[2019] UKUT 0301 (TCC)

Appeal number: UT/2019/0020

INCOME TAX – penalty for inaccuracy in return – whether FTT wrong to refuse to admit oral evidence – whether sufficient basis to uphold the penalty as charged

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

HAROLD WIESENFELD **ALEXANDER STROM**	**Appellants**
-and-	
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS	**Respondents**

TRIBUNAL **JUDGE JONATHAN RICHARDS**
JUDGE ASHLEY GREENBANK

Sitting in public at The Royal Courts of Justice, Strand, London on 3 September 2019 and having considered subsequent written submissions of both parties

Michael Weissbraun of Michael, Pasha & Co, for the Appellants

Joshua Carey, instructed by the General Counsel and Solicitor to Her Majesty's Revenue & Customs, for the Respondents

DECISION

1. Mr Wiesenfeld and Mr Strom (together the "Appellants") appeal to this Tribunal against a decision (the "Decision") of the First-tier Tribunal (Tax Chamber) (the "FTT") released on 16 November 2018.

2. In the tax years ended 6 April 2010, 2011, 2012 and 2013, the Appellants were involved in a property development business carried on in Poland. In relevant tax returns for those years, they claimed relief against income tax for losses they claimed to have incurred in connection with that business. HMRC, however, formed the view that the losses were incurred, not by the Appellants, but by a company incorporated in Poland, Alex Harold Sp zoo (the "Company") which they controlled and that the Appellants were not, therefore, entitled to claim relief for the losses. Having opened enquiries into the Appellants' tax returns for the relevant years, HMRC issued closure notices denying the Appellants the loss relief that they had claimed. HMRC also imposed penalties for what they regarded as careless inaccuracies in the Appellants' tax returns for the relevant years.

3. The Appellants appealed to the FTT against both HMRC's closure notices and the penalties. In the Decision, the FTT dismissed the appeals against the closure notices. It concluded that the Appellants were liable to penalties, but reduced them in amount.

4. With the permission of the Upper Tribunal, the Appellants now appeal against the FTT's decision on the penalties. The Appellants do not have permission to appeal against the FTT's decision on the closure notices and HMRC have not cross-appealed against the FTT's decision to reduce the penalties.[1]

Relevant statutory provisions

5. It was common ground, as it had to be, that if the Company rather than the Appellants carried on the property development activity, the Appellants were not entitled to relief for any losses that the Company incurred. It was also common ground that, if the Appellants carried on the property development activity in partnership, the partnership would be "transparent" so that the Appellants would be entitled to relief for losses incurred in the partnership business. We will not quote statutory provisions relevant to these uncontroversial propositions.

6. Schedule 24 of Finance Act 2007 ("Schedule 24") provides for penalties to be payable if a self-assessment return relating to income tax contains an "inaccuracy" (paragraph 1 of Schedule 24).

7. Paragraph 4 of Schedule 24 links the amount of penalty to the degree of culpability for the inaccuracy. If the inaccuracy arises because of a "failure to take reasonable

[1] Having applied to the Upper Tribunal for permission to appeal only against the FTT's decision on the penalties, the Appellants subsequently sought to amend their grounds of appeal so as to include an appeal against the FTT's decision on the closure notices. In a case management decision released on 19 June 2019, the Upper Tribunal refused the Appellants permission to amend their grounds of appeal and gave reasons for its refusal.

care", as to which it is common ground that HMRC bear the burden of proof, it is categorised as "careless" and attracts the lowest level of penalty. "Deliberate" inaccuracies attract penalties at a higher rate. Inaccuracies that do not arise from a failure to take reasonable care, or from deliberate actions, attract no penalty.

8. Schedule 24 sets out a detailed and prescriptive mechanism for calculating a penalty by applying a penalty percentage to "potential lost revenue" and then mitigating the penalty to reflect, for example, the degree to which the taxpayer co-operated with HMRC in correcting the inaccuracy in the return. Since the relevant dispute in this appeal relates to the threshold question of whether a penalty is due, and not how such a penalty should be calculated if it is due, we will not set out these provisions.

The decision of the FTT

9. References in square brackets are to paragraphs of the Decision unless the context requires otherwise.

The relevant procedural background and pleadings before the FTT

10. The Decision does not contain a record of the procedural background or pleadings that were before the FTT. Since those matters are relevant to our conclusions, we therefore set out our own summary.

11. On 13 January 2017, HMRC issued closure notices to the Appellants denying relief for the losses that they had claimed. On 1 March 2017, HMRC imposed penalties on both Appellants. The Appellants appealed to HMRC against both the closure notices and penalties and HMRC completed an internal review of their decisions on 4 May 2017.

12. On 2 June 2017, the Appellants notified their appeals against both the closure notices and the penalties to the FTT. The Appellants' Grounds of Appeal focused on the closure notices. Little, if any, argument was provided as to why HMRC were not entitled to charge penalties (and we infer that this is because the Appellants hoped to establish that, since they were entitled to relief for the losses as claimed, there was no "inaccuracy" in their returns and so no question of a penalty being due).

13. On 17 October 2017, HMRC served Statements of Case in relation to both Appellants' appeals. HMRC's Statements of Case focused exclusively on the closure notices and advanced no positive case as to why the Appellants were liable to penalties.

14. On 4 November 2017, the FTT made case management directions (the "Directions"). Direction 2 required both HMRC and the Appellants to serve witness statements by 5 January 2018. Direction 8 provided as follows:

> **8 Witness attendance at hearing**: At the hearing any party seeking to rely on a witness statement may call that witness to answer supplemental questions (but the statement shall be taken as read) and must call that witness to be available for cross-examination by the other party (unless

> notified in advance by the other party that the evidence of the witness is not in dispute).

15. On 11 January 2018, Mr Wiesenfeld provided an extremely brief witness statement. The entirety of the evidence set out in his witness statement was as follows:

> I rely on attendance and submissions by my accountant who has full authority in the matter.
>
> The evidence is all included in the bundles which my accountant sent in December and the bundle supplied by Mr Schryber [a reference to Dr Schryber who was the HMRC officer presenting the case] at the same time.
>
> My accountant will put forward the case which will stress the point that at all times both myself and Mr Strom believed the company to hold the property in Poland on Trust for them in equal shares.
>
> I do not believe there is more to be said at this time.

16. The FTT's hearing bundle included an unsigned, undated witness statement from Mr Strom in virtually identical terms.

17. Mr Weissbraun provided a witness statement dated 10 January 2018. Again, that was brief. In addition to a short paragraph setting out his views on the circumstances in which contracts could be the subject of rectification, the totality of Mr Weissbraun's witness evidence was as follows:

> The evidence is all included in the bundles which I sent in December and the bundle supplied by Mr Schryber at the same time.
>
> I will put forward the case which will stress the point that at all times Mr Strom, Mr Wiesenfeld and I believed the company to hold the property in Poland on Trust for them in equal shares. From the moment the project was entered into, everyone concerned was aware that only as a result of Polish law was the project forced to be entered as that of a Polish Company.

18. There was evidently some slippage in the FTT's case management timetable as the hearing was listed for 7 November 2018. Before the hearing, HMRC realised that their Statements of Case did not articulate any positive case on the penalties. On 24 October 2018, when serving their skeleton argument, HMRC told Mr Weissbraun that they would be applying to amend their Statements of Case and to put forward further witness evidence. HMRC made an application to that effect to the FTT on 25 October 2018, enclosing a copy of their proposed Amended Statement of Case (and copied their application to Mr Weissbraun on behalf of the taxpayers). HMRC sent Mr Pumfrey's proposed witness statement to the FTT and to Mr Weissbraun on 29 October 2018.

19. In their Amended Statements of Case, HMRC put their case on carelessness as follows (using the Statement of Case for Mr Strom as an example):

> 12. For the reasons given above, HMRC submit that the Appellant's two tax returns contained errors, namely the claims for relief for the Polish Losses. HMRC submit that if he had taken reasonable care to ascertain

> how the Polish development business was being operated then he would have concluded that the losses accrued to the Polish company and not to himself. HMRC therefore submit that the errors in the returns were down to carelessness on the part of the Appellant, and the penalties were properly charged within the terms of Schedule 24 to the Finance Act 2007.

20. As Mr Carey fairly accepted, this pleading was somewhat short in particulars. It was not said, for example, what steps a reasonable taxpayer would have taken to check the accuracy of the returns or which such steps Mr Wiesenfeld or Mr Strom failed to take.

21. Mr Pumfrey's witness statement explained why he had formed the view that the Appellants' behaviour was careless. In summary, Mr Pumfrey made the following points:

> (1) The Appellants had both signed the Partnership Agreement (referred to in more detail below) that referred to the activities being undertaken by the Company.
>
> (2) The Appellants knew that the Company had submitted accounts to the Polish tax authorities showing that the Company had made losses. They should, therefore, have known that the Company (rather than the Appellants themselves) had incurred those losses.
>
> (3) A reasonable taxpayer in the position of the Appellants would have taken advice on the ability or otherwise to claim relief for the losses. However, Mr Pumfrey had not been made aware of any specific advice that the Appellants took to confirm that they were entitled to relief for those losses.

22. On 31 October 2018, the FTT wrote to both parties to say that HMRC's applications to amend their Statements of Case and to rely on Mr Pumfrey's witness evidence would be allowed unless the Appellants objected by 4pm on 5 November 2018 and that if there was any objection, the application would be determined at the hearing on 7 November.

23. On 1 November 2018, Mr Weissbraun emailed the FTT and HMRC to say that the Appellants had no objection to HMRC's applications. Given the FTT's letter of 31 October 2018, that meant that both applications were allowed. However, the fact remained that the Appellants had only articulated their case on penalties very shortly before the hearing.

24. The FTT hearing took place on 7 November 2018. Neither Appellant attended the hearing, but Mr Weissbraun attended on their behalf. The FTT recorded Mr Weissbraun's explanation as to why Mr Strom was not attending namely that "he was suffering from serious and long-lasting ill-health" but did not make a positive finding that this was the case. We acknowledge Mr Carey's point to the effect that no medical evidence was provided. However, we accept the assurance of Mr Weissbraun, who has acted as Mr Weissbraun's accountant for several years and therefore knows him well, that Mr Strom suffered a stroke in 2015 which has left him paralysed, profoundly deaf and confined to a wheelchair. Mr Strom, therefore, had a good reason for not attending

the hearing. The FTT made no finding as to why Mr Wiesenfeld did not attend the hearing. Before us, Mr Weissbraun explained that his advice at the time was that Mr Wiesenfeld's attendance was not necessary and, since Mr Wiesenfeld understandably felt apprehensive about attending the hearing and being subjected to cross-examination, it was decided that he would not attend. That is not a good reason for his non-attendance, particularly given Direction 8 of the Directions referred to at [14] above.

25. Mr Pumfrey, HMRC's witness, did attend the hearing as required by Direction 8 of the Directions. However, no challenge was made to his witness evidence (see [17] of the Decision).

The FTT's decision

26. The FTT found at [7] that Mr Wiesenfeld claimed relief for losses in all tax years from, and including, 2009-10 to, and including, 2012-13. Mr Strom only claimed relief for losses in his tax returns for the 2011-12 and 2012-13 tax years.

27. Mr Wiesenfeld's tax returns for the years from 2009-10 to 2012-13 stated that he did not carry on business in partnership (see [33]). The FTT made no finding as to whether Mr Strom's tax returns for 2011-12 and 2012-13 contained a similar statement. However, we were shown copies of Mr Strom's tax returns for those years that were in evidence before the FTT and have concluded that, like Mr Wiesenfeld, Mr Strom did not claim in those tax returns to be carrying on business in partnership.

28. Central to the Appellants' case before the FTT against both HMRC's closure notice and the penalties was their argument that the Appellants carried on business in partnership and that the Company held its assets on trust for the Appellants. That, the Appellants argued, entitled them, as opposed to the Company, to claim relief for losses associated with the Polish property business.

29. In support of their case, the Appellants relied on a document headed "Partnership Agreement" dated 10 June 2007 (a date before the Company was incorporated on 10 August 2007). We will refer to that document as the "Partnership Agreement" (even though the FTT's ultimate conclusion was that the Polish property venture was not carried on in partnership between the Appellants).

30. The FTT quoted the entirety of that document at [20] as follows:

> This partnership agreement is made between Alexander Strom of [address] and Harold Wiesenfeld of [address].
>
> Both parties will provide equal funds from their own private resources or through bank facilities to purchase and develop property primarily in the Lodz area of Poland. The partnership will be managed through the offices of Mr Wieslaw Nowakowski… Any loan facility entered into will be the equal responsibility of the partners personally. Mr Nowakowski will have no personal responsibility or liability.
>
> In compliance with Polish legislation which permits foreign nationals to invest in property only through a limited company, a company will be

> formed named Alex Harold Ltd in whom title to any properties bought and traded will be [vested]. The company will be registered at Mr Nowakowski's home address. Mr Nowakowski (a Polish national) will hold 2% of the shares in Alex Harold Ltd and will be authorized to sign agreements under a Power of Attorney. The balance of 98% of the shares will be held by Alexander Strom who frequently travels to Poland on other textile related business and who will be holding 50% of the remaining 98% shares in trust for Harold Wiesenfeld.
>
> The beneficial owners of the properties will be Alexander Strom and Harold Wiesenfeld who will each have beneficial ownership of 48% of any property or assets purchased and will be equally responsible for costs, profits and losses.

31. The FTT directed itself that the onus was on the Appellants to establish that they were entitled to relief for the losses which they had claimed (see [45]). It rejected the Appellants' case that the Polish business was carried out in partnership with the Company holding its assets as nominee for the Appellants deciding, at [52], that the evidence "paints the clearest possible picture that it was the [Company] and not the individuals that was engaged in the Polish property venture". The FTT gave the following principal reasons for that conclusion:

> (1) The Partnership Agreement could not have operated as a declaration of trust made by the Company since it was not entered into by the Company not least since it was made before the Company even existed (see [47]). There was no contemporaneous document stating that the Company was buying any property otherwise than for its own benefit (see [51(2)]).
>
> (2) The Partnership Agreement could not have evidenced a common intention of the Appellants that, when the Company was formed and came to acquire assets, it would hold those assets on trust for the Appellants in equal shares since that would be to ignore the fact that the Partnership Agreement envisaged that Mr Nowakowski was to hold some beneficial interest in both the assets of the Company and shares in the Company (see [21] to [23] and [48]).
>
> (3) The Company had borrowed money (from Bank Zachodni WBK and from Strom International Limited) to finance the purchase price of properties. By contrast, there was no evidence that the Appellants had taken out loans in their own names (see [50]).
>
> (4) The Company drew up accounts showing that it was trading. It submitted tax returns to the Polish tax authorities between 2008 and 2012 with those returns showing trading losses in four years and a profit in one year (see [51(3)]).
>
> (5) The Appellants did not "register a partnership with HMRC" and did not submit partnership tax returns (see [51(4)]). Moreover, in their tax returns for the relevant years, the Appellants had stated expressly that they were <u>not</u> in partnership.
>
> (6) The FTT considered evidence that the Appellants had put forward of an architect who provided services in connection with the Polish property

> business successfully suing Mr Strom for damages in Poland arguing that this demonstrated that the business was carried on in partnership (and the architect was aware of this) since she had sued Mr Strom and not the Company. However, the FTT decided that evidence was inconclusive since conceptually, the Company's shareholders (or directors) could under Polish law have become liable for debts owed by the Company (see [41] and [49]).

32. The FTT reached the above conclusions by reference to documentary evidence and the brief witness statements of the Appellants and Mr Weissbraun to which we have already referred. During the hearing, Mr Weissbraun had asked the FTT for permission to give oral evidence at the hearing dealing with the existence of a trust. The FTT explained, and rejected, this request in the following passages of the Decision.

> 18. Mr Weissbraun stated that he was prepared to give evidence under oath that he had heard Mr Wiesenfeld declare in his presence that the Company was holding its assets on trust for Mr Wiesenfeld and Mr Strom. We considered however that this would amount to no more than hearsay and that although HMRC would have the opportunity to cross examine Mr Weissbraun on what he had heard they would be unable to cross examine Mr Wiesenfeld himself. As such this evidence would have limited value. Had Mr Weissbraun wished to call Mr Wiesenfeld as a witness he could have done so, but he did not.
>
> 19. We also had the benefit of brief witness statements from Mr Wiesenfeld and Mr Strom. Again the appellants had plenty of opportunity to make more detailed witness statements but they did not. We therefore relied on the evidence which was presented to us and which made clear that they intended to enter into a partnership.

33. The FTT's conclusion that the Appellants were not carrying on the Polish property business in partnership resulted in it dismissing the Appellants' appeals against the closure notices. It then went on to consider the penalties directing itself that the burden was on HMRC to show that the Appellants were "careless" and that the penalties were properly calculated (see [62]). It observed that, thereafter "it is for the taxpayers to show a reasonable excuse or special circumstances"[2].

34. As to the threshold condition for application of the penalties, the FTT directed itself at [63] that:

> 63. An inaccuracy in a return is careless if the inaccuracy is due to a failure to take reasonable care. It is not careless for a taxpayer to prepare his tax return using a basis which HMRC disputes, provided the basis adopted is objectively reasonable.

35. The FTT concluded that the Appellants had been careless. Their reasons are brief and we will quote them in their entirety:

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[2] In fact here is no statutory defence of "reasonable excuse" to the penalties at issue in this appeal. Paragraph 11 of Schedule 24 would permit HMRC, or the FTT on appeal, to reduce penalties by reason of the presence of "special circumstances", but no such circumstances were argued to be present.

> 64. However, in this case, Mr Strom traded in the UK both as a sole trader and through a limited company and so would be aware of the difference. The document of 10 June 2007 stated that Mr Strom travelled frequently to Poland on business and implied that Mr Wiesenfeld did not. In both cases, developing property in Poland was an unusual and complex activity which apparently turned sour fairly quickly. Any reasonable taxpayer would take advice on his tax position. Both individuals had experience of UK property development and could be expected to understand the principles of calculating profits and losses.
>
> 65. In our view, given that the factors listed above, which paint the clearest possible picture that the Polish Company carried on the Polish trade, claiming losses as individuals was, at the least, careless.

(The reference to the "factors listed above" at [65] appears, in context, to be a reference to paragraph [51] that sets out reasons why the FTT concluded that the evidence in favour of a partnership was "very weak").

36. Having reached this conclusion, the FTT went on to consider the amount of the penalties that should be imposed. It decided to reduce the penalties but, since HMRC have not appealed against that aspect of the Decision, we need say nothing more about the reasons underpinning that conclusion.

The Grounds of appeal against the Decision

37. The Appellants appeal against the Decision on three grounds:

> (1) Ground 1 – The FTT erred in concluding that the oral evidence that Mr Weissbraun was proposing to give consisted, insofar as it was relevant to the penalties, of hearsay evidence.
>
> (2) Ground 2 – Whether or not Mr Weissbraun's evidence consisted of hearsay evidence, the FTT was wrong to decline to exercise its power to admit that evidence[3].
>
> (3) Ground 3 – The FTT was not entitled on the facts that it found or on the evidence before it, to conclude that HMRC had discharged their burden of proving that they had behaved "carelessly".

The arguments of the parties

The Appellants' arguments

38. Mr Weissbraun presented the Appellants' case. As he acknowledged, he is not experienced in litigation matters: his primary area of expertise consists of the provision

[3] As originally formulated, Ground 2 read "To the extent that Mr Weissbraun's evidence consisted of hearsay evidence, the FTT was wrong to decline to exercise its power to admit that evidence". That formulation would mean that Ground 2 only needed to be considered if that evidence was hearsay. However, it was clear that the Appellants wish to challenge the FTT's exercise of discretion in refusing to admit the evidence, hearsay or not, and we therefore permitted an amendment to the formulation of Ground 2 during the hearing.

of tax advice. That meant that his submissions occasionally involved him seeking to give evidence (for example as to why the Partnership Agreement was drafted as it was or why it was that the Company came to show losses on a tax return it submitted in Poland). We will not set out in detail the evidence that he sought to give because the Tribunal's function in this appeal is not to hear new evidence but rather to decide whether, on the basis of the findings of fact that the FTT made, and the evidence that was before the FTT, the Decision contains an error of law.

39. In relation to Ground 1, Mr Weissbraun maintained that the oral evidence he sought permission to give was not hearsay. Moreover, turning to Ground 2, he argued that the FTT had made an error of law since the only reason it declined to hear his evidence was because of its perception that it was hearsay. In short, he argued that the FTT showed no sign of appreciating that it had any discretion to admit his evidence and still less did it conduct any balancing exercise of the kind that would be needed if it were to decide if it would exercise its discretion in the Appellants' favour.

40. In relation to Ground 3, Mr Weissbraun argued that there were two principal reasons why the FTT concluded that the Appellants were not conducting their business in partnership:

> (1) The Partnership Agreement was drawn up before the Company existed, and so could not amount to a deed of trust under which the Company held its assets on trust. No one identified this problem until Mrs Hogan spotted it during the course of her review of HMRC's decisions.
>
> (2) There were flaws in the drafting of the Partnership Agreement. These flaws were identified by the FTT during the hearing itself.

Given that neither Mr Weissbraun nor Mr Pumfrey had noticed these problems, the Appellants could scarcely have been careless in failing to notice them.

41. More generally, Mr Weissbraun submitted that the Appellants had asked a professional to prepare their tax returns on their behalf and had therefore clearly taken professional advice that they were entitled to claim relief for the losses they incurred. The obtaining of that advice demonstrated that they had taken reasonable care.

HMRC's arguments

42. In relation to Grounds 1 and 2, HMRC argue that the evidence that Mr Weissbraun was offering to give was hearsay. They rightly accept that the FTT has power, under Rule 15 of the Tribunal Procedure (First-tier Tribunal)(Tax Chamber) Rules 2009 (the "FTT Rules") to admit hearsay evidence. Therefore, HMRC accept that, if the FTT had refused to admit Mr Weissbraun's evidence for the only reason that it was hearsay, that would have involved an error of law. However, HMRC argue that this was not the only reason why the FTT declined to admit the evidence: it also took into account considerations of procedural fairness in deciding to refuse to admit evidence that would, in Mr Carey's submission, have been given for the first time orally at the hearing and "from the Bar table". That, HMRC argue, involved the exercise of a case management discretion with which this Tribunal should be slow to interfere.

43. In relation to Ground 3, HMRC support the reasoning of the FTT at [64] and [65]. The Appellants were relatively experienced business people trading in an unusual and complex foreign industry. They had not given any evidence as to why they thought they could claim relief for losses incurred by a Polish company. Given that HMRC had pleaded a case based on the Appellants' failure to take adequate advice and given Mr Pumfrey's unchallenged evidence that he had not been made aware of the contents of any contemporaneous advice, it was not sufficient for the Appellants simply to allude in general terms to the fact that they had engaged Mr Weissbraun, a chartered accountant. They needed to explain what Mr Weissbraun's advice was, when it was given and why that advice caused them to believe their tax returns to be accurate. Since the Appellants elected to give no evidence on these important matters the FTT was both entitled, and obliged, to conclude that HMRC had established that the Appellants behaved carelessly.

Discussion

Grounds 1 and 2

44. As the parties did in their submissions, we will deal with Grounds 1 and 2 together.

45. Although the Civil Evidence Act 1995 does not apply in the context of the Appellants' appeal to the FTT, both parties agreed that s1(1) of that Act sets out the relevant definition of "hearsay" evidence as follows:

> "hearsay" means a statement made otherwise than by a person while giving oral evidence in the proceedings which is tendered as evidence of the matters stated

46. Mr Weissbraun explained to us that he wanted to give evidence that he had heard Mr Wiesenfeld, in his capacity as a director of the Company, making an oral declaration of trust over assets of the Company. Mr Weissbraun was, therefore, proposing to give first-hand oral evidence in the proceedings that the Company had declared a trust over its assets. That would not have been hearsay evidence.

47. It is possible that the FTT did not quite understand the nature of the evidence that Mr Weissbraun wanted to give. The discussion at [18] suggests that the FTT may have thought that Mr Weissbraun wanted to say that Mr Wiesenfeld had told him about a declaration of trust that had been made at another time (when Mr Weissbraun was not present). That would have been hearsay evidence since it would have involved Mr Weissbraun asserting that Mr Wiesenfeld (who was not giving oral evidence in the proceedings) was correct when he told Mr Weissbraun that a declaration of trust had been made on that other occasion.

48. The FTT was, therefore, wrong to decide that Mr Weissbraun's proposed evidence was hearsay. We certainly agree with Mr Carey that, whether or not it was hearsay, the FTT was by no means bound to permit Mr Weissbraun to give oral evidence at the hearing. Since that evidence was not contained in the very brief witness statements that were served there was a real risk of HMRC being "ambushed" by that evidence. However, we do not accept Mr Carey's submission that the FTT had in mind questions

of procedural fairness when deciding to refuse to exercise its discretion to admit the evidence.

49. The crucial passage of the FTT's reasoning is as follows:

> 18. We considered however that [Mr Weissbraun's evidence] would amount to no more than hearsay and that although HMRC would have the opportunity to cross examine Mr Weissbraun on what he had heard they would be unable to cross examine Mr Wiesenfeld himself. As such this evidence would have limited value. Had Mr Weissbraun wished to call Mr Wiesenfeld as a witness he could have done so, but he did not.

50. Mr Carey submitted that, in this passage, the FTT gives multiple reasons for refusing to admit the evidence. The first reason we have discussed: the FTT's mistaken belief that the evidence was hearsay in nature. The second reason, he submitted, was a "fairness" issue, namely that, if the evidence was admitted, since it had not been included in any witness statement, it would have been procedurally unfair to admit it.

51. However, despite Mr Carey's valiant efforts, we are unable to read this as a decision to refuse to admit the evidence on the grounds that it was late and not contained in witness statements. The "unfairness" that the FTT identifies (the inability to cross-examine Mr Wiesenfeld on the averred oral declaration of trust) is simply an aspect of its conclusion that the evidence was hearsay. Since the evidence was not hearsay, there was no unfairness of the type that the FTT identified: since Mr Weissbraun was seeking to give first-hand evidence of the oral declaration of trust, HMRC did not need to cross-examine Mr Wiesenfeld to challenge that evidence; they could have done so by challenging Mr Weissbraun. Similarly, Mr Weissbraun did not need to "call Mr Wiesenfeld as a witness" in order to give the evidence he wanted to give since he was seeking to confirm that he (Mr Weissbraun) had himself seen and heard the declaration of trust being made.

52. We are fortified in that conclusion by the fact that the FTT does not refer in its decision to Rule 15 of the FTT Rules. If it had concluded that, even if the evidence was hearsay, the FTT nevertheless retained a discretion to admit it (under Rule 15), but that the FTT would not exercise its discretion in the Appellants' favour because of considerations of procedural fairness, one might have expected some reference to Rule 15.

53. There were other issues of procedural fairness that would have needed to be considered before admitting Mr Wiesenfeld's oral evidence – primarily the question of whether HMRC would be "ambushed" by that evidence since it was not contained in witness statements and we will consider these later in the decision. However, we are not satisfied that this was the reason why the FTT refused to admit the evidence. Rather, overall, we consider that the overwhelming reason why the FTT refused to admit the evidence was because of its first error of law: its mistaken belief that the evidence would be hearsay. Moreover, having reached that mistaken conclusion, the FTT did not acknowledge that it nevertheless retained a discretion to admit the evidence, hearsay or not, and by not engaging with that discretion made a second error of law. Therefore,

although we agree with Mr Carey that the FTT made a case management decision to refuse to admit the evidence, we consider that decision was vitiated by errors of law.

Ground 3

54. Just two weeks or so prior to the FTT hearing, HMRC articulated a case as to why the Appellants were careless. It was clear from HMRC's Amended Statement of Case and witness statements that their central allegation was that the Appellants knew that the Company was to carry on the business in Poland yet, despite that knowledge, and despite being experienced businessmen, they did not take proper advice to check that they were entitled to claim relief for losses incurred by the Company.

55. It is unfortunate that the Appellants, through Mr Weissbraun, did not object to HMRC's belated service of a pleaded case on the penalties, or to HMRC's belated service of Mr Pumfrey's witness evidence. Indeed, by failing to object when the FTT had said that the applications would be allowed in the absence of an objection, the Appellants were effectively assenting to them. They should have objected or, at the very least, have requested further time to provide their own witness evidence to deal with HMRC's newly advanced case. Since they took neither course, by the time of the hearing the Appellants had provided no witness statements to explain what checks they undertook to satisfy themselves that they were entitled to claim the losses. They did not even positively assert in witness evidence that they had taken any advice, still less explain why that advice caused them to believe that their tax returns were accurate.

56. The Appellants' witness statements, therefore, contained no evidence to rebut HMRC's case. Not only did the Appellants fail to provide any evidence to meet HMRC's case, they did not challenge any of Mr Pumfrey's evidence including his assertion that he was unaware of the Appellants taking any advice on their tax position. It is difficult to avoid the conclusion that the Appellants were somewhat naïve in their approach. However, the FTT can only decide appeals on the evidence before it and the unfortunate effect of that approach was that, by the time of the hearing, the Appellants had advanced little, if any, evidence to meet HMRC's case that they were experienced businessmen who failed to take adequate advice on their UK tax position.

57. Mr Weissbraun argued in his oral submissions that the FTT was wrong to find the Appellants "careless" on the basis of mistakes in, or aspects of, the Partnership Agreement that no-one had identified prior to the hearing. In essence, his argument was that if those points had eluded others for a long period of time, the Appellants could not have been careless in failing to spot them. However, that is to misunderstand HMRC's case. HMRC were not saying that the Appellants were careless because the Partnership Agreement contained errors. Rather, HMRC were arguing that the Appellants were careless because they had failed to take reasonable steps to check they were entitled to claim the losses they were claiming. The way for the Appellants to rebut that case was by giving their own evidence as to the steps they did take. For example, if Mr Weissbraun had provided them with advice, the Appellants could have explained, in their witness evidence, what that advice was and why it gave them assurance that their tax returns were correct.

58. It was unwise of the Appellants to fail to request permission to supplement the witness statements they had already given. The Appellants were also unwise to accept as unchallenged Mr Pumfrey's evidence that he was unaware of the Appellants taking any advice. However, unwise though the Appellants' approach was, the FTT was entitled to infer that HMRC's case was made out given that it had found that the Appellants' tax returns did contain an inaccuracy and HMRC's case and evidence on lack of care had not been contradicted. That conclusion is not altered by Mr Weissbraun's statement in his oral submissions that he did not realise how important witness statements were and that he had assumed they could be supplemented by oral evidence at the hearing. Put simply, Mr Weissbraun's understanding was mistaken, and at odds with the clear terms of the Directions referred to at [14].

59. In his oral submissions, Mr Weissbraun asserted that he had provided the Appellants with advice that it was in order for them to claim relief for the losses since he thought the Appellants were in partnership and the Company held its assets as nominee for the Appellants as partnership property. He criticised the FTT for not allowing him to give oral evidence at the hearing: if he had been allowed to give that evidence, it would have been plain that the Appellants had relied on his advice and had not been careless. However, the difficulty with this argument is that the FTT had made directions requiring witness evidence to be set out in witness statements served in advance of the hearing. Perhaps if Mr Weissbraun had explained at the FTT hearing that, since HMRC had only recently articulated their case on penalties, he should be permitted to give oral evidence on the steps that the Appellants took to check their tax returns he would have been permitted to do so. But he has not said that he made any such request (beyond the request to give oral evidence on the declaration of trust that we have dealt with under Grounds 1 and 2). Moreover, even if Mr Weissbraun had given evidence, that could have taken the Appellants only so far. What mattered was the Appellants' conduct, not that of Mr Weissbraun. Mr Weissbraun could not give evidence as to how the Appellants viewed his advice, whether they knew or believed that the Company was claiming relief for losses in Poland and, if so, why they thought they could claim relief for those losses in the UK.

60. Finally, Mr Weissbraun has emphasised that it has been clear throughout that the Appellants were professionally advised. Their tax returns were submitted by Mr Weissbraun's firm. Similarly, Mr Weissbraun's firm dealt with correspondence on behalf of the taxpayers. That alone, he submitted, made it abundantly clear that the taxpayers had checked with a professional that they were entitled to claim relief for the losses and so were not careless. We quite accept the general point that people tend to engage professionals to assist with tax compliance because they do not themselves know enough about tax to be confident their tax returns are correct. If the Appellants had given evidence that they checked the position with Mr Weissbraun before their returns were submitted, that they provided Mr Weissbraun with all the necessary factual background and that Mr Weissbraun had told them that, in his opinion, they were entitled to relief for the losses, we are prepared to accept that it was likely the FTT would accept that evidence. However, the FTT was not obliged to speculate on what the Appellants' evidence would have been. It had to deal with the case on the basis of the evidence that was actually before it.

61. Overall, we feel some sympathy for the Appellants. They did not realise the significance of HMRC's late application to articulate a case on the penalties. They did not realise the importance of witness statements or of Mr Wiesenfeld's attendance at the hearing. They did not realise that, if they disagreed with Mr Pumfrey's evidence that the Appellants failed to take adequate advice, they should challenge it in cross-examination. However, they were professionally represented by Mr Weissbraun and their (and Mr Weissbraun's) ignorance on the above matters cannot overcome the fact that they failed to provide any significant evidence to meet HMRC's pleaded case on carelessness that was backed up by Mr Pumfrey's unchallenged witness evidence. In the circumstances, the FTT was entitled to conclude that the Appellants were careless and we do not consider that Ground 3 is established.

Whether to remake or set aside the Decision

62. We have decided that the Decision contains the errors of law summarised at [53]. In those circumstances, s12 of the Tribunals, Courts and Enforcement Act 2007 provides that:

> (1) We may (but need not) set aside the Decision.
>
> (2) If we do set aside the Decision we may either (i) remit the case back to the FTT with directions for its reconsideration or (ii) re-make the Decision.

63. We have decided that we will not set aside the Decision. Mr Weissbraun's proposed oral evidence went to the question of whether the Company had declared a trust over its assets. That was the province of the FTT's decision on the closure notices, and the Appellants have not obtained permission to appeal against that aspect of the Decision. Since the Appellants cannot challenge the decision on the closure notices, in deciding whether to set aside the FTT's decision on the penalties, we have to take as our starting point the proposition that there was an "inaccuracy" in the Appellants' tax returns arising from the fact that the Company had not declared a trust over its assets in favour of the Appellants in partnership, but rather was conducting the business in Poland in its own name. Accordingly, we consider that the FTT's mistaken conclusion that Mr Weissbraun's evidence should be excluded on the grounds only that it was hearsay had no actual effect on the outcome of the penalty appeal.

64. In reaching the above conclusion, we are not saying that, if we were to remake the Decision, we would have decided that Mr Weissbraun's oral evidence should have been admitted. On the contrary, we too would not have permitted that evidence to be given albeit for somewhat different reasons from those the FTT gave.

65. The FTT had made directions requiring witness evidence to be set out in written witness statements and for witnesses to attend the hearing for cross-examination. Mr Weissbraun was not seeking to give his oral evidence as a response to HMRC's belated articulation of a case on the penalties. If Mr Weissbraun had given his evidence orally for the first time at the hearing when witness statements made no mention whatsoever of an oral declaration of trust, the Appellants would have circumvented the requirements of the FTT's directions and exposed HMRC to a risk of "ambush". It is no answer for Mr Weissbraun to say that he did not appreciate the significance of

witness statements: he was the Appellants' duly appointed representative and should not have acted in that capacity unless he felt that he had a sufficient knowledge of Tribunal procedure and general principles of litigation.

66. We accept that Mr Strom had a good reason for not attending the hearing. However, the oral declaration of trust was said to have been made by Mr Wiesenfeld. In those circumstances, Mr Wiesenfeld should have mentioned it in his witness statement and should have attended the hearing for cross-examination. It follows that Mr Strom's ill-health was not a sufficient reason for Mr Weissbraun to be permitted to give new evidence on this issue for the first time at the hearing.

67. Overall, therefore, if we had remade the Decision, even making due allowance for Mr Strom's health problems, we would have decided that it was in accordance with the overriding objective in Rule 2 of the FTT Rules for Mr Weissbraun not to be permitted to give oral evidence at the hearing.

Disposition

68. The Decision contains errors of law. However, those errors had no material effect on the outcome of the penalty appeal. We will not, therefore, set aside the Decision and the Appellants' appeal is accordingly dismissed.

JUDGE JONATHAN RICHARDS
JUDGE ASHLEY GREENBANK

RELEASE DATE: 14 October 2019