaction came to be undertaken. In back duty disputes, the issue may be whether primary facts showing dishonesty can lead to the conclusion of a dishonest course of conduct. An example is the decision of the High Court in Rosetta Franks (King Street) Ltd. v. Dick[5] where the Revenue successfully established fraud before the Commissioners on the basis of the evidence of a single customer who had been asked to pay for goods by means of a bearer cheque; had received a receipt not in the name of the taxpayer's business; and where the amount paid was never recorded in the taxpayer's books. It is sufficient, in a case such as this, for the Commissioners to conclude, on the balance of probabilities, that certain proven facts lead to a factual conclusion. They are not seeking to arrive at a conclusion only if the conclusion is beyond reasonable doubt.

5.08 Apart from the submissions in law by Counsel for the parties, the Stated Case is all that the Court has to work with, and in particular, contains the sum of the factual information available. The duty of the Court, in this situation, is to consider whether the determination is sound on the basis of the facts. The Courts cannot consider whether the facts are to be accepted, unless the question is whether, on the basis of the evidence, the facts should have been accepted by the Commissioners themselves. In I.R.C. v. Fraser[6] Lord

Normand said "In cases where it is competent for a tribunal to make findings in fact which are excluded from review, the Appeal Court has always jurisdiction to intervene if it appears either that the Tribunal has misunderstood the statutory language - because a proper construction of the statutory language is a matter of law - or that the Tribunal has made a finding for which there is no evidence or which is inconsistent with the evidence and contradictory of it. It is not as a rule possible to say whether the Tribunal, in any particular case where the Court finds that it has erred, has failed to appreciate the meaning of the statute or whether it has made a finding without having evidence to support it".

5.09 In the later case of Edwards v. Bairstow[7] Lord Radcliffe put the same point in the following way "..... the Commissioners are the first Tribunal to try an appeal, and ..... their decisions can only be upset on appeal if they have been positively wrong in law. The Court is not there to give a second opinion where there is a reasonable ground for the first".

5.10 It follows from these and other decisions that conclusions from primary facts may be reversed, as a matter of law, if the Stated Case contains something which is bad law and affects the determination, or the facts found are such that no person properly instructed in the relevant law could have reached that determination. The question for the Court, in the latter situation, is whether there is evidence to support the determination. It is only if there is no evidence to support it, that the determination can be upset. Time and again, judges have been at pains to state that determinations by Commissioners are final and binding, notwithstanding that, had the judge himself been a Commissioner he would have reached a different conclusion on the same evidence. In Pilkington v. Randall,[8] Lord Justice Salmon expressed the point in the following way "But it is important to guard oneself against the temptation, to which I suppose we are all prone ..... . When we think a conclusion of fact is one at which we would not have arrived ourselves, we are tempted to say that it follows that no reasonable person could have come to that conclusion". This limitation was also expressed by Lord Brightman in Furniss v. Dawson[9] when he said:-

"I agree with the proposition (that the inference to be drawn from facts is a question of law) only if it means that the appellate Court, where jurisdiction is limited to questions of law, can and should interfere with an inference of fact drawn by the fact-finding tribunal which cannot be justified by primary facts. I do not agree with it if it is intended to mean that, if the primary facts justify alternative inferences of fact, an appellate Court can substitute its own preferred inference for the inferences drawn by the fact-finding tribunal".

These aspects have been stressed because of their importance in back duty appeals. It is rare for Commissioners to state a case where the facts found are such that there is no evidence to support the determination. Accordingly, it is the normal practice of the Revenue, when they are unsuccessful before Commissioners on a back duty appeal - and they are sometimes unsuccessful - to accept the decision of the Commissioners. As a result, almost every appeal to the Court on a back duty case has been an appeal by an unsuccessful taxpayer, and with one or two minor, and only partial, exceptions, the taxpayer has been unsuccessful in every case. This fact serves to emphasise a fundamental aspect of Commissioners Hearings namely, the nature and the quality of the evidence which is led before them. An exception to the usual attitude of the Revenue when unsuccessful in a back duty appeal is Brimelow v. Price.[9a] In that case the evidence before the General Commissioners pointed to wilful default, but the Commissioners found against the Revenue. No reason was given in the Stated Case. Even then, the Court refused to reverse the decision. Instead the Stated Case was sent back to the Commissioners, who were merely asked to explain their findings.

ONUS OF PROOF

5.11 In an appeal against an assessment, it is for the taxpayer to show that the assessment is too high, and to do this he must present evidence to satisfy the Commissioners on this point. In the early case of Haythornwaite v. Kelly[10] the capital of a company was increased by £22,920 without a satisfactory explanation being given to the

Inspector, who issued an additional estimated assessment of £50,000. In an attempt to obtain information from the shareholders, the Commissioners issued a demand, or precept, requiring the shareholders to submit their bank passbooks. The precept was not complied with, and the assessment was confirmed. The taxpayers appealed, on the grounds that the precept was ultra vires. In finding for the Revenue the Master of the Rolls, Lord Hanworth said: "..... That, (the precept), was wrong, as I had pointed out, but on the other hand, right or wrong, one cannot but give effect to this, that the company, whose Counsel has revealed the fact that some other profits had been made, which enabled the shareholders to provide capital for the company, did not call any of those persons to speak either to the facts relating to those speculations, or to offer the books for criticism - the books as well of the company, as of the persons whose resources were challenged, and the details of which were given - and there is no doubt that whether the Commissioners could demand them by precept or not, in as much as the onus lay upon the company to displace the assessment, those who were concerned for the company had a great responsibility in not producing, if they were available, materials which would undoubtedly have been of serious import and great business value for the purposes of forming the Commissioners' opinion". In the later cases of Stoneleigh Products Ltd. v. Dodd[11] and Pierson v Belcher[12] the Commissioners confirmed assessments for lack of evidence that they were excessive, and the determinations were upheld by the Court. In a recent case on this point, Bookey v. Edwards,[13] the Inspector made estimated assessments under Schedule D Case 1 on a taxpayer, in the absence of returns from him. On appeal, the taxpayer produced the return but no accounts or records to support the figures. The taxpayer was a driver and a company which had engaged him gave evidence of the amounts paid to him by way of fees and expenses. The amounts paid for expenses were much higher than the fees, but there was no satisfactory evidence to support the taxpayer's contention that the amounts reimbursed by way of expenses had actually been paid away by him in the course of his trade. On the basis of the evidence, however, the Commissioners decided that the estimated assessments were too high, and confirmed them in amounts less than the Inspector's figures, but much greater than the figures for which the taxpayer contended. The Court

held that the Commissioners were entitled to infer the amount of profit from the evidence before them and refused to interfere with their determination.

5.12 However, although the onus is on the taxpayer to displace the amount of an assessment, the onus is clearly on the Inspector if he maintains that an assessment has been made for a special purpose, such as the recovery of tax lost due to fraud, wilful default or neglect. In Hillenbrand v. IRC,[14] the Lord President expressed this principle in the following way:-

> "It was contended to us on behalf of the Crown that wilful default within the meaning of the Income Tax Acts, can be established by the Inland Revenue by means of a presumption of guilt without the Inland Revenue requiring to establish wilful default on the taxpayer's part. An obiter dictum of a single Judge in an English case was quoted to justify this startling proposition. In my opinion, the dictum, which was obiter in that case, does not support such a contention, and I should like to make it perfectly clear that in my view there is no warrant whatever for the idea that under the Income Tax Acts people are presumed to be guilty of wilful default unless they can disprove it. To establish wilful default within the meaning of those words in the Income Tax Act 1952 Section 47 the onus is quite clearly on the Crown and the taxpayer is not in the position of having to prove himself innocent of such a charge without proof by the Inland Revenue that he is guilty of default".

5.13 This shift of onus is important in two respects. First, if the Revenue seek to recover penalties or default interest in respect of an assessment it is necessary for them to show that the assessment is tainted with one of the three offences of fraud, wilful default or neglect. Even if the assessment has been confirmed by the Commissioners, it does not necessarily follow that the tax recovered was lost due to the taxpayer's fault so that, in theory at least, the onus would be on the taxpayer, in the first instance, to show that the assessment should be discharged, but if confirmed it is then for the Inspector to show that there is evidence to support a finding of fraud,

wilful default or neglect. Although in theory these two aspects are different, in practice they are rarely so. If an estimated assessment has been made in the absence of returns, or other satisfactory evidence, then it is plain that the assessment and the basis on which it is made are so closely connected that the taxpayer, in producing evidence to show the assessment is excessive, must also produce evidence to show that he is not guilty of any offence. If, therefore, the assessments are confirmed, and the Inspector succeeds in the assessment, he will have little difficulty in establishing the offence.

5.14 The second aspect where the onus is important is in connection with out of time assessments under Sections 36 to 40 of the 1970 Act. To make an assessment outwith the normal 6 year period, the Inspector has to have the leave of a General or a Special Commissioner, who must be satisfied that there are reasonable grounds for believing that tax has or may have been lost to the Crown "owing to the fraud or wilful default or neglect of any person". It has been held that the duty of Commissioners in this regard is a purely administrative one, and that the taxpayer has no right to be present when the application is made, although in the recent case of R v. Special Commissioners, ex parti Stipplechoice Ltd.[15] the taxpayer company successfully obtained a judicial review of the power of a Commissioner to grant the Inspector the right to raise an assessment outwith the normal six year period, on the grounds that the evidence presented by the Inspector was not factually correct.

STANDARD OF PROOF

5.15 Proceedings before the General and Special Commissioners are civil proceedings, and accordingly, the standard of proof is not the criminal standard of "beyond reasonable doubt". This is so, even where the Revenue allege fraud. In Fen Farming Co. Ltd. v. Dunsford,[16] an Inland Revenue enquiry into the tax affairs of a company and several of its directors was concluded by an offer in settlement of the outstanding tax, plus interest and penalties. Some years later, following the death of the company's managing director, a concealed bank account came to light, and it was apparent that during the earlier

enquiry the profits of the company had not been fully disclosed to the Revenue. On appeal to the General Commissioners, the company offered no evidence as to the source of the funds in the bank account, while the Revenue produced rather flimsy evidence from which it could be inferred that the account contained undisclosed profits made by the company. The Commissioners found that the company was guilty of wilful default. On appeal to the Court, the company contended that the proceedings before the Commissioners were quasi-criminal, and that accordingly, the standard of proof required was higher than the civil standard of "balance of probabilities". In advancing this contention, the taxpayer relied on dicta in the earlier case of Amis v. Colls.[17] The High Court rejected the taxpayer's contention, however, and held that in a civil case, the criminal standard of proof was not required. It may be, however, that when the Revenue allege fraud before the Commissioners, a standard of proof higher than "balance of probabilities" is required. In Lennon v. Co-operative Insurance Society Ltd.[17a] a case on civil fraud, the Lord Ordinary said "I accept ..... that the standard of proof ..... is lower than the criminal standard, namely, beyond reasonable doubt but higher than on the balance of probabilities. I am not able to state in words the extent of that onus but it is ..... somewhere half-way between that and reasonable doubt". The standard of proof therefore depends on the offence, and not on the nature of the proceedings.

5.16 It is, of course, open to the Revenue, where fraud is suspected, to seek to prosecute the taxpayer. In England, the Revenue is its own prosecuting authority, but in Scotland the decision to prosecute is for the Procurator Fiscal, or the Crown Office, on the basis of the evidence presented by the Revenue. If the Revenue decide to take criminal proceedings against a taxpayer, the civil standard of proof will not apply. Instead, it will be necessary for the Crown to show that the taxpayer is guilty "beyond reasonable doubt".

EVIDENCE

5.17 The starting point in any commentary on the importance of evidence in back duty appeals is Section 50(6) of the Taxes Management Act 1970 which provides that, on an appeal, an assessment may only be reduced if a majority of the Commissioners present so decide, by examination of the appellant on oath or affirmation, or by means of other lawful evidence. Section 51 of the 1970 Act gives the Commissioners power to obtain information from an appellant in a tax appeal, and entitles any officer of the Board to inspect books or documents and to take copies. Section 52 entitles either party to an appeal to adduce any lawful evidence in support of his contentions and gives the Commissioners power to summons witnesses to give evidence. Commissioners are entitled to hear such evidence on oath. Penalties may be imposed for failure to comply with these provisions.

5.18 The law of evidence in Scotland is a large and complex subject. Its purpose is to regulate proof and it does this by placing obstacles in the path of anyone who, by forensic means, seeks to establish facts as true. If the obstacles are successfully surmounted, it may be said that the facts in issue are proved.

5.19 Evidence may be:-

(a) Direct or circumstantial. Evidence is direct where it is evidence of a fact in issue; indirect or circumstantial when it is evidence of a fact from which the Commissioners may infer a fact in issue. In taxation appeals, this inference can normally be made only by combining a number of pieces of circumstantial evidence.

(b) Primary or secondary. Primary evidence is evidence proceeding from a witness's own knowledge or from an original document. Secondary evidence is evidence by a witness of what he has heard someone say, or from a copy of a document. Hearsay evidence is secondary evidence.

(c) Written oral or real. Written evidence, if not probative, must be spoken to by oral evidence, as must all items of real evidence.

(d) Evidence of fact or of opinion. What a witness perceives with any of his senses may be spoken to by him. But his opinion can only be founded on if he is an expert on the subject on which he gives evidence.

5.20 The rules on "best evidence" say that evidence put forward to a Court or a Tribunal must be the best which is available. Thus, a photocopy of a document is not best evidence if the original document can be produced. It seems however that this rule, although in the past strongly observed, has now been considerably weakened, and may be of little relevance in taxation appeals.

5.21 To be admissible before a Court or Tribunal, evidence must be relevant to the dispute. For example, if the Revenue allege that the reported profits of a trader are incorrect, it is unlikely to be relevant, without qualification, that the profits of some other trader are higher. This aspect can be important in back duty appeals. One technique adopted by the Revenue (and by Customs) is to obtain details of a trader's purchases and then see whether the gross profit percentage earned on his sales is adequate. Adequacy may be tested in one of two ways. One way is by looking at average rates of gross profit returns for similar traders in the same area. It is questionable whether this evidence is relevant, and, it is submitted, it would not be admissible as opinion evidence unless put forward by someone acceptable as an expert witness. A more acceptable alternative is to take the gross profit percentage which the taxpayer himself seeks to obtain and then see whether his accounts support this.

5.22 In taxation appeals hearsay evidence merits special attention. Hearsay evidence is evidence of what another person has said or written. As such, it is good evidence so far as it goes - as testimony of what has been said or written. But it cannot go beyond that, by proving the truth of the matter stated. The main reason why hearsay evidence is of limited value is that it is not the best evidence - that

can be obtained only from the person who made the written or spoken comment. For example, if a witness says that a taxpayer admitted that his accountancy records were inaccurate that evidence is not primary evidence of the fact of the inaccuracy. It is only evidence that the taxpayer said that his books of account were inaccurate. Hearsay evidence may be admissible, however, in exceptional circumstances, such as where the maker of the original statement is dead.

5.23 A difficulty with hearsay evidence is that, unless it is objected to at the outset, it may be impossible for Commissioners to reach a conclusion without, admittedly inadvertently, taking it into account. In Spedding v. Sabine[18] an Inspector put before General Commissioners hearsay evidence of what the manager of a business had told him about the owner's alleged business dealings. The General Commissioners found for the Revenue. In confirming the Commissioners' decision, the Judge said:-

> "The burden was on the taxpayer to discharge the assessments and he has failed to do so ..... it is clear to me that here was this improbable story told, and the Inspector was entitled to say; I wrote to this man and told him this was quite different from the story I had in my possession from another source, and he never chose to answer ..... They (the Commissioners) might suppose that he did not have an answer. That would be quite enough to justify them in rejecting the appellant's story."

5.24 This is an example of primary hearsay. The Inspector was quite entitled to tell the Commissioners that he had written to the taxpayer asking for an explanation of information which was at variance with the taxpayer's version. The evidence did not prove, or seek to prove, that the Inspector's version was correct. But the Commissioners concluded that it was, in the absence of a satisfactory explanation from the taxpayer. The decision demonstrates the fine dividing line between hearsay evidence being acceptable as to what was said, but unacceptable as to what actually happened. The Spedding case is not however, authority for the proposition that the rules against hearsay evidence are to be disregarded, although the Judge did remark that the

evidence might not have been properly obtained. Although, in practice, an Inspector's suspicions may be aroused by hearsay evidence, and he may even construct his enquiries around such evidence, the Revenue, in an appeal, will be quick to object to such evidence advanced by a taxpayer if it suits them to do so. In Forth Investments Ltd. v. IRC[19] a company sought by means of statements by its company secretary, and by the Barbados Inland Revenue, to establish before Commissioners that it was resident in the Barbados. The Inspector successfully objected to the documents on the grounds that they were hearsay and that better evidence was available but had not been produced. The Commissioners found for the Revenue, and the Court upheld the finding.

5.24a In the recent case of Schister v. Scott[19a] the Inspector had prepared estimates of omitted profits based on figures supplied by the taxpayer. The estimates were held to be admissible. The fact that they were based on the taxpayer's own figures meant that they were not hearsay.

5.25 Facts which are admitted may be taken as evidence, without formal proof. It is a common practice, in appeals to the General or Special Commissioners, for the parties to jointly submit a statement of agreed facts for which no formal proof is necessary. The booklet on tax appeals published by the Special Commissioners encourages the production of such statements. There is no doubt that a statement of agreed facts can save much time and trouble but it is dangerous to take the practice too far. In Bolson & Son Ltd. v. Farrelly,[20] the Court of Appeal expressed some nervousness over the use of such statements in the following way "I do not say it is wrong .... for an appellant before the General Commissioners to submit a statement which is accepted by the Inspector without objection as presenting correctly the facts of the case. That course, from a practical point of view, may be economical and convenient but I think it should be adopted with discrimination."

5.26 Having considered the general principles, it is now necessary to see how they apply to appeals to the Commissioners on back duty matters. Earlier in this chapter, it was explained that the onus was

on the taxpayer to show that an assessment was too high. However, the burden lies with the Crown in establishing that an assessment was made for a special purpose, for example, to recover tax lost due to fraud, wilful default, or neglect. On the face of it, therefore, the burden of proof in a back duty appeal seems to be at cross purposes. On the one hand, the taxpayer must show that the assessment is too high. On the other hand, the Revenue have to show the purpose for which the assessment was made. It would appear that, if the purpose of the assessment is central to its validity, it is for the Crown to establish, at the outset, the presence of fraud, wilful default, or neglect. In Hudson v. Humbles[22] Mr. Justice Pennycook, in the High Court said:-

> "It is well established that, where the Revenue make an assessment which would be out of time apart from the proviso as to sub-section (1) of Section 36 of the Taxes Management Act 1970, the burden lies upon the Revenue to establish that some form of fraud or wilful default has been committed by the taxpayer in connection with or in relation to income tax. If the Revenue succeed at this stage, the burden then shifts to the taxpayer to displace the assessment, for example, on the grounds that it is excessive in amount."

5.27 In the Hudson case, the Inspector's evidence consisted of a capital statement. This was prima facie evidence only, but no evidence was put forward by the taxpayer to challenge it, and accordingly, it was accepted. Where, however, it is not necessary for the Inspector to establish that an assessment has been made for a special purpose, the onus of discharging the assessment would lie, in the first instance, with the taxpayer. If he succeeds, the question of fraud, wilful default, or neglect will not arise. But if he fails, then it seems reasonable to assume that the evidence of the alleged fraud etc. will have been put before the Commissioners in the course of the Hearing.[22a] Normally, therefore, the allegation of fraud etc. would immediately follow the determination of the assessment. There is no need for the Revenue to give particulars of the alleged fraud, etc. at the outset, if it appears from the evidence that fraud is present.[23] But it does not follow that because estimated assessments are confirmed, fraud,

wilful default, or neglect are present. In Wellington v. Reynolds[24] a taxpayer was able to show that his income had been understated because his wife had misled him as to the full amount of profits from her business. It was held that the taxpayer was not himself guilty of wilful default. But the close connection between the amount of the assessment and its purpose makes such a circumstance unusual in practice. Another circumstance which is unusual is for Commissioners to refuse to accept the evidence of one party, in the absence of evidence by the other. In Hudson v. Humbles,[22] the taxpayer refused to put forward any evidence, and the Commissioners found in favour of the Inspector. The Court confirmed the Commissioners findings. In another case, Nicholson v. Morris[25] Inland Revenue enquiries into the fees received by a Barrister's Clerk resulted in estimated assessments being made on him. Some of the assessments were out of time, but had been made with the leave of a General Commissioner. On appeal, the taxpayer did not put forward any evidence to discharge the onus on him of showing the assessments were excessive. Instead, he cross-examined the Inspector of Taxes on the account book which had formed the basis of the Revenue's contentions. The book however, was never formally proved in evidence. The taxpayer's appeals were dismissed, and the assessments confirmed. On appeal to the High Court, the taxpayer contended that the Commissioners were not entitled to infer that he was guilty of fraud or wilful default for all the years under appeal. His contentions were dismissed. The burden was on him to show that the assessments were excessive. If he failed to produce evidence to that effect, he could not succeed. The Hudson and Nicholson cases are examples of the folly of relying on the Revenue's inability to put forward a satisfactory case. It is dangerous for a taxpayer to say "The Revenue have no case, so I can win by saying nothing". Such an attitude merely strengthens the Revenue's hand, no matter any inherent weakness. The general position of the Court where a taxpayer has contended that he has no case to answer was set out by Mr. Justice Upjohn (as he then was) in IRC v. White Brothers Ltd.,[26] in the following terms:-

"The Commissioners when hearing cases where the onus is on the Crown ought not to listen to a submission of "no case to answer". It must

be met with the polite riposte "Do you or do you not elect to call any evidence in this case?" If the taxpayer elects to call no evidence then, of course, he cannot complain if the Commissioners or, on appeal, this Court comes to the conclusion that the Crown has discharged the onus which is upon it, and it would be too late for him then to ask for leave to call evidence."

5.28 The practical consequences of the law described in this chapter can be shown by an examination of a selection of the many cases on back duty appeals which have reached the Courts. In all of these cases, it will be observed that the Inland Revenue have acknowledged an onus to produce at the very least a prima facie case showing that taxable income has been understated, and the question for the Commissioners has been whether the taxpayer can satisfy the onus placed on him of showing that his returns, or business accounts, have disclosed the true amount of taxable income.

5.29 In George Deacon & Sons v. IRC[27] the Inspector discovered that the partners in a firm had over £29,000 among them in private bank accounts. In an attempt to discover the source of this money, the Inspector asked for the production of business books. Some of the books were produced, but the production of others was refused. At a hearing before the General Commissioners, the only evidence put forward by the taxpayers was the audited accounts, which they maintained were correct. They also maintained that the accountancy records supported the annual accounts, but the records were not produced in evidence. The Inspector produced figures showing that the rates of gross profit on the annual accounts had fluctuated wildly from year to year, and that in two years, personal drawings were very high in comparison with other years. The taxpayers alleged that the source of the monies in the private bank accounts was betting winnings, and produced a bookmaker who gave evidence to that effect. But under cross-examination, the bookmakers' evidence proved unsatisfactory and in the end, the Commissioners did not accept the evidence which he gave. Accordingly, the General Commissioners determined the assessments in the amounts brought out by the Inspector in his calculations. On appeal, Counsel for the taxpayer argued that "without

some direct evidence of improper entries or omissions from the books of the business, the Commissioners has no right to draw the conclusion of fact that the business profits had been understated". Mr. Justice Donovan, in dismissing the appeal said that this argument was "just as fallacious ..... as to argue that no-one should ever be convicted on circumstantial evidence alone".

It would seem that the weakness of the taxpayer's case in Deacon was that the refusal to produce books and records supporting the accounts was seen by the Commissioners as tantamount to an admission of guilt. Although the decision of the Commissioners was largely one of inference on circumstantial evidence, the case shows that that will be enough to satisfy the Court.

5.30 In another case, Horrowitz v. Farrand,[28] the private assets of the director of a private company could not be reconciled with his known sources of income. He was therefore assessed to income tax on the footing that he was carrying on a trade separate from his company. His accountants had reported that they had been unable to vouch £650 of the company's purchases, and that the purchases had been paid for by Horrowitz out of his own pocket. However, a proper receipt for the purchases was not available. Before the Commissioners, the taxpayer maintained that his capital increases came from betting winnings and the sales of jewellery and furniture. His accountants did not give evidence since they had resigned before the appeal was heard. The Inspector's evidence was a capital statement which he had prepared before the hearing, and on which he had invited the taxpayer to comment. The taxpayer had produced figures for the sales of jewellery and furniture, and for betting winnings. At the hearing a witness testified that he had bought furniture from the taxpayer and paid him in cash, but no documentary evidence was produced to substantiate this evidence. The Inspector succeeded. The Court held that the Commissioners had evidence to justify their findings. The findings were clearly based on the inferences from the evidence, but once again, that was enough.

5.31 Moschi v. Kelly[29] was a case where, in the High Court, the question of onus of proof was important. The taxpayer, who had come to the United Kingdom in 1933 and had carried on a trade, had introduced new capital of £29,500 into his business between 1938 and 1944, and by 1945, owned jewellery worth £10,000. He was assessed on these sums on the footing that they represented undeclared business profits. On appeal, the taxpayer maintained that he brought cash into the country in 1933, and converted it into sterling through a bank. But the bank could not support the contentions. He also said that he had brought diamonds into this country in 1933. That was accepted by the Revenue, although it was still maintained that there were profits not fully taxed. The General Commissioners found for the Revenue. In the Court of Appeal counsel for the taxpayer submitted that once the Revenue accepted that the taxpayer had brought diamonds into this country in 1933, the onus was on them to show that the apparent deficiencies had come from undisclosed profits, and not from the sale of the diamonds. Lord Justice Somerville did not agree. In his view the appellant had not given evidence in support of his contention that he had brought diamonds into the U.K. in 1933, and there were documents and other facts which were considered by the Commissioners as leading to the inference that the appellant had not had the diamonds in his possession for twelve years. Instead, there was evidence that a cheque for £1500 paid by a customer had been misappropriated by the taxpayer. On the basis of this evidence, the Commissioners were entitled to infer that the Inspector's calculations were correct, and that the assessment should be confirmed. The point here was that the onus of proof had never shifted from the taxpayer at all, because he had not substantiated the basis upon which the onus could have been shifted from him. Accordingly, the evidence of the Revenue, although flimsy, was sufficient. Another case in which relatively flimsy evidence enabled the Revenue to succeed was Rosette Franks (King Street) Ltd. v. Dick[30] where the Crown's case that the accounts of the taxpaying company were wrong was based on the evidence of a witness who, having made a purchase for £39.45 was asked to make out the cheque in favour of the owner of the company, and not the company itself. As a cheque had already been made out in favour of the company, a fresh cheque had to be drawn, and a receipt was given without the shop's name on it.

The customer reported the matter to the Revenue. Capital statements were prepared, and they succeeded in establishing the Crown's case although only one faulty transaction was ever proved. The case is unique since it hinged on a single proved omission, and in practice, it is often relied on by the Revenue, not always successfully, to show that if business books are not wholly accurate, they cannot be relied on.

5.32 The general conclusion to be drawn from these four cases is that the Revenue can prove an omission from tax returns without proving that the taxpayer's accounts are wrong. But they can only succeed if the Inspector can put forward at least a prima facie case to show that there are undeclared profits, and if the taxpayer cannot put forward any satisfactory alternative explanation. Since Commissioners findings of fact cannot be challenged on appeal, and since their conclusions will not be reversed unless they are wholly inconsistent with the facts, there is very little prospect of the losing party succeeding before the Court. This is true where the losing party is the Crown, which is why the Revenue do not normally appeal against adverse Commissioners decisions in back duty matters. Examples of cases which go the other way are therefore not usually reported. In one such case before the General Commissioners, Rafferty v. IRC (unreported) the taxpayer, a hairdresser, had a cash hoard which he kept at home. He maintained that the money had come from his father-in-law, a doctor in Canada, who was in the habit of giving substantial cash gifts in foreign currency to his daughter, when he visited her from time to time. He told the Inspector that he had not lodged these amounts in his bank account because the account was overdrawn, and he feared that if he paid off his overdraft, his bank manager would not give him another one. So he used the cash for private purposes, such as holidays. The Inspector refused to believe him, and raised estimated assessments. Before the General Commissioners, the taxpayer's father-in-law gave evidence on oath that he had given substantial sums to his daughter and his grandchildren, in foreign currency. The taxpayer gave evidence on oath that these gifts were the source of the cash hoard, and that he had converted the currency into sterling by selling to a local bank, although he produced no evidence to support

this. The accountant gave evidence that the annual accounts, although not audited accounts, were correct according to the books and records, some of which were produced. The Inspector who had examined the accountancy records in depth, produced evidence of a number of discrepancies between an appointments diary and a cash book. Nevertheless, the Commissioners accepted the taxpayer's evidence, and the assessments were discharged.

In another unreported case, the taxpayer carried on the trade of selling newspapers, cigarettes, and sweets from a corner kiosk. It was admitted that the accountancy records were "scrappy". There were wide fluctuations in profit, and in gross profit margins, and the Inspector maintained that these fluctuations, together with the inadequate records, showed that the annual accounts could not be relied on. He raised estimated assessments. Before the Special Commissioners the taxpayer admitted that she had little knowledge of book-keeping. She explained the discrepancies in the profit pattern by saying that customers did not stop at the kiosk during bad weather, and that to keep her business going, she had to offer cigarettes and confectionery at reduced prices, from time to time. Her evidence, which was given on oath, was accepted by the Special Commissioners, who said that although they could not be convinced that the true profit had been returned, the evidence as to the reasons for the apparent discrepancies in the annual accounts had satisfied them. The annual accounts were therefore evidence of the taxpayer's profits, and the Inspector had failed to discharge the onus on him of showing that the accounts were wrong.

CONCLUSION ON APPEALS

5.33 Reports of cases on back duty matters show clearly the function and duties of Commissioners to find and evaluate facts, and to reach conclusions based on these facts. Although the law is complex, it very rarely figures in appeals of this sort. If, therefore, a taxpayer is challenged by an Inspector who believes that his returns are incorrect, and the explanations are not accepted, the taxpayer cannot expect to succeed before the Commissioners unless he can shift the onus of proof back to the Inspector, and keep it there. If he

fails at that point, or if the onus moves back to him, and he cannot discharge it, then it is unlikely that he will succeed in the Courts.

JUDICIAL REVIEW

5.34 The power of Judicial Review is based on the duty of the United Kingdom Courts to right wrongs. Originally, in England, a citizen could ask the Court to right a wrong by applying for a writ (or order) of certiorari, mandamus, or prohibition. These common law procedures were consolidated by the Administration of Justice (Miscellaneous Provisions) Act 1938. They are now contained in Order 53 of the Rules of the Supreme Court of 1977. Judicial review in Scotland stems partly from the nobile officium of the Court of Session, and partly from English procedures imported into Scotland by the Exchequer Court (Scotland) Act 1856. It seems, however, that the absence of a clear procedure in Scotland was thought to put the Scots at a disadvantage, and so new Scots procedure for judicial review has recently been introduced.

Judicial review has rarely been successful in back duty matters, but the climate is changing and so a brief review of the subject, particularly in Scotland, is merited.

JUDICIAL REVIEW IN ENGLAND

5.35 An order of mandamus is a prerogative order by which the Queens Bench Division of the High Court in England may direct a person, or an inferior Court or Tribunal, to do a particular thing which it is its duty to do. The order is at the discretion of the Court, and it will only be granted in the absence of an alternative, more convenient, remedy. To obtain an order of mandamus, an applicant must show, first, that he has a sufficient interest in the proceedings, and second, that the person, or body, concerned has an obligation to the applicant to perform the duty in respect of which the order is sought. In taxation appeals, an order of mandamus is rarely granted because the normal course in a dispute, is recourse to the Commissioners by way of an appeal. Mandamus is not an alternative to the appeals procedure.

5.36 An order of prohibition is a prerogative order issued to an inferior Court or to a Tribunal having judicial or quasi-judicial functions ordering it not to proceed or continue with proceedings which are outwith its jurisdiction. Once again, an order of prohibition is not an alternative to an appeal to Commissioners.

5.37 An order of certiorari operates to modify or quash a decision of an inferior Court or a Tribunal acting judicially or quasi-judicially. In such a case, it has to be shown that the Court or Tribunal concerned did not have the authority or jurisdiction to do what it did.

5.38 Two leading modern authorities on judicial review in England, in taxation disputes, are Rossminster Ltd. v. I.R.C.[31] and R. v. Inland Revenue Commissioners ex parte National Federation of Self-Employed and Small Businesses Ltd.[32] The former was an attempt to obtain a judicial review of a raid carried out by Inspectors on Rossminster Bank Ltd. and on the homes of a number of its executives. The latter was an attempt, by a organisation representing small business, to obtain an order of mandamus requiring the Revenue to pursue certain taxpayers for tax allegedly due, which the Revenue had waived. Both cases went to the House of Lords.

5.39 The National Federation case arose out of an Inland Revenue enquiry. For many years, it had been the practice of newspaper owners in London to employ men on a daily basis. These "Fleet Street casuals" were paid by the day, and under a long-standing practice, they were paid without deduction of income tax under PAYE. Instead, each employee was required to sign a receipt showing his name and address and the amount paid, this being the basis on which the Revenue could check that the amounts were duly shown in the recipients' income tax returns. Inevitably, many of the names used were fictitious. The Revenue's investigation disclosed that "Mickey Mouse of Sunset Boulevard" regularly worked on the National Press, sometimes putting in two or three shifts a day. Although it was estimated that considerable sums of tax had been lost to the Exchequer, the Inland Revenue decided that for fiscal years before 1977-78, they would take no proceedings to

recover the lost tax, but would concentrate on 1977-78, and subsequent years of assessment. The National Federation petitioned the Courts for a judicial review, first, to declare that the Revenue were ultra vires in granting the amnesty, and second, to obtain an order of mandamus requiring the Board of Inland Revenue to collect the outstanding tax for the years for which the amnesty had been granted. To obtain the remedies sought, the National Federation had to show that, first, it had somehow been prejudiced or had suffered as a result of the Revenue's discretion, and that, second, the Revenue did not have the power to exercise its discretion in the way in which it had been exercised. Although the principles involved had been before the Courts many times, this was the first case of its kind on a taxation matter. Accordingly, there were no direct authorities to assist the Court. In the House of Lords, the Revenue were successful, on the grounds that the Federation did not have a sufficient interest to complain about how they treated other taxpayers and that, in any event, the Revenue had not been guilty of a breach of duty, or an unlawful act, in the agreement which it made with the Fleet Street casuals. This case is therefore of great importance in demonstrating the wide, and unique, powers of discretion vested in the Board of Inland Revenue in its care and management of direct taxation. It was these wide powers which were at the root of the decision of the supreme court which confirmed that a taxpayer's right to seek redress of a wrong is confined to a wrong against him, or a wrong by virtue of which he himself has directly suffered.

5.40 The Rossminster case was altogether different. Rossminster Ltd. was a bank, which was openly engaged in tax avoidance, but the Revenue believed that some of its transactions amounted to fraudulent evasion. Accordingly, the Revenue obtained warrants under Section 20(c) of the Taxes Management Act 1970, and raided the Bank and the homes of certain directors. Various documents were seized. Judicial review was sought on the grounds that the warrants did not state the alleged offences and that the documents seized had been illegally taken. The House of Lords reversed the decision of the Court of Appeal and refused the application, on the grounds that (a) the warrant strictly complied with the terms of Section 20(c) of the 1970 Act, and

(b) that in all the circumstances, the officers of the Revenue had been entitled to seize the documents taken. However, the decision exposed the exceptional powers conferred on the Revenue by Section 20 of the Taxes Management Act 1970, and as a direct result, a Committee was set up, chaired by Lord Keith of Kinkel, to review the workings of the enforcement powers of the Revenue departments. The Committee's work is referred to briefly in Chapter 1.

5.41 At the outset, it must be stated that judicial review is more of a reserve power than an alternative to an appeal under Section 56 of the Taxes Management Act 1970. Section 56 entitles either party to an appeal before Commissioners to express dissatisfaction with the Commissioners' decision, on a point of law, and to require the Commissioner to state a case, setting out the facts and the determination, for the opinion of the Court. The power of the Court is contained in S.56(6). That sub-section is widely drawn, and entitles the Court to amend, review, or affirm the decision on any point of law; to remit the case back to the Commissioners with instructions; and to make "such other order ..... as the Court may seem fit". In the recent case of R v. Brentwood Commissioners (ex.p. Chan),[34] Taylor J. said at p.7 "It is wide open to a judge on a Section 56 appeal to deal with procedural irregularities such as a wrongful refusal of an adjournment ....". Only in exceptional circumstances was judicial review competent, and since Chan contained no such circumstance, judicial review was refused.

5.42 It is not proposed to examine the legal principles underlying the power of judicial review, but merely to comment on some of the cases which have been before the Courts.

Before examining situations where judicial review in taxation has been held to be competent, it is important to set out, by reference to the authorities, those matters in respect of which judicial review is not available. They are summarised as follows:-

1. Other than in exceptional cases, judicial review is not an alternative to an appeal, within the normal taxation appeals

procedure (R. v. Special Commissioners ex parte Morey,[35] R. v. Inspector ex parte Frost,[36] R. v. Kensington Commissioners ex parte Wyner.[37]) It cannot be used to circumvent the workings of the Taxes Act 1970 (R. v. Special Commissioners, ex parte Elmhirst).[38]

2. Judicial review is not competent to challenge the jurisdiction of particular Commissioners to hear an appeal, since that matter is itself within the scope of the normal appeals procedure (Parikh v. Birmingham North Commissioners).[39]

3. The procedure cannot be used to challenge Commissioners' decisions, on matters of fact or law (R. v. Winchester Commissioners,[40] R. v. St.Marleybone Commissioners.[41])

4. A taxpayer cannot use the judicial review procedure to oblige Commissioners to hear evidence which ought to have but did not, come before them on appeal (Argosam Finance Co. Ltd. v. Oxby)[42] nor can the procedure be used to require Commissioners to reconsider evidence which was brought before them on appeal (R. v. Special Commissioners, ex parte Phillipi).[43]

5. A taxpayer cannot obtain judicial review by claiming unfair treatment by reference to the treatment of other taxpayers (National Federation). However, in the very recent case of R. v. A-G ex parte Imperial Chemical Industries Ltd. plc,[44] the taxpayer claimed that the behaviour of the Revenue had resulted in commercial disadvantages as compared with its competitors. Judicial review was granted. Locus standi was established in that the other companies referred to were the taxpayer's competitors.

6. Finally, judicial review is not an alternative to an appeal to the Court by way of Stated Case (R. v. Special Commissioners ex parte Rogers).[45]

5.43 In recent years taxpayers have had some success in the use of judicial review in challenging the use, by the Revenue, of their statutory and discretionary powers. A review of these more recent

cases is therefore a valuable indicator of developments in this branch of the law.

5.44 In R. v. Special Commissioners ex parte Stipplechoice Ltd.[15] the taxpayer company successfully obtained a judicial review of the power of a Commissioner to grant an Inspector the right to raise an assessment outwith the normal six year period, under Section 41 of the Taxes Management Act 1970. The case arose from a dispute between the company and the Inspector as to whether the company had ceased to trade on a date, as maintained by the Inspector, or had continued to trade beyond that date, as was contended by the company. Originally, an assessment to tax had been made on the basis that the company had not ceased to trade, and that assessment had been agreed, and the tax assessed had been paid. Some years later, the Inspector wrote to the taxpayer company contending, on the basis of undisclosed information, that trading had ceased before the date to which final accounts had been made up. The information had been made available to the Inspector by one of the company's shareholders. By this time, the normal six year time limit for raising assessments had expired, but the Inspector successfully obtained leave from a Special Commissioner to make an assessment out of time, on the grounds that tax had been lost due to the fraud, wilful default or neglect of the taxpayer. The decision in Perlberg v. Varty[46] showed that where an Inspector, in terms of Section 41 of the 1970 Act, seeks leave from a Commissioner to raise an assessment out of time, the taxpayer has no right to make representations to the Commissioner. Nevertheless, the statute requires that the Commissioner has to be satisfied that there are reasonable grounds for believing that tax has been lost to the Crown due to fraud, wilful default or neglect. The Commissioner therefore has a duty to act fairly. In this case, a director of Stipplechoice Ltd. had informed the Inspector that the information which he had was wrong, but the Inspector refused to say, in correspondence, whether or not the taxpayer company's contentions had been put before the Commissioners when the application for the assessment had been made. Accordingly, the Court of Appeal decided that the decision of the Commissioner was susceptible to judicial review, and that leave for judicial review should be given. It was, of

course, stressed that it was perfectly possible that, on review, it would be found that the Commissioners' decision was justified, and it seems at least possible, from the closing comments of Lord Justice Ackner, that had the Inspector been more forthcoming in his correspondence, judicial review would have been refused as unnecessary. The case shows that in matters of private application decisions of Commissioners are judicial decisions, and in consequence, there is an obligation on them to act fairly, notwithstanding that the result of that decision, for example, the issue of the assessment, could itself be challenged on appeal.

5.45 The case of R. v. Inspector, ex parte Lansing Bagnall Ltd.[47] concerned the improper use of Revenue discretion. The taxpayer company was a closely controlled company, and as such, liable to have its income apportioned among shareholders, insofar as the income did not have to be retained for the purposes of the company's business. The company's expenses included payments to charities by way of covenant which, in terms of paragraph 3(1) of Schedule 16 to the Finance Act 1972, were to be treated as added to the amount of the distributable income. In respect of any covenanted payment, paragraph 3 provided that "(It) may be apportioned ..... as if it were income of (the) close company". The Inland Revenue took the view that the word "may" in paragraph (1) of Schedule 16 was a direction which required the amounts paid by way of covenant to be apportioned amongst shareholders. The company maintained that there were good business reasons why these amounts should not be so apportioned, but the Inspector, relying on her belief that apportionment was compulsory, refused to consider these representations. The taxpayer company's application for a judicial review in this case was granted on the grounds (a) that the Revenue interpretation of paragraph 3(1) was incorrect - the word "may" conferred a discretion on the Inspector, not a direction, and (b) that discretion could only be properly exercised after taking into account the representations which the taxpayer company had made. This case is of some importance, since discretionary powers are widespread in fiscal legislation, embracing matters such as the extension of time limits, and the mitigation of interest and penalties on overdue tax.

5.46 A third case which merits consideration is unusual in that judicial review was granted in circumstances where an appeal would have been competent. In R. v. Inspector ex parte Kissane,[48] a firm of solicitors were assessed to tax on certain transactions in land, under Section 488 of the Taxes Act 1970. The gain assessed accrued from a transaction by a Jersey company which had acquired land in the U.K., and later sold it to a U.K. company of which the partners were directors, making a profit of about £800,000. There was no evidence that the partners who were assessed were ever beneficially entitled to the gain, or to any of the property. The grounds on which judicial review was sought were that (1) there was no evidence on which the Inspector could have judged that the tax assessed was due from the appellants, and (2) the Inspector had acted improperly, or by way of an abuse of power, in that the assessments were made with an intention other than that of recovering tax genuinely believed to be due from the taxpayers, and for the purpose of making enquiries about other individuals of a kind not authorised by statute. Although these matters could have been pursued on appeal, judicial review was granted on the grounds that the Inspector's decision to make the assessment amounted to an excess of the proper use of statutory powers, and that on appeal before the Commissioners, the taxpayer, if successful, would not have been entitled to an award of costs. This case shows that "discovery" assessments, under Section 29(3) of the Taxes Management Act 1970 can be the subject of judicial review of the Inspector's statutory grounds for making them.

5.47 It can therefore be said that judicial review in England is, in practice, and in the absence of special circumstances, confined to remedying breaches of administrative procedure or natural justice, not catered for in the Taxes Management Act itself, and in particular, where an appeal by way of Stated Case cannot be made. Judicial review has been granted where:-

1. A General Commissioners' Hearing took place, without the taxpayer having been served with a notice to attend (R. v. Tavistock Commissioners ex parte Adam).[49]

2. One of two General Commissioners' hearing an appeal was a competitor of the taxpayer, and might have been prejudiced in his judgement (R. v. Holyhead Commissioners ex parte Roberts).[50]

3. Prior to a General Commissioners' Hearing, the Inspector told the taxpayer's agent that the case had been adjourned, but the Commissioners did in fact hear the appeal, and subsequently refused to re-open it (R. v. O'Brien ex parte Lissner).[51]

4. Before General Commissioners, evidence was led in a manner which subsequently was accepted as being incorrect (Khan v. Edwards).[52]

JUDICIAL REVIEW IN SCOTLAND

5.48 Mandamus, prohibition and certiorari are English legal concepts, and their procedure is English procedure. Although mandamus and certiorari were imported into Scots procedure by the Exchequer Court (Scotland) Act 1856, they are not known in the common law of Scotland. Nevertheless, the Scottish Courts have the power of judicial review, rooted in Scots common law. Whereas in England the Courts of Equity and the Courts of Common Law were traditionally separate, and developed along different lines, in Scotland equity has always been an integral part of Scots common law. This point was emphasised by Lord President Clyde in a case on charities in 1933, Gibson's Trustees[53] where he said:-

"Owing to its peculiar history, the law of Scotland has never known either distinction or conflict between common law and the principles of equity. It is often said and truly said that in the law of Scotland law is equity and equity is law; and when a Scots lawyer uses the expression common law, he uses it in contra-distinction to laws made by Parliament."

5.49 Thus the Scottish Courts have a duty to ensure that the law is administered fairly. They have a power to right manifest wrongs. In addition, the Court of Session and the High Court of Judiciary have a common law power, the nobile officium, to provide equitable remedies,

in the absence of any other procedure. In the case of the High Court of Justiciary, the nobile officium is restricted to a power of interfering, in extraordinary circumstances, in criminal causes, where no other procedure for review is available. The Court of Session's nobile officium is, by precedent, normally limited to correcting a manifest defect in a statute; to equitable jurisdiction with reference to trusts, in particular charitable trusts; to applications by petition not founded on statute, for example, for the appointment of judicial factors; and to applications for the appointment of public officers in the event of the death or incapacity of an existing officer. In practice, it is unlikely to be extended to other matters. However, in the recent case of Royal Bank of Scotland v. Gillies[54] the Lord Justice-Clerk said that the nobile officium gave the Court the right to assist a petitioner where no other remedy is available.[55] Accordingly, the power is not limited, save that it is a remedy of last resort. In addition to its nobile officium, however, the Court of Session in Scotland has a general power, at common law, to right wrongs; to review the judicial and quasi-judicial decisions of inferior Courts and Tribunals; and in general, to ensure that justice is administered in a fair and proper way. Like the nobile officium, this common law power is an old power. Lord Kames, in the 4th edition of his "Historical Law Tracts" said, at page 228:-

> "Under the cognisance of The Privy Council in Scotland came many injuries, which by abolition of that Court, are left without any peculiar remedy; and the Court of Session have with reluctance been forced to listen to complaints of various kinds ..... Thus it is the province of this Court to redress all wrongs for which no other remedy is provided."

This power may be of relevance in taxation disputes.

5.50 A leading authority on the Court of Session's common law power of review is McDonald & Ors. v. Lanarkshire Fire Brigade Joint Committee.[56] In that case, three members of a fire brigade were disciplined by a committee constituted under the Fire Services (Discipline) (Scotland) Regulations 1953. At the hearing before that

Committee, two of the firemen were found guilty of disobedience, and the third was found guilty of making a false statement. The Committee punished all three by stoppage of pay. The three firemen brought an action against the Lanarkshire Fire Brigade Joint Committee for a reduction of the decision of the Committee and of the punishment imposed. The pursuers' case was that there had been a breach of procedure under the regulations in that they had not been properly served with notice of the charges against them until four days before the hearing, and that at the hearing itself their representative, himself a fireman, who asked for an adjournment, first, to prepare his case properly, and second, on the grounds of his physical exhaustion, was refused the adjournment which he had sought. The pursuers averred that this was contrary to natural justice. The case became before Lord Guthrie in the Outer House. The defenders maintained that the Court had no power to intervene, since the Committee was dealing with a domestic matter of internal discipline in the fire service, and was not, therefore, a judicial or quasi-judicial tribunal. In rejecting this argument, Lord Guthrie stated that in a case involving a breach of regulations, or of the conditions of service imposed on them, the pursuers were entitled to seek the assistance of the Court to enforce these conditions, unless the Court's assistance was excluded by statute. Next, his Lordship held that since the Committee operated in terms of Regulations which included the requiring of a written charge, the issue of documents to the accused, the attendance of witnesses who could be examined and cross-examined, and the possibility that parties may be represented, showed that the proceedings were to be conducted in a judicial or quasi-judicial manner. His Lordship concluded that since there had been a manifest breach of regulations the Committee's proceedings were null and void and that in consequence, the punishment imposed on the pursuers should be set aside. In these circumstances, it was not necessary for the Court to consider whether or not there had been a breach of natural justice because the firemen had had insufficient time to prepare their defence, and had been denied an ajournment at the hearing itself. The judgement, however, implies that if, on a proof, there had been evidence showing that insufficient time to prepare the defence had been given, that would have been a breach of natural justice.

5.51 The Lanarkshire Fire Brigade's case was not, of course, a tax case. Nevertheless, it is of importance in showing that, without reference to statutory authority or any other statutory appeals procedure, a citizen has the right to enlist the support of the Court to obtain justice. A more recent case of interest, Wordie Property Co. Ltd. v. Secretary of State for Scotland[57] concerned the Secretary of State's discretionary power in a planning appeal. In the course of his judgement, the Lord President set out the basis on which the exercise of an administrative discretion may be quashed by the Court. Lord Emslie said:-

> "A decision of the Secretary of State acting within his statutory remit is ultra vires if he has improperly exercised the discretion confided in him. In particular, it will be ultra vires if it is based upon a material error of law going to the root of the question for determination. It will be ultra vires, too, if the Secretary of State has taken into account irrelevant considerations, or has failed to take account of relevant or material considerations which ought to have been taken into account. Similarly it will fall to be quashed on that ground if, where it is one for which a factual basis is required, there is no proper basis in fact to support it. It will also fall to be quashed if it ..... is so unreasonable that no reasonable Secretary of State could have reached or imposed it."

5.52 Several English and Scottish authorities were quoted to support Lord Emslie's statement of the law. Although the statement was made in the context of planning law, it is of wide application. In a case on the provision of housing accommodation (Kelly v. Monkland District Council)[58] it was quoted with approval.

5.53 The broad uniformity of the law between England and Scotland was confirmed by Lord Fraser of Tullybelton in another case on homeless persons, (Brown v. Hamilton District Council).[59] At page 414, Lord Fraser said:-

> "It is not necessary for me to consider the grounds on which judicial review may be open. The decisions in the English cases .....

so far as they relate to matters of substance and not of procedure are accepted as being applicable in Scotland. There is no difference of substance between the laws of the two countries on this matter .....".

5.54 His Lordship also dealt with the question of procedure, when he said, at page 418:-

"(It) is for consideration whether there might not be advantages in developing special procedure in Scotland for dealing with questions in the public law area, comparable to the English prerogative orders."

5.55 As a consequence of Lord Fraser's comments in Brown, and in Stevenson v. Midlothian District Council,[60] a committee was set up under Lord Dunpark to devise procedures for judicial review in Scotland. The result of the committee's work in Rule 260B of the Rules of Court in which the Scots procedure for judicial review is embodied.

5.56 The English authorities show that judicial review is a process apt for dealing with taxation matters in appropriate circumstances. It has not been used in Scotland, however, so far as the writer is aware, and it is an open question whether the Scottish Courts would regard the Scottish procedure as an alternative to the normal appeal procedure.

In the context of taxation the position is, of course, that there is a statutory appeals framework, which provides for a hearing of a tax appeal before General or Special Commissioners. Either party may appeal against a decision of Commissioners to the High Court, or, in Scotland, to the Court of Session, on a point of law. The meaning of the phrase, "on a point of law" has already been analysed and has been held to include procedural matters before the Commissioners. In R. & D. McKerron Ltd. v. I.R.C.[61] a solicitor was appointed to represent taxpayers at an appeal hearing before the Aberdeen General Commissioners on May 25, 1978. The appeal was a "delay case", and was set down for 10.30 a.m. on the appointed day within the Sheriff Court Building. The solicitor duly arrived in good time for the appeal

hearing, but at 10.38 a.m., before his case had been called, he went to the Sheriff Court, in the same corridor in the building in which the Commissioners were sitting, to check on the progress of a criminal trial, in which he had been instructed to tender a plea of guilty. He returned to the Commissioners' waiting room at 10.40 a.m. In the two minutes of his absence, his case was called, and the Commissioners, in the absence of the appellant or his representative, confirmed the assessment. When the solicitor asked the Commissioners, through their Clerk, to hear him, on behalf of his clients, they refused. All he wanted to do was to ask for a continuation of the appeal, which, almost certainly, would have been granted. The Commissioners dispersed at 11 a.m. Since the Commissioners had the discretion to hear the appellant's agent, but had refused to do so, the taxpayers appealed on the grounds that the Commissioners' failure was a breach of natural justice.

5.57 The case came before the First Division of the Court of Session in November 1978, at which the Lord President, Lord Emslie, reformulated the question of law for the Courts' consideration as "Whether, in refusing the solicitor's request to be heard, the Commissioners exercised their discretion reasonably and in a judicial way". That reformulation was necessary, in the opinion of the Lord President, in order that the Court could consider a question which was a question of law. In all the circumstances, the Court concluded that the Commissioners had failed to exercise their discretion properly, and that accordingly, judgement was given against the Crown. The determination was quashed, and the Commissioners were instructed to rehear the appellant's appeal.

5.58 The McKerron decision is in line with an earlier income tax case, Ross & Coulter v. I.R.C.,[62] a case on excess profits tax where, in the House of Lords, Lord Simonds said that the decision of Commissioners was not judicially exercised if its statutory basis was misconceived. It seems, therefore, that despite different procedures the Scottish Courts are in line with the English Courts in treating procedural errors before Commissioners, and abuse of Commissioners' discretion, as matters of law, apt for the appeals procedure contained

in Section 56 of the Taxes Management Act 1970, as opposed to a judicial review. In adopting this approach, the Scottish Courts, in relation to taxation disputes, have avoided the undecided controversy as to whether, in Scotland, the Court can interfere with an inferior Court or Tribunal, to quash a decision for non-jurisdictional error of law. The Franks Committee on Administrative Tribunals and Enquiries[63] said that the Courts in Scotland do not exercise such jurisdiction. Sheriff Middleton, in an article in the 1958 Juridical Review, at page 183 supported the Franks approach, and said "The distinction between error of law, on the one hand, and excess of jurisdiction or oppression or failure of duty, on the other hand, is fundamental, even if not always quite clear cut, and it would be unfortunate if the Scottish Courts were to follow English Courts in mixing them up". Professor J.D.B. Mitchell, on the other hand, in an article entitled "The Scope of Judicial Review" 1959 Juridical Review at page 197, maintains that Sheriff Middleton's distinction is a distinction in name only, and that the Scottish Courts have always regarded themselves capable of correcting manifest errors of law. This argument becomes somewhat academic, in the context of taxation appeals, given that the practice of the Scottish Courts, wherever possible, is to encourage such matters to be brought forward for appeal by way of Stated Case. Thus Scottish procedure would appear to conform with English procedure, although perhaps for different historical reasons.

CERTIORARI AND MANDAMUS IN SCOTS LAW

5.59 Before the introduction of Rule 260B, there was only one statutory procedure for judicial review of taxation decisions in Scotland. Its origin and background are something of an historical curiosity.

Article 19 of the Scottish Act of Union of 1707 provided for the establishment of a "Court of Exchequer in Scotland after the Union, for deciding questions concerning the revenues of Customs and Excise there, having the same power and authority in such cases, as the Court of Exchequer has in England." By 1856 it had been found that "the practice and procedure in the Court of Exchequer in Scotland (was)

inconvenient and troublesome", and so by the Exchequer Court (Scotland) Act of that year the authority and jurisdiction of the Exchequer Court was transferred to and vested in the Court of Session in Scotland. The 1856 Act remains in force; the Court of Session still sits as Court of Exchequer in Scotland, and its procedures are still governed, in principle, by the Act of 1856.

5.60 Section 15 of the 1856 Act provides for procedure in lieu of mandamus. Section 17 contains procedure for the issue of a writ of certiorari. Prohibition is not mentioned, and is foreign to Scots law, but it would appear to be similar in nature to the "injunction" referred to in Section 14.

5.61 The procedures provided for in the Act of 1856 have rarely been invoked in relation to any matter. In the context of income tax, so far as the writer can ascertain, there is only one reported case, that of I.R.C. v. Hood-Barrs,[64] which is therefore the only source of judicial guidance on how these procedures apply in direct taxation appeals.

5.62 The Hood-Barrs case concerned tax relief for losses. Under Section 34 of the Income Tax Act 1918, which consolidated Section 23 of the 1890 Act as amended by the Acts of 1907 and 1916, a person who had sustained a loss in a trade profession or vocation could apply to the General or Special Commissioners to have the loss set against his other income for the year in which the loss was sustained. Where the Commissioners were satisfied on the amount of the loss and had evidence that tax on the other income had been paid, they were authorised, by Section 34(2) to issue a certificate authorising the appropriate income tax repayment. Upon receipt of the certificate, the Commissioners (Board) of Inland Revenue were instructed to repay tax, in conformity with the certificate. It is an interesting feature of the legislation that no right of appeal was provided for until 1953.

5.63 Mr. Hood-Barrs was a timber merchant who, in November 1958, submitted computations of business losses for the years 1947 to 1951 to the local General Commissioners. The losses totalled £4221. The

taxpayer's figures were not computed for the purposes of a loss claim under Section 34 of the Income Tax Act 1918, and the General Commissioners took them into account only in deciding that he had not made a taxable profit. In January 1959, the Clerk to the General Commissioners sent the taxpayer and the local Inspector of Taxes a "directive" signed by the General Commissioners, which purported to make certain legal findings concerning the computation of these losses, and directing the parties to agree the amount of the trading losses in accordance with these findings. This was the first occasion on which any Inspector of Taxes had ever received any intimation of these losses. In February 1959 the General Commissioners proceeded to issue four loss certificates for the four years ended 1951, amounting to £34,348. These certificates were issued without the prior knowledge or agreement of the Inspector. Accordingly, the Solicitor of Inland Revenue (Scotland) appealed to the Court of Session, as Court of Exchequer in Scotland, in terms of Section 17 of the Exchequer Court (Scotland) Act 1856, for a writ of certiorari to quash the loss certificates which had been issued.

5.64 The first problem for the Lord Ordinary was whether an appeal under Section 17 of the Act of 1856 was competent. For it to be competent, it had to be shown that such an action would have been competent in the Court of Exchequer itself before its jurisdiction was transferred to the Court of Session. The difficulty here was that the loss relief claimed had first been introduced in 1890, that is, 34 years after the Court of Exchequer had ceased to exist. In finding in favour of the Revenue on this point, the Lord Ordinary was assisted by the decision in Balfour[65] in which the Lord President had concluded that the correct approach was to consider whether a writ of certiorari could have been brought before the Court of Exchequer, if such Court had continued to exist. It followed, therefore, that the fact that the demise of the Exchequer Court pre-dated the introduction of the loss relief did not prevent Section 17 of the 1856 Act from applying.

5.65 The next problem was to see whether a writ of certiorari was the appropriate course of appeal. The Lord Ordinary judged that an application for a writ was the appropriate course, since in Bruce v.

Burton,[66] the English Court had decided that it was not open to Commissioners to state a case for the opinion of the Court in relation to loss certificates. In the absence of a statutory appeals procedure, therefore, the Court held that an application under Section 17 of the 1856 Act was competent.

5.66 The third question considered by the Court was whether, having applied for the writ, the pursuers had established that there were grounds for certiorari. This depended on whether certiorari extended to a review of the Commissioners decision, for error in law, or whether all that Section 17 did was to authorise the Court to review the Commissioners findings on the grounds of a breach of natural justice which, in the view of the Lord Ordinary, excluded a review for error in law. The Lord Ordinary does not seem to have dealt in any detail with the point. However, he concluded that although there was no error of law on the face of the certificates, the General Commissioners were in breach of a fundamental principle of natural justice by failing to give the Inspector the opportunity of considering the claim for loss relief and making representations. The Lord Ordinary therefore set aside the four loss certificates.

5.67 On appeal, the first division of the Court of Session confirmed the opinion of the Lord Ordinary, and held that:-

1. The appeal was competent.

2. The proceedings before the General Commissioners were quasi-judicial proceedings.

3. The loss certificates were to be quashed on the grounds that there had been a denial of natural justice because the Inspector had had no opportunity to challenge the taxpayer's computation of loss before the certificates were issued, and (reversing the Lord Ordinary on this point) that there was an error of law on the face of the proceedings, since although the certificates themselves betrayed no such error, the directive on which they were based mis-stated the law.

5.68 The House of Lords, in dismissing the taxpayers appeal, held that (a) proceedings before the Commissioners were quasi-judicial and (b) no tribunal, however informal was entitled to reach a decision against any person without giving him a chance to put forward his case.

5.69 The position in Scotland therefore appears to be this. Equity is part of the common law of Scotland. A breach of equity is therefore a breach of law. A taxpayer who, on appeal by way of Stated Case, maintains that the hearing before Commissioners was unfair, has grounds in law for his appeal. Where there is no appeal by way of Stated Case a taxpayer, or for that matter, the Inland Revenue, may have grounds under the Exchequer Court (Scotland) Act 1856. These grounds import English principles, and in consequence, the English decisions may be of some value to the Scottish Courts. In addition, there may be grounds for judicial review of matters not capable of appeal, such as the exercise of Revenue discretion, or the abuse of power, along lines similar to those in England.

CONCLUSION ON JUDICIAL REVIEW

5.70 It would seem that the place of judicial review in taxation appeals may be summarised thus:-

(a) Despite differing history and procedure, the Courts in England and Scotland are likely to apply judicial review of taxation matters in the same way.

(b) Judicial review is not normally an alternative to any remedy catered for by the Taxes Management Act 1970.

(c) Judicial review is normally given where:-

1. there has been an abuse of Inland Revenue discretion, or

2. an abuse of some procedural matter for which the 1970 Act does not cater, or

3. a breach of natural justice has occurred for which a remedy under the 1970 Act is not, or is no longer, available.

CH. 5

1. TMA 1970 S.44-46
1a. IRC v. Sneath 17 TC 149
2. 39 T.C. 665
3. 36 T.C. 576
4. 42 T.C. 599
5. 36 T.C. 100
6. 24 T.C. 498
7. 36 T.C. 207
8. 42 T.C. 662
9. 55 T.C. 324
9a. 49 T.C. 41
10. 11 T.C. 657
11. 30 T.C. 1
12. 38 T.C. 387
13. 55 T.C. 486
14. 42 T.C. 617
15. 1986 STC 474
16. 49 T.C. 246
17. 39 T.C. 148
17a. 1986 SLT 98
18. 35 T.C. 239
19. 50 T.C. 617
19a. 1978 STC 48 For an analysis of this case in the context of the (English) Criminal Evidence Act 1968 see 1977 BTR 241
20. 34 T.C. 161
21. 1984 STC 124
22. 42 T.C. 380
22a. For an example of the application of this important principle see 1976 BTR 355
23. R v. Special Commissioners ex.p. Martin 48 T.C.1, p11
24. 40 T.C. 209
25. 1976 STC 269
26. 36 T.C. 587
27. 33 T.C. 66

28. 33 T.C. 221
29. 33 T.C. 442
30. 36 T.C. 100
31. 52 T.C. 106
32. 55 T.C. 133
34. 1986 STC 65
35. 49 T.C. 71
36. (1973) STC 579
37. 49 T.C. 571
38. 20 T.C. 381
39. 1976 STC 365
40. 1922 ATC 49
41. 1981 STC 557
42. 42 T.C. 86
43. 44 T.C. 31
44. STI 20th March 1986
45. 8 T.C.46
46. 48 T.C. 14
47. 1986 STC 117, 453
48. 1986 STC 152
49. 46 T.C. 154
50. Tax Case Leaflet 2903
51. 1984 Simon's Tax Intelligence 710
52. 1986 STC 331
53. 1933 S.C. 190, pp.198-199
54. 1987 SLT 54
55. Glasgow Magdalene Institute, Petr, 1964 SLT 185
56. 1959 SLT 309
57. 1984 SLT 345
58. 1986 SLT 165
59. 1983 SLT 396
60. 1983 SLT 433
61. 53 T.C. 28
62. 27 ATC 209
63. Cmnd. 218, 1957 pp 25 & 26
64. 27 TC 358
65. 1909 1 SLT 76

66. 4 TC 399

67. 1961 SLT 343