

Penalty mitigation – special reduction (Lecture P1315 – 12.55 minutes)

This article will consider the provisions relating to special reduction – the ability to reduce certain penalties, including to below the statutory minimum. When advisers are dealing with a case where there are, or may be, penalties charged by HMRC, advisers should also consider the other sessions on penalty mitigation, as appropriate.

Overview

HMRC may reduce certain penalties if they “think it right because of special circumstances”. The concept of special reduction applies to the following penalty regimes:

- FA07/SCH24 - inaccuracy penalties;
- FA08/SCH41 - failure to notify and VAT and Excise wrongdoing penalties;
- FA09/SCH55 - failure to make a return;
- FA09/SCH56 - failure to make payment on time;
- FA 2016/SCH22 - asset-based penalties for offshore inaccuracies and failures.

It is important to note that there is no statutory definition of “special circumstances”, although the law outlines certain situations which do not constitute “special circumstances”, see below.

Application of the provisions can result in HMRC “staying” a penalty (where HMRC stop or postponement enforcement) or “agreeing a compromise” (foregoing all or part of a penalty). Where a relevant penalty regime, as noted above, applies, HMRC must consider applying a special reduction.

Although, in theory, the special reduction provisions are good news for clients, they are dependent on HMRC’s discretion (or a favourable decision at the tribunal). Ultimately, each case must be determined on the facts and circumstances.

What are not special circumstances?

The penalty regimes noted above provide that “special circumstances” do not include the ability to pay, or the fact that a potential loss of revenue from one taxpayer is balanced by a potential over-payment by another.

What is HMRC’s view?

HMRC’s guidance on this subject is found in the Compliance Handbook (at CH170100 to CH175200). HMRC’s view is that special circumstances are either:

- Uncommon or exceptional; or
- Where the strict application of the penalty law produces a result that is contrary to the clear compliance intention of that penalty law.

The guidance notes that any other factors that might remove or reduce the penalty should be considered first. This would include, in a case involving a failure to notify, for example, considering whether there is a reasonable excuse.

HMRC consider that the following do not constitute special circumstances:

- Point covered by some other point of law;
- Items balanced out in other accounting periods;
- Where the behaviour is deliberate;
- Size of penalty;
- Proportionality.

HMRC is less expressive when it comes to stating what might be special circumstances. The guidance provides three examples (at CH 170800) of what might be accepted.

What might be special circumstances?

The HMRC guidance on what might be special circumstances do not greatly assist in considering this matter. Advisers should consider all relevant facts relating to their client's circumstances, which might include the following:

- What caused the inaccuracy?
- What caused the client not to take reasonable care?
- What caused the client to make a disclosure that was prompted rather than unprompted?
- Procedural errors by the client
- Mistakes by HMRC, including failure to follow normal working practices
- Lack of contact from HMRC
- Mental health issues
- Life events

Special reduction at the tribunal

There isn't a right of appeal in relation to a special reduction, but the client's remedy is an appeal against the penalty charged by HMRC, or, as appropriate, the level of that penalty. The appeal can include a hearing at the tribunal, although the tribunal's options are somewhat limited. The tribunal may either affirm HMRC's decision on special reduction, or substitute their decision on special reduction for HMRC's decision (but only if the tribunal considers that HMRC's decision was flawed). In this context, a flawed decision has the same meaning as for judicial review (which might include where HMRC has considered irrelevant facts).

Hardy v HMRC [2011] UKFTT 592 (TC) (careless error)

White v HMRC [2012] UKFTT 364 (TC) (careless error)

Klein [2017] UKFTT 0088 (TC) (late filing penalties)

Practical considerations

Advisers should consider other penalty mitigation options before focusing on special reduction. If it can be established that an error in a return has arisen despite the client taking reasonable care, a penalty will not be charged by HMRC. In such a case it will not be necessary to consider whether there are any special circumstances. Similarly, when it can be established that the error arises from careless behaviour, it would normally be preferable to seek suspension of the penalty, if applicable, before pursuing special circumstances.

Where HMRC do not decide to allow a special reduction, advisers should check that HMRC had at least considered whether special circumstances existed. A special reduction may be possible on appeal, if HMRC has not done so, or does not provide an explanation for its decision. This will depend on the facts of the case.

The adviser should determine all relevant facts relating to the offence leading to the penalty and collate any supporting documentation. Reference should be made to any relevant tribunal decisions, to establish whether there are any similar cases. As each case is determined on its own particulars, consideration of tribunal decisions will only provide an indication of how the tribunal might view your client's position. Advisers should consider seeking specialist advice, including whether to help establish the relevant facts, or in making representations to HMRC.

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