UT Neutral citation number: **[2026] UKUT 00007 (TCC)**

UT (Tax & Chancery) Case Number: UT/2024/000114

Upper Tribunal
(Tax and Chancery Chamber)

PENALTIES – HMRC had refused to exercise its discretion to suspend penalties for careless inaccuracies – inaccuracies arose as a result of a one-off event and HMRC could not see any future careless inaccuracies that could be avoided by setting a condition – FTT decided that HMRC's refusal to suspend was not flawed – held – appeals dismissed

Hearing venue: The Rolls Building
London
EC4A 1NL

Heard on: 9 October 2025
Judgment date: 7 January 2026

Before

JUDGE JEANETTE ZAMAN
JUDGE JENNIFER DEAN

Between

PHILIP COX (1)
DEBRA COX (2)

Appellants

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellants: Christopher Vallis, instructed by TaxFellowship

For the Respondents: Laura Ruxandu, instructed by the General Counsel and Solicitor for His Majesty’s Revenue and Customs

DECISION

INTRODUCTION

1. Philip Cox and Debra Cox ("the Appellants") appeal the decision of the First-tier Tribunal (Tax Chamber) ("the FTT") released on 3 June 2024 ("the FTT Decision"). HMRC had issued penalties to the Appellants in respect of inaccuracies in their self-assessment returns for the tax year 2019/2020 on the basis that the Appellants had failed to take reasonable care and claimed entrepreneurs' relief (also referred to as business asset disposal relief or "BADR") to which they were not entitled as they did not own the required minimum shareholding of 5% in the company.

2. The FTT dismissed the Appellants' appeals against:

   (1) penalties of £16,152.90 (for Mr Cox) and £16,252.35 (for Mrs Cox) for careless inaccuracies; and

   (2) HMRC's refusal to suspend these penalties.

3. The appeals to the Upper Tribunal concern only HMRC's refusal to suspend the penalties.

4. We have summarised the facts as found by the FTT below, and refer to paragraphs of the FTT Decision as "FTT[x]". In the FTT Decision the Appellants were referred to as "PC" and "DC" respectively and, together, as "PDC".

5. For the reasons set out below, we have dismissed the appeals.

FTT DECISION

6. The Appellants were (along with others) shareholders in David Williams IFA Holdings Ltd ("DWIFA"). The directors of DWIFA were Mr Beal, Mr Cox, Mr Lowe, Mr Sparrow and Mr Womack (FTT[6]).

7. The Appellants, along with four of the other shareholders (together, the outgoing shareholders) decided in 2018 to dispose of their shareholdings in DWIFA to the remaining shareholders, David Sparrow, Gillian Sparrow, Stephen Womack and Lucy Womack (together, the continuing shareholders). A new vehicle was set up to acquire the business (FTT[6]).

8. It had been agreed informally by the outgoing shareholders that Mr Sparrow and Mr Beal (one of the outgoing shareholders) would act as the points of contact for them, including liaising with solicitors and keeping them informed (FTT[7]).

9. DWIFA instructed EWM Solicitors ("EWM") to advise on the transaction (FTT[8] and [253]).

10. Mr Cox attended a meeting on 18 April 2019 with all the directors of DWIFA, Ian Morris (a partner at EWM) and Lisa Stevenson (a tax specialist and senior associate at EWM). At that meeting it was confirmed that the Appellants owned their shares for the relevant period of time, that the shares related to a qualifying company and that they had "enough" shares (FTT[8] and [20]). Everyone at the meeting was aware of the 5% shareholding which was required to claim entrepreneurs' relief (FTT[21]). At the date of the meeting, the Appellants each held 6.4% of the shares in DWIFA (FTT[44]).

11. At subsequent meetings, the directors of DWIFA discussed how the consideration for the sale should be split in a way that more accurately reflected each individual's contribution to the business. The outcome of this was that it was agreed that the Appellants (and two of the other outgoing shareholders) would transfer shares to David Sparrow and Gillian Sparrow (FTT[23]).

12. Mr Sparrow suggested that they gift these shares as he felt sure it would not lead to any CGT, as the gift would qualify for holdover relief from CGT, and there would be no Inheritance Tax ("IHT") issues, as the shares to be gifted were "business property" and eligible for relief (FTT[24]).

13. On 25 April 2019, Mr Sparrow and Mr Beal asked Mr Morris whether he foresaw any problem with the proposed gifting of the shares and the revised structure of the deal (FTT[25]). Mr Morris replied by email to Mr Beal, with a copy to Mr Sparrow, on 29 April 2019 saying: "At first glance I do not see anything wrong with the proposal to give some B shares to David and Gillian but as previously discussed I am not an out and out tax expert. If you want proper sign off both on CGT and IHT I would need to refer the proposal to Lisa and there would be a cost implication for the extra work" (FTT[42]). Mr Beal and Mr Sparrow did not ask for such a sign-off (FTT[43]).

14. On 30 April 2019 the Appellants each gifted shares to other shareholders of DWIFA, taking their percentage ownership of DWIFA to below 5% each (FTT[10]).

15. The Appellants disposed of their remaining shares on 20 May 2019, and subsequently claimed entrepreneurs' relief on this disposal in their 2019/20 self-assessment returns (FTT[11]).

16. Following enquiries into the Appellants' self-assessment returns, HMRC issued closure notices amending the returns to reflect the fact that the Appellants were not entitled to entrepreneurs' relief. HMRC also assessed the Appellants to penalties for careless behaviour. HMRC allowed the maximum level of mitigation and imposed the minimum penalty of 15% of the potential lost revenue.

17. In correspondence, the Appellants' advisers asked HMRC to suspend the penalties. Various potential conditions of suspension were put forward on behalf of the Appellants. HMRC refused to suspend the penalties. The conditions proposed and HMRC's reasons for refusal are set out separately below.

18. The FTT found that the Appellants acted carelessly in submitting erroneous self-assessment returns:

> (1) The FTT found that the Appellants were not receiving specialist professional advice on their specific and changed circumstances and were also relying on Mr Sparrow's advice on the CGT holdover and IHT consequences of their gifts, which was not relevant to entrepreneurs' relief (FTT[246]).
>
> (2) The Appellants did not as a matter of fact seek appropriate advice from a competent professional adviser after the meeting on 18 April 2019 when their circumstances had changed (FTT[251]).
>
> (3) To the extent that the Appellants received advice at the meeting on 18 April 2019 in relation to their paramount wish to obtain entrepreneurs' relief, they did not seek subsequent advice, nor did DWIFA, following the gift of shares which resulted in the failure to meet the 5% shareholding limit (FTT[252]). The professional advice was provided to DWIFA not to the Appellants regarding tax and buyout structuring issues, and it was not reasonable to rely on the 18 April 2019 meeting advice after having gifted some of their shares (FTT[253]).
>
> (4) Mr Cox was a financial adviser and both the Appellants were company directors. They had not behaved as prudent and reasonable taxpayers (FTT[254]).

19. The FTT also concluded that HMRC's decision to refuse to suspend the penalties was not flawed.

RELEVANT LAW

20. Provisions in relation to penalties are contained in Schedule 24 to Finance Act 2007, and references in this decision to paragraphs are to paragraphs of that Schedule to that Act.

21. Paragraph 14 provides as follows:

> "(1) HMRC may suspend all or part of a penalty for a careless inaccuracy under paragraph 1 by notice in writing to P.
>
> (2) A notice must specify -
>
> (a) what part of the penalty is to be suspended,
>
> (b) a period of suspension not exceeding two years, and
>
> (c) conditions of suspension to be complied with by P.
>
> (3) HMRC may suspend all or part of a penalty only if compliance with condition of suspension would help P to avoid becoming liable to further penalties under paragraph 1 for careless inaccuracy.
>
> (4) A condition of suspension may specify -
>
> (a) action to be taken, and
>
> (b) a period within which it must be taken.
>
> (5) On the expiry of the period of suspension -
>
> (a) if P satisfies HMRC that the conditions of suspension have been complied with, the suspended penalty or part is cancelled, and
>
> (b) otherwise, the suspended penalty or part becomes payable.
>
> (6) If, during the period of suspension of all or part of a penalty under paragraph 1, P becomes liable for another penalty under that paragraph, the suspended penalty or part becomes payable."

22. A refusal to suspend a penalty may be appealed under paragraph 15(3). Paragraph 17(4) provides, so far as relevant:

> "On an appeal under paragraph 15(3) the tribunal may order HMRC to suspend the penalty only if it thinks that HMRC's decision not to suspend was flawed…"

23. Paragraph 17(6) provides, so far as relevant:

> "In sub-paragraph … (4)(a) 'flawed' means flawed when considered in the light of the principles applicable in proceedings for judicial review."

24. There was no disagreement between the parties as to the applicable principles, which are summarised by Lord Greene MR in *Associated Provincial Picture Houses Ltd v Wednesbury Corp* [1948] 1 KB 223 at pg 233 to 234:

> "The court is entitled to investigate the action of the local authority with a view to seeing whether they have taken into account matters which they ought not to take into account, or, conversely, have refused to take into account or neglected to take into account matters which they ought to take into account. Once that question is answered in favour of the local authority, it may be still possible to say that, although the local authority have kept within the four corners of the matters which they ought to consider, they have nevertheless come to a conclusion so unreasonable that no reasonable authority could ever have come to it. In such a case, again, I think the court can interfere. The power of the court to interfere in each case is not as an appellate authority to override a decision of the local authority, but as a judicial authority which is concerned,

> and concerned only, to see whether the local authority have contravened the law by acting in excess of the powers which Parliament has confided in them."

GROUNDS OF APPEAL

25. The Upper Tribunal granted permission to appeal on four (of nine) grounds sought by the Appellants in relation to HMRC's refusal to suspend the penalties. Those four grounds are:

(1) The FTT was wrong to conclude (see for example FTT[287] and [288]) that HMRC had not unreasonably fettered their discretion in following the rule that a penalty cannot be suspended where it is not possible to set conditions because a similar inaccuracy is unlikely to happen in the future (see for example FTT[65]).

(2) The FTT erred in concluding that there must, by virtue of paragraph 14(3), be a link between the type of inaccuracy giving rise to the penalty and any future inaccuracies, and therefore that a "one-off" error would not be suitable for a suspended penalty (see FTT[290]).

(3) The FTT was wrong to conclude that HMRC had not unreasonably fettered their discretion by applying the SMART criteria (insofar as these criteria are deemed to exclude the possibility of suspension in cases of one-off inaccuracies).

(4) The FTT erred in applying the rule that the conditions applied must amount to more than "the actions of a reasonable and prudent taxpayer" (see FTT[296]) and in concluding that the proposed conditions for suspension were inappropriate as they were "no more than a basic requirement" (see FTT[273]) that future returns should be free from careless inaccuracies, where it is the purpose of the legislation to encourage taxpayers to act reasonably and prudently (ie not carelessly) and, indeed, a taxpayer can do no more than submit a return free from careless inaccuracies.

26. The Appellants' grounds of appeal are detailed and wide-ranging. HMRC's submissions included that these grounds nevertheless misrepresented the reasons for HMRC's refusal decision and/or the FTT Decision.

27. The issue for the Upper Tribunal is whether the FTT made an error of law in deciding that HMRC's decision was not flawed on the basis of any of the Appellants' grounds of appeal (and, if so, whether such error was material to its decision).

STRUCTURE OF THIS DECISION

28. In this decision we:

(1) set out the correspondence between the Appellants and HMRC which records HMRC's decision to refuse to suspend the penalties;

(2) summarise the FTT's decision in relation to suspension;

(3) summarise the submissions of the parties;

(4) address the approach to paragraph 14 and HMRC's discretion to suspend a penalty for a careless inaccuracy; and

(5) explain our decision on the Appellants' grounds of appeal.

29. There is no authority binding on the Upper Tribunal in relation to an appeal against HMRC's decision to refuse to exercise its discretion to suspend a penalty under paragraph 14. We were taken by both parties to various decisions of the FTT, in particular:

(1) *Fane v HMRC* [2011] UKFTT 210 (TC) ("*Fane*"),

(2) *Testa v HMRC* [2013] UKFTT 151 (TC) ("*Testa*"),

(3) *Steady v HMRC* [2016] UKFTT 473 (TC) ("*Steady*"), and

(4) *Eastman v HMRC* [2016] UKFTT 527 (TC) ("*Eastman*").

30. We have referred to some of the reasoning in those decisions to the extent we have found it helpful to do so, particularly where we consider this assists with understanding the reasoning in the FTT Decision (which refers to these other decisions) but emphasise that this is not an appeal against any of those decisions.

CORRESPONDENCE BETWEEN HMRC AND THE APPELLANTS ON SUSPENSION OF PENALTIES

31. The correspondence between HMRC and the Appellants includes the (three) conditions for suspension that were proposed at different times by the Appellants and the reasons HMRC gave for refusing to suspend the penalties.

32. In a letter dated 5 May 2022 HMRC explained HMRC's decision to impose the minimum penalties for the careless inaccuracies. At that time, HMRC explained its refusal to suspend the penalties as follows:

> "The knowledge you have gained as a result of this enquiry is what will assist you in determining whether potential future claims to BADR are valid.
>
> I am unable to set any specific, measurable, achievable, realistic and time bound (SMART) conditions to help you avoid making these inaccuracies in future and so the penalty will be charged."

33. The Appellants responded on 25 May 2022 setting out their position that their behaviour had not been careless and stated:

> "It is surely possible to set a condition which stipulates that they will commit to taking advice on any future transactions on their own behalf rather than relying on advice taken via any third party over an agreed timescale as required by the legislation."

34. On 12 July 2022 HMRC explained its position as follows:

> "It appears to me that it is unlikely that similar careless inaccuracies will arise in future. Firstly, your clients will have gained knowledge from this enquiry that will help them avoid a similar error in future.
>
> Additionally, as far as I am aware, neither of your clients currently hold any offices, nor any employments currently. While of course other eligibility criteria also apply, this does not indicate that your clients currently have any capability or intention to dispose of shares that could qualify for BADR. Currently I have no reason to believe that it is likely that your client's will ever have further share disposals that may qualify for BADR.
>
> Therefore, as it seems unlikely that a similar careless error will occur again, I find it difficult to see how any suspension condition relating to this could be measured (as per the SMART criteria)."

35. On 21 August 2022 the Appellants said that the reason given by HMRC, and the reference to "similar", was not the test required by the legislation and continued:

> "Therefore, it becomes possible to identify what could have been done differently so that an inaccuracy can be avoided in future. We put it to you that this failure could be attributed to the advice being targeted on the transaction as a whole and, in the process, the focus on the specific position of our clients was lost. It then is possible to set a condition for the future that the Coxs' always appoint separate Advisers dedicated to their particular circumstances and, secondly, that any advice given at client meetings is always confirmed in writing."

36. HMRC responded on 14 September 2022:

> "I note your point in response to my previous mention of "similar" inaccuracies and would explain that this is not a reference to the legislation but to HMRC guidance on suspension of penalties as per the previously issued factsheet CC/FS10. The legislation at FA 2007 Sch.24 paragraph 14 is not specific regarding which careless errors could be avoided in the future through any suspension conditions as you point out. However, the point remains that I cannot see any future careless error(s) that could be avoided by setting a suspension condition in this case.
>
> As mentioned in my previous correspondence, the legislation states that HMRC may suspend a penalty, only if compliance with a condition of suspension would help a taxpayer to avoid becoming liable to further penalties for careless inaccuracy. Your response suggests a condition relating to your clients seeking individual advisors that will consider only your clients particular circumstances, in the event any further advice is required. This condition would unfortunately not meet the suspension criteria for several reasons.
>
> Firstly, a promise to check with an advisor in future is not a measurable condition. I would refer again to CC/FS10 which sets out that any suspension condition must be specific, measurable, achievable, realistic and timebound. The condition does not relate to a definite specific action, but rather an action that could be taken if the situation arose.
>
> Furthermore, such a situation may not arise within the suspension period and therefore again this would be a suspension condition which does not meet the criteria set out in the legislation (as above) as the condition will not have avoided any future careless errors. Also, were this to be the case, adherence to the condition could not be measured.
>
> Additionally, seeking appropriate advice where required, to meet tax obligations is a responsibility already expected of reasonable taxpayers, regardless of a suspension condition. It's everyone's own responsibility to get their tax right. As mentioned above, in HMRC's view it is reasonable to expect a person who encounters a transaction or other event with which they are not familiar to take care to find out about the correct tax treatment or to seek appropriate advice.
>
> Therefore, due to the points raised above I can't see how appropriate suspension conditions can be set to avoid a future careless inaccuracy and allow the penalties to be suspended."

37. HMRC issued the penalty notices on 3 October 2022.

38. On 17 October 2022 the Appellants proposed an alternative condition:

> "We can understand your view that promising to do something contingently in the future may not be a suitable condition for suspension. However, our proposal is that each year, with immediate effect, our client should have a formal minuted, in-person meeting with a partner in this firm specifically to review each entry on the return before the return is submitted. Had that happened in this case, the anomaly between the client's circumstances and the advice received would have become apparent, enabling a further review to be undertaken and the inaccuracy obviated."

39. HMRC issued their "view of the matter" letter on 4 November 2022, which stated "My view of the matter remains as explained in my letter of 14 September 2022" without repeating any of the prior explanations and accepted the Appellants' request for an independent review.

40. HMRC's reviewing officer said in the review conclusion letter dated 16 December 2022:

> "In order to suspend a penalty for a careless inaccuracy, HMRC must be able to set at least one specific suspension condition that would help a person to avoid becoming liable to a further careless inaccuracy under Paragraph 1.
>
> In your case I am unable to identify a careless inaccuracy that will be avoided by setting conditions. There is no underlying weakness in your record keeping etc, and therefore suspension does not appear to fit in your case".

FTT DECISION ON SUSPENSION

41. The FTT's decision on HMRC's refusal to suspend the penalties is at FTT[259] to [308]. The summary below largely follows the order of the FTT Decision to record the path by which it reached its conclusions.

42. The FTT referred to paragraph 14 and in particular the specific limitation on the exercise of HMRCs discretion in paragraph 14(3) that the penalty or part of the penalty can be suspended only if compliance with the condition of suspension would help the person to avoid becoming liable to future penalties for future inaccuracies (FTT [259] and [260]).

43. The FTT recorded that all the decisions to which it was referred "accepted or did not disagree" with the proposition in *Fane* that the conditions of suspension must contain more than just a "basic requirement" that tax returns should be free from careless inaccuracies (FTT[266]). The FTT agreed with the statement in *Eastman* at [42] that "Every case must fall to be considered by reference to its own facts and circumstances" and a tribunal has to consider whether the conditions amount to no more than carrying out the tasks that reasonable and prudent taxpayers should when submitting their tax returns" (FTT[267]).

44. The FTT considered that the conditions put forward by the Appellants were no more than a basic requirement, and the decision to preclude suspension was justified and not flawed on those grounds (FTT[273]).

45. The FTT then went on to decide that, even if it was wrong in categorising the conditions put forward by the Appellants as no more than a basic requirement, it considered that the exercise of HMRC's discretion not to suspend the penalties was in any event not flawed (FTT[274]).

46. The FTT accepted that HMRC's SMART criteria are there to achieve, so far as possible, a consistency of approach by HMRC officers, and that HMRC had applied these correctly in this case (FTT[278]).

47. The conditions put forward by the Appellants related to an event that was not likely to be repeated within the specified period; HMRC would be attempting to prevent something that "cannot happen" (FTT[282]).

48. The FTT did not consider that HMRC had adopted a rigid approach, and had not decided that the inaccuracy was a one-off event and automatically precluded suspension (FTT[284]).

49. The FTT referred to the proposed condition of taking advice and the underlying behaviour which caused the inaccuracy. The FTT referred to the fact that for decades the Appellants had submitted correct tax returns; they did take advice when submitting their returns (FTT[285] to [286]).

50. The FTT disagreed with the statement at [39] in *Eastman* that "there is no necessary link between the type of inaccuracy and the possibility of further penalty" (FTT[287] to [288]). In exercising HMRC's discretion there must be some consideration of the causes of the careless inaccuracy which resulted in the penalty, but the exercise of that discretion should not be entirely specific to that and/or adopted with a rigid approach (FTT289]). Agreeing with *Testa*,

the use of the word "further" in paragraph 14(3) implies a link between the type of inaccuracy for which the original penalty has been levied and the type of inaccuracy which might give rise to further penalties (FTT[290]).

51. The FTT agreed with *Fane* that a one-off error would not normally be suitable for a suspended penalty (FTT[290]). The penalties issued to the Appellants arose because of a one-off event (FTT[293]).

52. HMRC were acting reasonably in considering whether the conditions of suspension, or any conditions of suspension, could avoid a taxpayer becoming liable to further penalties for careless inaccuracy within the period of suspension not exceeding two years by applying the SMART criteria (FTT[294]).

53. There has to be some connection between the careless error and the source of the error; and not none at all (FTT[298]).

54. The history over the previous 20 years was that the Appellants had accurately and competently completed their tax returns without requiring any of the conditions proposed (FTT[279] and [301]). The proposals to meet with a partner and go through the tax return did little more than transfer what had been carried out electronically to a face-to-face meeting (FTT[302]). HMRC had said they could not identify an underlying weakness in the Appellants' record-keeping (FTT[303]).

55. The error was in relation to a one-off event which was out of the ordinary. If there was no serious contemplation of further out of the ordinary events, there would be little likelihood of the proposed change of behaviour having any effect on future carelessness. The connection between the event and the behaviour is relevant (FTT[304] to [306]).

56. The FTT stated that it considered that the conditions put forward by the Appellants amounted to no more than a basic requirement that their tax returns should be free from careless inaccuracies; that the conditions should be and were reviewed by HMRC who carried out their due diligence in a practical and measurable manner by using the SMART criteria to achieve the statutory objective; the inaccuracy was a "one-off" error which would not normally be suitable for a suspended penalty, and that is applicable in this case (FTT[307]).

SUMMARY OF SUBMISSIONS

57. We have not considered it necessary to set out all of the parties' written and oral submissions, or to cite all of the cases to which we were referred. We have, however, taken all of these submissions into account when reaching our decision.

Summary of Appellants' Submissions

58. Mr Vallis' skeleton argument characterised the FTT decision as follows:

(1) The FTT held that the Appellants' error was a one-off event that was not likely to reoccur within the suspension period and therefore the penalty could not be suspended.

(2) The FTT held that HMRC were entitled to apply the SMART criteria even though this effectively ruled out suspension in cases of isolated or one-off inaccuracies.

(3) The FTT decision records that the consequence of using the SMART criteria is that one-off errors cannot qualify for suspension.

(4) The FTT found that HMRC restricted its discretion in accordance with its SMART criteria, the consequence of which was to prevent the suspension of penalties where HMRC cannot see any future careless errors (such as in the case of one-off errors). The FTT found that this restriction was "not flawed according to judicial review principles".

Grounds 1 and 3

59. Mr Vallis addressed Grounds 1 and 3 together and submitted that HMRC had applied their guidance in such a way that conditions related to one-off events cannot be "measurable" (by reference to the SMART criteria, namely HMRC's guidance that conditions be specific, measurable, achievable, realistic and time-bound), and submitted that the FTT had endorsed HMRC's approach, referring to in particular to FTT[278], [294] and [307].

60. Mr Vallis submitted that the FTT had recognised that guidance should not unreasonably fetter HMRC's discretion; but he accepted that it is proper for a decision-making authority to introduce guidance about the exercise of discretion.

61. Whilst Mr Vallis' skeleton argument had stated it was the Appellants' case that HMRC's policy (that suspension conditions must meet the SMART criteria) unreasonably fetters HMRC's discretion, at the hearing Mr Vallis retreated from this and confirmed the Appellants' position was not that the policy itself unreasonably fettered HMRC's discretion, but that the way it which it was applied in this case resulted in an unreasonable fettering of that discretion.

62. The focus of Mr Vallis' submissions was thus the way in which HMRC had applied the guidance.

63. Mr Vallis submitted that HMRC's application of the guidance, and its application of the SMART criteria in this way, in particular its approach to "measurable" (which he submitted amounted to an attempt to measure something that cannot be measured because it is unlikely to happen) amounted to HMRC misdirecting themselves in law. He submitted that HMRC were failing to promote the policy behind the exercise of the discretion (which he submitted is to help a taxpayer avoid future careless inaccuracies, ie focus on changing the behaviour of the taxpayer) and taken into account irrelevant considerations, namely the likelihood of the situation which gave rise to the inaccuracy recurring. He submitted that by treating inaccuracies which are unlikely to reoccur as unsuitable for suspension, HMRC has introduced an extra-statutory limitation, thereby narrowing the discretion conferred by Parliament, and in applying its guidance in this way, HMRC has unreasonably fettered its discretion.

64. Mr Vallis referred to *Eastman*, where at [38] and [39] the FTT had said:

> "38. Mr Sinclair drew our attention to a report - *Tax penalties: final report* – published by the Office of Tax Simplification in November 2014 in which it had noted the tribunal cases and had, at para 3.9 of the report, remarked that there had been a change of approach by HMRC and that updated guidance stated that it is possible to suspend penalties in instances where there have been one-off errors so long as it is possible to set appropriate suspension provisions. The guidance quoted there is from CH405050: "A penalty cannot be suspended where it is not possible to set specific conditions because the same type of inaccuracy is unlikely to happen in the future."
>
> 39. We have to say that this emphasis on the type of the inaccuracy remains vulnerable to the criticism that it unreasonably fetters the discretion of HMRC. All that para 14(3) requires is that the conditions or conditions would help the taxpayer avoid further penalties for careless inaccuracy. There is no necessary link between the type of inaccuracy and the possibility of further penalty. We respectfully disagree with the tribunal in Testa to the extent that it was suggesting, at [32], that the use of the word "further" in para 14(3) implies a link between the type of inaccuracy for which the original penalty has been levied and the type of inaccuracy which might give rise to a future penalty. In our view, the word "further" does no more than describe another penalty for careless inaccuracy that might arise in the future."

65. The FTT in this appeal had (at FTT[288]) disagreed with this statement about the emphasis on the type of the inaccuracy. Whilst the FTT did not consider that HMRC had adopted a rigid approach (FTT[284]), Mr Vallis submitted that this makes no difference where HMRC have applied the SMART criteria to conclude that suspension is not available where the inaccuracy was the result of a one-off event.

66. Further, Mr Vallis submitted that it is the condition itself which must be measurable, and the conditions proposed by the Appellants could be measured, eg that they "should have formal minuted, in-person meeting with a partner in this firm specifically to review each entry on the return before the return is submitted". Mr Vallis gave an example of a non-measurable condition as "the taxpayer should take greater care with his tax affairs in future".

Ground 2

67. Mr Vallis submitted that the FTT had erred in concluding at FTT[290] that the use of the word "further" in paragraph 14(3) implies that there must be a link between the type of inaccuracy giving rise to the penalty and any future inaccuracies, and therefore that a one-off error would not be suitable for a suspended penalty.

68. Mr Vallis submitted that, contrary to HMRC's submissions, this was not an incidental comment by the FTT - it is part of its reasoning, which the FTT had then applied to the facts at FTT[304] to [306].

69. Mr Vallis submitted that there is no basis upon which to infer such a linkage. His submissions on this point included that if Parliament had intended to require such a link, it could have done so expressly, eg by referring to "similar careless inaccuracies"; and the wording of paragraph 14(3) is clear and unambiguous such that there is no reason to seek to read an additional meaning into the words used. Instead, Mr Vallis submitted that, as explained in *Eastman*, the emphasis should be on the underlying behaviour and not the "type" of inaccuracy.

70. Mr Vallis submitted that if the decision-maker focuses on the nature of the inaccuracy, it becomes impossible to apply condition(s) of suspension in respect of penalties which have been imposed for one-off errors.

71. Mr Vallis submitted that the final condition proposed by the Appellants in their letter of 17 October 2022 (that they have a minuted, in person meeting with a partner to review each entry on the return) entirely satisfies the requirements of paragraph 14(3) and should not be rejected simply because HMRC do not foresee that the Appellants will dispose of shares within the suspension period.

Ground 4

72. Mr Vallis submitted that the FTT erred in applying the rule that conditions must amount to more than the actions of a reasonable and prudent taxpayer, and in concluding that the proposed conditions were no more than a basic requirement that future returns should be free from careless inaccuracies.

73. At FTT[295], the FTT referred to [56] of *Eastman* where the FTT had found that a condition for Mr Eastman to keep records would satisfy paragraph 14(3) even though the disposal of the business premises was a one-off event:

> "56. Having considered the evidence for ourselves, we consider that it was a failure by Mr Eastman to keep a proper record for himself of the disposal of the business premises that led to him failing to spot the error which had undoubtedly first emanated from his accountants. Although he had a file for more mundane tax documents he did not have any means of double-checking the contents of that file. That is something that is capable of remedy for the

> future, and is properly something that can be dealt with by way of a suspensive condition. It does not matter that the disposal of the business premises was a one-off event or that Mr Eastman no longer has business assets. Nor would it necessarily be a bar to a suspensive condition if he had no other chargeable assets, so long as he had a continuing requirement to make self assessment returns and thus a risk of a penalty for careless inaccuracy."

74. At FTT[296] to [297] the FTT then concluded that, as the result of this reasoning, a taxpayer could "get out of jail free" simply by following a condition that resulted in actions of a reasonable and prudent taxpayer, and considered that this cannot have been Parliament's intention.

75. Mr Vallis submitted that the FTT took the view that paragraph 14(3) could not be satisfied by the imposition of conditions whose performance amounted to the actions of a reasonable and prudent taxpayer. Mr Vallis submitted that this is an error; this is entirely the purpose of paragraph 14(3). Suspension conditions are intended to offer a careless taxpayer a structured opportunity to adopt the practices and safeguards that a prudent taxpayer would already have in place.

76. Mr Vallis referred to the decision in *Fane*, where the taxpayer had argued that the penalty should be suspended on the condition that "the Appellant correctly returned rental income in the self-assessment return" ([41]). The FTT in *Fane* said at [60] that "it is clear from the statutory context that a condition of suspension must be more than an obligation to avoid making further returns containing careless inaccuracies over the period of suspension (two years)" and concluded at [64] that:

> "64. A condition of suspension, therefore, must contain something more than just a basic requirement that tax returns should be free from careless inaccuracies. This suggests, therefore, that the condition of suspension must contain a more practical and measurable condition (e.g. improvement to systems) which would help the taxpayer to achieve the statutory objective i.e. the tax returns should be free from errors caused by a failure to exercise reasonable care."

77. Mr Vallis submitted it was then illogical for the FTT in *Fane* to have stated at [65] that "Bearing these considerations in mind, HMRC's guidance indicating that a one-off error would not normally be suitable for a suspended penalty is understandable and, in our view, justified."

78. In *Steady*, the taxpayer proposed that he could maintain a schedule of all investments held and monitor this annually to ensure that interest was accurately recorded and returned in each tax year. In that case HMRC submitted that Mr Steady's case was on all fours with that of Mr Fane, and that maintaining a spreadsheet of this sort was no more than HMRC would expect of a prudent taxpayer in any event. The FTT in *Steady* rejected that argument:

> "28. Mr Steady's case is not on all fours with Fane. In Fane, the suspension condition being considered was merely that Mr Fane file accurate self-assessment returns in future. In Mr Steady's case, it is proposed that a detailed schedule of his savings accounts is kept, and that this will help him to ensure that his tax returns are accurate in future. It matters not that a prudent taxpayer might keep such a schedule (although we would question whether a typical prudent taxpayer would keep such a schedule) – indeed it could be argued that the purpose of the suspension conditions is 10 to bring the standard of compliance of the careless taxpayer up to the standard of a prudent taxpayer. We are satisfied (and find) that a requirement to maintain a schedule of the sort described by Mrs Foyle, would be a practical and measurable condition (e.g. improvement to systems) which would help Mr Steady to achieve the

> statutory objective that his tax returns should be free from errors caused by a failure to exercise reasonable care."

79. Mr Vallis submitted that in the FTT Decision the FTT had placed a similar misconstrued reliance on *Fane*, referring to:

(1) FTT[266] where the FTT said all the cases to which they were referred accepted or did not disagree with the proposition in *Fane* that the conditions of suspension must contain more than just a basic requirement that tax returns should be free from careless inaccuracies; and

(2) FTT[273] where the FTT considered that the conditions put forward by the Appellants are "no more than a basic requirement and the decision to preclude suspension was justified and not flawed on those grounds".

80. Mr Vallis submitted that, as explained in *Steady*, the FTT in *Fane* was merely indicating that a suspensive condition must go beyond merely undertaking to be accurate next time; and there is no requirement that the conditions should require a taxpayer to do more than carrying out the tasks of a reasonable and prudent taxpayer.

81. Mr Vallis submitted that the conditions put forward by the Appellants meet the statutory requirements (and the SMART criteria).

Summary of HMRC's Submissions

82. Ms Ruxandu submitted that the FTT had rightly dismissed the Appellants' appeals, and that the Appellants' characterisation of the FTT Decision (summarised at [58] above) misrepresented that decision.

83. HMRC's position on the reasons for the officer's decision to refuse to suspend the penalties was as follows:

(1) HMRC accept that the reference in the letter of 12 July 2022 to "similar careless inaccuracies" and "a similar careless error" was wrong. However, they submit that this was accepted as an error by the officer during the course of the correspondence and was not the reason, or part of the reason, for refusing to suspend the penalties.

(2) The basis of HMRC's decision to refuse to suspend the penalties was set out in the letter of 14 September 2022, where the officer said "However, the point remains that I cannot see any future careless error(s) that could be avoided by setting a suspension condition in this case."

84. Ms Ruxandu submitted that the focus of paragraph 14 is improvements in taxpayer behaviour to help to reduce the risk of careless inaccuracies in the future, and that if it was not possible to identify future errors that could arise, or if no improvement could be identified, then it is not possible to set a condition to help to reduce such risk. Ms Ruxandu submitted that it is implicit in paragraph 14(3) that there must be cases where HMRC cannot set a condition that would satisfy 14(3).

85. HMRC agrees and accepts that there is no automatic decision or presumption that it is not appropriate to suspend a penalty where the careless inaccuracy for which the taxpayer is liable to a penalty arises from a one-off event. However, HMRC's position is that the one-off nature of the inaccuracy is one factor to be taken into account when considering whether to decide to suspend a penalty; the nature of the inaccuracy is a relevant consideration, such that failing to take account of this would be wrong in law. HMRC does therefore depart from the approach it had adopted in *Fane* (and *Steady*) and from that decision.

86. The conditions proposed by the Appellants related to taking advice. The FTT found at FTT[286] that for decades the Appellants "had submitted correct tax returns using an established communication method with their accountant" and at FTT[302] that "the proposals to meet with a partner and go through the tax return did little more than transfer what had been carried out electronically to a face-to-face meeting". Ms Ruxandu submitted that in this situation, such a condition was, on the basis of these facts, precluded by paragraph 14(3); no condition was appropriate or could improve their behaviour. Ms Ruxandu accepted that HMRC's position was that the same type of careless behaviour by two different taxpayers with, eg, a different approach to record-keeping, may result in a different decision on whether a condition of suspension could be imposed.

87. Ms Ruxandu submitted that a taxpayer does not automatically qualify for a penalty to be suspended as a result of previous good behaviour. Parliament could have taken this approach, eg the points system used in VAT, but has not done so.

88. Ms Ruxandu submitted that HMRC's decision to refuse to suspend the penalties was made on 3 October 2022, when the penalties were issued to the Appellants. When considering whether that decision was flawed, it was, she submitted, the facts, matters and circumstances known to HMRC at the time that were relevant and it was irrelevant that an alternative condition was put forward by the Appellants on 17 October 2022. In any event, she submitted that the view of the matter letter (and subsequent review conclusion letter) engages with this proposal.

Grounds 1 and 3

89. Ms Ruxandu submitted that HMRC had not followed a rule that a penalty cannot be suspended where a similar inaccuracy is unlikely to happen in the future. The FTT had found to this effect, finding at FTT[284] that HMRC had not adopted a rigid approach. Ms Ruxandu submitted that the SMART criteria are not deemed to exclude the possibility of suspension in the case of one-off inaccuracies. The Appellants do not point to any finding by the FTT that they apply in this way.

Ground 2

90. Ms Ruxandu submitted that this was not the basis for HMRC's decision to refuse suspension. Whilst this comment was made by the FTT, HMRC's decision was not based on there being no link between the type of the inaccuracy and any future inaccuracies; it was based on the fact that the officer could not identify any future inaccuracies (whether linked or not). This ground of appeal therefore makes no difference to the outcome. In any event, HMRC's position is that there must be some link between the behaviour which led to the careless inaccuracy and the suspension conditions which would help to avoid a further inaccuracy.

Ground 4

91. Ms Ruxandu submitted that this was not the basis of HMRC's decision. Here, the conditions proposed by the Appellants were little more than what was already done by the Appellants. In any event, the FTT was correct in finding that general "basic requirements" would not be suitable conditions for suspension, as this would make paragraph 14(3) entirely unnecessary as there would always be a possible general and basic condition capable of lowering a hypothetical risk of inaccuracy.

92. Ms Ruxandu submitted that the Upper Tribunal should dismiss the appeals. If we were to allow the appeals and remake the decision, we could only order HMRC to suspend the penalties if we considered that a condition of suspension could be imposed that would satisfy paragraph 14(3), albeit we could not require HMRC to impose that condition. She submitted that the conditions proposed by the Appellants would not satisfy paragraph 14(3).

PARAGRAPH 14 AND THE DISCRETION AFFORDED TO HMRC

93. Schedule 24 Finance Act 2007 sets out the provisions in relation to penalties for errors, including provisions relating to the calculation of the penalty for careless inaccuracies and deliberate inaccuracies by reference to the "potential lost revenue" and the reductions available for disclosure. Paragraph 14 then deals with suspension, and only applies where it has been determined that there was an inaccuracy in a document and such inaccuracy was careless.

94. Paragraph 14(1) provides that HMRC "may suspend all or part of a penalty for a careless inaccuracy" by giving notice to the taxpayer. Whilst this discretion is expressed broadly, paragraph 14 does include some restrictions and guidance on the exercise of HMRC's discretion to suspend a penalty for a careless inaccuracy:

(1) Paragraph 14(3) provides that HMRC may suspend a penalty "only if compliance with a condition of suspension would help P to avoid becoming liable to further penalties under paragraph 1". A penalty can therefore only be suspended if a condition can be imposed as well as a period of suspension not exceeding two years (which must be specified in the notice under paragraph 14(2)) – we agree with Ms Ruxandu that paragraph 14 thus contemplates that there may be some scenarios in which a penalty cannot be suspended. Paragraph 14(3) has also prescribed the purpose of the condition, namely to help the taxpayer avoid becoming liable to further penalties.

(2) Paragraph 14(5) provides that on the expiry of the period of suspension, if the taxpayer satisfies HMRC that the condition(s) of suspension have been complied with, the suspended penalty is cancelled, otherwise it becomes payable. This makes it clear that the condition must be one which can be complied with, and in respect of which the taxpayer can demonstrate to HMRC (to HMRC's satisfaction) that they have complied.

95. Paragraph 14(6) then provides that if the taxpayer "becomes liable for another penalty" under paragraph 1 during the period of suspension, the penalty for the careless inaccuracy becomes payable.

96. We agree with the FTT in *Eastman* at [33], and it was common ground between the parties, that:

> "33. It is necessary, in order that HMRC can operate fairly amongst all taxpayers, that guidance is issued to officers tasked with the exercise of a discretion such as that which applies to the question of the suspension of a penalty. But that guidance should go no further than is required to ensure consistency of approach. It should not fetter the discretion of an HMRC officer otherwise than is consistent with the legislative scheme itself. If it does, then any decision which is constrained in that way will be likely to be flawed in the sense provided for by para 17(6)."

97. HMRC's published guidance sets out that the conditions to be imposed have to be considered according to the "SMART" criteria, namely whether they are specific, measurable, achievable, realistic and time-bound. HMRC has updated this guidance from time-to-time. As recorded above, Mr Vallis confirmed at the hearing that the Appellants do not challenge HMRC's policy (or guidance) that conditions of suspension should meet these SMART criteria.

98. The parties made detailed submissions in relation to whether paragraph 14 requires a link between the careless inaccuracy in respect of which the taxpayer is liable to the penalty and any future inaccuracy for which the taxpayer may become liable for a penalty, addressing the use of the word "further" in paragraph 14(3) and referring in particular to the decisions in *Fane*, *Testa, Steady* and *Eastman,* and how this applies or should apply where the careless inaccuracy is in respect of a one-off event. We need to consider some of these decisions, as in the FTT

Decision the FTT stated its agreement or disagreement with parts of these decisions (which themselves commented on the earlier decisions).

99. In *Fane* the FTT identified at [58] that the important feature of paragraph 14(3) is "the link between the condition and the statutory objective: there must be a condition which would help the taxpayer to avoid becoming liable for further careless inaccuracy penalties". The officer had considered that a condition of suspension could not properly apply to a "one-off event" ([59]). The FTT said on the face of the wording of paragraph 14(3) there is no restriction in respect of a one-off event ([60]). The FTT cited paragraph 14(6) and stated that if the condition was simply that, eg, the taxpayer must file tax returns free from material careless inaccuracies, paragraph 14(6) would be redundant ([61]) and it is difficult to see how a taxpayer could satisfy HMRC that such a condition had been satisfied ([62]). The FTT nevertheless concluded that HMRC's guidance indicating that a one-off error would not normally be suitable for a suspended penalty was understandable and justified.

100. Whilst the FTT in *Fane* did briefly raise the issue of a "link", that was in the context of a link between the condition and the statutory objective. It was more fully considered by the FTT in *Testa*:

> "31. The apparent underlying purpose of the legislation is not simply to allow a taxpayer the opportunity of "a last chance" if he mends his ways (akin to a suspended sentence in the criminal sphere) but only to allow him that last chance if he takes some specific and observable action which is specifically designed to improve his compliance.
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> 32. Although the legislation does not specify the nature or extent of the required linkage between the earlier default and the action required by the suspensive condition, the use of the word "further" in paragraph 14(3) seems to us to imply that there must be some such linkage.
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> 33. It therefore seems unlikely that paragraph 14(3) is intended to cover a situation where, for example, a taxpayer carelessly gives inaccurate information in a Construction Industry Scheme return and then seeks to have the penalty suspended on the basis of a promised improvement in his PAYE record keeping processes.
>
> 34. On the other hand, consider a case in which the original inaccuracy had arisen, say, because of a particular weakness in the taxpayer's system for distinguishing between CIS payments for materials and construction services in certain unique circumstances. Let us assume the taxpayer, alarmed by the problem, had instructed an external professional firm to carry out a full review of its whole CIS reporting process and obtained a report giving recommendations for its improvement (including the elimination of the weakness that gave rise to the particular error, even though it was unlikely to recur). If the taxpayer offered to agree a condition requiring it to implement those recommendations, that would surely meet the underlying purpose of the legislation and fall within paragraph 14(3), even if the circumstances giving rise to the particular error were a "one off" and unlikely ever to be repeated.
>
> 35. HMRC's policy (as referred to in their letters referred to at [11] and [13] above) sits uneasily with the above example. If their stance were correct that "one-off" inaccuracies (or inaccuracies arising from "one off" events) could never benefit from the suspension regime, then they would refuse to allow the suspension. This must in our view be wrong. Instead in such a case they should simply consider whether the implementation of the external report would help the taxpayer to avoid future inaccuracies in its CIS returns."

101. This decision in *Testa* was then considered by the FTT in *Eastman*:

"38. Mr Sinclair drew our attention to a report - Tax penalties: final report – published by the Office of Tax Simplification in November 2014 in which it had noted the tribunal cases and had, at para 3.9 of the report, remarked that there had been a change of approach by HMRC and that updated guidance stated that it is possible to suspend penalties in instances where there have been one-off errors so long as it is possible to set appropriate suspension provisions. The guidance quoted there is from CH405050: "A penalty cannot be suspended where it is not possible to set specific conditions because the same type of inaccuracy is unlikely to happen in the future."

39. We have to say that this emphasis on the type of the inaccuracy remains vulnerable to the criticism that it unreasonably fetters the discretion of HMRC. All that para 14(3) requires is that the conditions or conditions would help the taxpayer avoid further penalties for careless inaccuracy. There is no necessary link between the type of inaccuracy and the possibility of further penalty. We respectfully disagree with the tribunal in *Testa* to the extent that it was suggesting, at [32], that the use of the word "further" in para 14(3) implies a link between the type of inaccuracy for which the original penalty has been levied and the type of inaccuracy which might give rise to a future penalty. In our view, the word "further" does no more than describe another penalty for careless inaccuracy that might arise in the future.

40. Whilst the nature of the inaccuracy in respect of which the penalty has been levied is a relevant factor for HMRC to consider in the exercise of their discretion, we do not consider that it should constrain the nature of the inaccuracies available to be considered for the purpose of determining whether conditions may be imposed which will help avoid penalties for carelessness in those respects as well as those related to the original inaccuracy. Paragraph 14(3) does not differentiate between types of careless inaccuracy any more than the provisions imposing the penalty do.

41. In the same way that the penalty for careless inaccuracy seeks to deter careless behaviour and penalise it, para 14 recognises that the imposition of conditions may alter behaviour so as to avoid that behaviour being repeated. It is therefore necessary, in exercising a discretion, for the decision-maker to have regard to the underlying behaviour that has given rise to the penalty and to determine whether a condition may be imposed to affect or obviate that same behaviour in the future. That is not something that is confined to the nature of the original inaccuracy, including whether it arose as a consequence of a one-off event that is not expected to be repeated.

42. We do not consider that the Explanatory Notes to the Finance Bill 2007 are of assistance in this respect. In our judgment they do not reflect the statutory language that has been used. To the extent that those Notes are sought to be relied upon to restrict, beyond the language of para 14(3), the cases where discretion in favour of a suspended penalty may be exercised, we consider that they represent an unwarranted fetter on the exercise of that discretion. Every case must fall to be considered by reference to its own facts and circumstances.

43. In considering whether any appropriate conditions may be imposed, the acid test, in our view, is to ask what the taxpayer could reasonably have done differently that would have avoided the original inaccuracy. That, in different words, is a similar approach to that adopted most recently by the tribunal in *Paul Ronald Steady v Revenue and Customs Commissioners* [2016] UKFTT 473 (TC) where it said, at [28], that it could be argued that the purpose of the suspension conditions is to bring the standard of compliance up to the level of a prudent taxpayer. Having ascertained what could have been done in that

> respect, the question is whether, educated by that answer, a condition may be imposed which would help avoid future careless inaccuracies. As a penalty would not differentiate between types of inaccuracy, the condition must encompass all risks of future careless inaccuracy that can reasonably be identified.
>
> …
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> 56. Having considered the evidence for ourselves, we consider that it was a failure by Mr Eastman to keep a proper record for himself of the disposal of the business premises that led to him failing to spot the error which had undoubtedly first emanated from his accountants. Although he had a file for more mundane tax documents he did not have any means of double-checking the contents of that file. That is something that is capable of remedy for the future, and is properly something that can be dealt with by way of a suspensive condition. It does not matter that the disposal of the business premises was a one-off event or that Mr Eastman no longer has business assets. Nor would it necessarily be a bar to a suspensive condition if he had no other chargeable assets, so long as he had a continuing requirement to make self assessment returns and thus a risk of a penalty for careless inaccuracy. In fact, of course, he does continue to own chargeable assets on which capital gains may have to be accounted for."

102. It is clear from the lengthy summary of the parties' submissions in the FTT Decision that these decisions were cited to the FTT, and the FTT set out its conclusions on some of the points raised (although before us Mr Vallis and Ms Ruxandu disagreed as to whether these formed part of the reasons for the FTT's decision):

(1) The FTT cited [37] of *Eastman* at FTT[283] and found at FTT[284] that HMRC had not adopted a rigid approach and decided that the inaccuracy was a one-off event and automatically precluded suspension.

(2) The FTT cited [39] of *Eastman* (where it was said that all that paragraph 14(3) requires is that the condition(s) would help avoid further penalties for careless inaccuracy and that there is no necessary link between the type of inaccuracy and the possibility of further penalty) and disagreed (FTT[287] to [288]).

(3) At FTT[290] the FTT agreed with *Testa* at [32] that the use of the word "further" in paragraph 14(3) implies a link between the type of inaccuracy for which the original penalty has been levied and the type of inaccuracy which might give rise to further penalties and with *Fane* that a one-off error would not normally be suitable for a suspended penalty.

(4) The FTT cited [56] of *Eastman* and said this suggested that anyone required to make future tax returns and who sets out conditions which may amount to the actions of a reasonable and prudent taxpayer, or little more than that, should have a penalty suspended and brings into question the purpose of having a system of penalties, rather than suspensive penalties, for careless inaccuracies (FTT[295] to [296]). The FTT considered it cannot have been Parliament's intention that paragraph 14 should become a "get out of jail free" card; there has to be some connection between the careless error and the source of the error, and not none at all (FTT[297] to [298]).

(5) At FTT[306] the FTT considered that the connection referred to in *Fane* between the event and behaviour is relevant. This reference to *Fane* should, we consider, be a reference to *Testa*.

103. Paragraph 14 does not require that there be a link between the type of inaccuracy for which the penalty in issue has been levied and the type of inaccuracy which might give rise to a penalty in the future, whether "type" be explained by reference to the tax in issue or the event being returned (one-off or recurring); accordingly, there is no need that the future inaccuracy be "similar" to the careless inaccuracy to which the penalty relates. We accept Mr Vallis' submissions that the statutory language does not require such an interpretation, and consider HMRC are correct to accept that suspension is not automatically precluded where the careless inaccuracy which has resulted in a penalty is a one-off event. This does not, however, mean that there is no link or connection between the careless inaccuracy and the possibility of any further penalty. Paragraph 14(3) requires that the condition "would help P to avoid" becoming liable for further penalties for careless inaccuracy: as the parties agreed, this focuses on the behaviour of the particular taxpayer, including the basis on which it was concluded that such taxpayer was careless, and what would help that taxpayer to avoid further careless inaccuracies.

104. Looking at the position which had been reached in earlier decisions, the FTT in *Eastman* had said at [39] that there is "no necessary link between the type of inaccuracy and the possibility of further penalty". They disagreed with *Testa* "to the extent" it was suggesting at [32] that the use of the word "further" implies a link between the type of inaccuracy for which the original penalty has been levied and the type of inaccuracy which might give rise to a future penalty; in the view of the FTT in *Eastman*, the word "further" does no more than describe another penalty for careless inaccuracy that might arise in the future. As to these points:

(1) We do not consider that the FTT in *Testa* had decided that the implied link was between the type of inaccuracy which gave rise to the careless penalty and the type of inaccuracy which might give rise to a future penalty. The FTT had said that the use of the word "further" in paragraph 14(3) implied "some such linkage" between the earlier default and the action required by the suspensive condition (at [32]); and the example it gave in [34] contemplated a condition requiring a taxpayer to implement recommendations even if the circumstances giving rise to the particular error were a one-off and unlikely ever to be repeated. The FTT was not implying a link between the type of inaccuracy on each occasion. (For completeness, we record that the FTT in *Testa* gave the example at [33] where the careless inaccuracy was in a Construction Industry Scheme ("CIS") return but the condition proposed related to a promised improvement in record-keeping processes for PAYE. The FTT suggested it seemed unlikely that paragraph 14(3) was intended to cover this situation, contrasting it at [34] with a case where the original inaccuracy had arisen because of a particular weakness in the taxpayer's system. We are not persuaded by this example – if the inaccuracy in the CIS return was a result of poor record-keeping, then a condition related to record-keeping may well help to avoid future careless inaccuracies and the fact that the returns relate to different taxes should not necessarily preclude such a condition of suspension.)

(2) Even though the FTT in *Eastman* said at [39] that there is no necessary link between the type of inaccuracy and the possibility of further penalty, the FTT then accepted that the nature of the inaccuracy in respect of which the penalty has been levied is a relevant factor for HMRC to consider in the exercise of their discretion (at [40]), and that it is necessary for the decision-maker to have regard to the underlying behaviour that has given rise to the penalty and to determine whether a condition may be imposed to affect or obviate that same behaviour in the future (at [41]). The FTT was thus nevertheless looking for some form of link or connection as a way of specifying a condition to improve taxpayer behaviour having regard to the careless inaccuracy which had occurred. That is what the FTT then identified in its decision on the facts at [56]; we consider it was seeking

to identify "some specific and observable action which is specifically designed to improve his compliance" (using the language of the FTT at [31] in *Testa*).

105. Whilst the parties agreed that paragraph 14 requires that HMRC focus on the behaviour of the taxpayer whose document contained a careless inaccuracy when considering whether to exercise their discretion to suspend a penalty, they placed different emphases on the basis for any condition of suspension. Ms Ruxandu submitted that any condition of suspension needed to address a specific improvement in the taxpayer's behaviour; whereas Mr Vallis submitted that it was not about improvement per se but about instilling good practice.

106. We agree with Ms Ruxandu that paragraph 14 envisages that the condition would be intended to change or improve the taxpayer's behaviour. The premise is that the taxpayer has submitted a return (or other document) that contained a careless inaccuracy, and paragraph 14(3) requires that the condition must help them to avoid becoming liable for further penalties, ie making further errors. This involves identifying, essentially, what went wrong, and what the taxpayer could reasonably have done differently that would have avoided, or helped to avoid, the inaccuracy. The type or nature of the inaccuracy is a relevant factor to be considered for this purpose, but it is just that, a relevant factor, and not determinative. The decision-maker then needs to consider whether there is a condition of suspension which would help to avoid, or reduce the risk, of that taxpayer making further errors in the future. This may involve specifying actions which are regarded as good practice for reasonable and prudent taxpayers, but in any event should represent an improvement in the particular taxpayer's previous practice or behaviour.

107. Having set out the above, we now turn to the Appellants' grounds of appeal by reference to the decision of HMRC to refuse to suspend the penalties and the FTT's conclusion that this decision was not flawed.

108. As to the making of the decision by HMRC and the relevant date for the purpose of considering whether that decision was flawed, the penalties were issued on 3 October 2022, and Ms Ruxandu submitted that this was when HMRC's decision to refuse suspension was made, such that facts, matters and circumstances arising subsequently (here, the Appellants' letter of 17 October 2022 proposing an alternative condition of suspension and HMRC's responses thereto) are not relevant when considering a challenge to a decision on the basis of principles of judicial review. We disagree; whilst HMRC had taken a decision not to suspend when it issued the penalties (with its reasons having been set out the previous month), the statutory review process enables that decision to be re-examined following such further submissions as may be received and then either upheld or amended. The decision was upheld, and the appeal to the FTT was in respect of that decision as upheld on 16 December 2022.

GROUNDS 1 AND 3

109. Grounds 1 and 3 are as follows:

(1) the FTT was wrong to conclude (see for example FTT[287] and [288]) that HMRC had not unreasonably fettered their discretion in following the rule that a penalty cannot be suspended where it is not possible to set conditions because a similar inaccuracy is unlikely to happen in the future (see for example FTT[65]); and

(2) the FTT was wrong to conclude that HMRC had not unreasonably fettered their discretion by applying the SMART criteria (insofar as these criteria are deemed to exclude the possibility of suspension in cases of one-off inaccuracies).

Discussion and conclusions

110. Mr Vallis submitted that the FTT made an error of law in concluding that HMRC had not unreasonably fettered their discretion in following the rule that a penalty cannot be suspended

where it is not possible to set conditions because a similar inaccuracy is unlikely to happen in the future.

111. As explained below, whilst we agree with Mr Vallis' submission that paragraph 14 does not require that any further penalties are for a similar inaccuracy, this was not the reason (or one of the reasons) for HMRC's decision to refuse to suspend the penalties. The FTT did not then conclude that HMRC had followed such a rule, or that it was not an unreasonable fetter on HMRC's discretion to follow a rule that a penalty cannot be suspended where it is not possible to set conditions because a similar inaccuracy is unlikely to happen in the future.

112. In Ground 1 Mr Vallis refers specifically to FTT[65] as an example, where the FTT quotes from HMRC's letter of 12 July 2022 (in which HMRC referred in two places to it being unlikely that a "similar" careless inaccuracy will arise in the future). However, this was not the basis of HMRC's decision. It is clear from the subsequent correspondence that HMRC's position changed. On 21 August 2022 the Appellants challenged HMRC's reference to the inaccuracy being "similar", stating that this was not the test required by the legislation, and in their letter of 14 September 2022 HMRC accepted that the legislation did not refer to the inaccuracy being "similar", and said that this was from HMRC's guidance. HMRC acknowledged that the legislation is not specific regarding which careless errors could be avoided in future, and went on to say that they could not see "any future careless errors" that could be avoided by setting a suspension condition. HMRC's view of the matter letter referred back to this letter of 14 September 2022 (albeit without further explanation) and the reviewing officer stated on 16 December 2022 that they were "unable to identify a careless inaccuracy that will be avoided by setting conditions", adding that there is no underlying weakness in the Appellants' record-keeping, etc, and suspension does not appear to fit in this case.

113. The FTT identified these reasons in HMRC's letter of 14 September 2022 at FTT[72] to [73]. The FTT's subsequent discussion of HMRC's decision to refuse to suspend the penalties is not based on HMRC having considered that further penalties would need to be for a similar inaccuracy. Indeed, the part of the FTT Decision which discusses suspension (FTT[259] to [308]) does not contain any reference to a "similar inaccuracy". Instead, the FTT were addressing the reasons why HMRC could not identify any future careless errors, which included:

(1) for decades the Appellants had submitted correct tax returns using an established communication method with their accountant (FTT[286]);

(2) the penalties arose from a one-off event (FTT[293] and FTT[304]); and

(3) the history over the previous 20 years was that the Appellants had accurately and competently completed their tax returns without requiring any of the conditions proposed for suspension of their penalties (FTT[301]).

114. The FTT did find that the penalties arose from a one-off event, and they took this into account, they made findings which supported HMRC's decision that they could not identify any future careless errors or inaccuracies that could be avoided by setting a condition of suspension by reference to the Appellants' earlier behaviour.

115. Ground 1 also refers to FTT[287] and [288], expressly stating that these were examples of the alleged error of law by the FTT. These paragraphs provide:

> "287. The Eastman Tribunal stated at [39] that the emphasis on the type of inaccuracy:
>
> "…remains vulnerable to the criticism that it unreasonably fetters the discretion of HMRC. All that para 14(3) requires is that the conditions or conditions (sic) would help avoid further penalties for careless inaccuracy.

> There is no necessary link between the type of inaccuracy and the possibility of further penalty."
>
> 288. The tribunal respectfully disagrees."

116. We have explained our conclusion that paragraph 14 does not require that there be a link between the type of inaccuracy for which the penalty in issue has been levied and the type of inaccuracy which might give rise to a penalty in the future; but that this does not mean that there is no link or connection between the careless inaccuracy and the possibility of any further penalty. Viewing these two paragraphs of the FTT Decision in isolation, we agree with Mr Vallis' submission that the FTT made an error of law in stating its disagreement to this part of [39] of *Eastman*. However, importantly, not only was this not the basis of HMRC's decision to refuse to suspend the penalties (and therefore it is not material to the FTT's decision that HMRC's decision was not flawed) but in any event it needs to be read in the context of the FTT Decision as a whole.

117. We have set out above the basis of HMRC's decision. It was not that there is a necessary link between the type of inaccuracy and the possibility of further penalty. Furthermore, the approach taken by the FTT was as follows:

(1) The FTT had referred at FTT[285] to the Appellants' proposed condition of taking advice and HMRC's response, and stated at FTT[286] that this is relevant to considering the "underlying behaviour which caused the inaccuracy" (citing *Eastman*) – they had taken advice and thought that this was unchanged when their circumstances changed, and the Appellants had submitted correct tax returns for decades using an established communication method with their accountant.

(2) The FTT then cited *Eastman* and disagreed at FTT[287] to [288].

(3) At FTT[289] the FTT said it considered that "in exercising HMRC's discretion there must be some consideration of the causes of the careless inaccuracy which resulted in the penalty, but the exercise of that discretion should not be entirely specific to that and/or adopted with "a rigid approach"".

(4) At FTT[290] the FTT stated it agreed with *Testa* that the use of the word "further" in paragraph 14(3) implies a link between the type of inaccuracy which might give rise to further penalties and with *Fane* that a "one-off" error would not normally be suitable for a suspended penalty.

(5) The FTT considered the penalties were levied on the Appellants because of a one-off event (FTT[293]).

(6) HMRC were acting reasonably in considering whether the conditions of suspension, or any conditions of suspension, could avoid a taxpayer becoming liable for further penalties within the period of suspension by applying the SMART criteria (FTT[294]).

(7) Its concluding paragraphs explaining its decision were then:

> "301. The history over the previous 20 years, prior to the submission of the 2019-20 tax return, was that PDC had accurately and competently completed their tax returns without requiring any of the conditions proposed for suspension of their penalties.
>
> 302. The tribunal agreed with HMRC's submission that the proposals to meet with a partner and go through the tax return did little more than transfer what had been carried out electronically to a face-to-face meeting.

> 303. HMRC said in respect of the proposals, that they could identify "no underlying weakness in your record keeping etc. and therefore suspension does not appear to fit in your case."
>
> 304. The error was in relation to a 'one-off' event which was out of the ordinary for the completion of PDC's tax returns.
>
> 305. If there was no serious contemplation of further out of the ordinary events, there would be little likelihood of the proposed change of behaviour having any effect on future carelessness.
>
> 306. Accordingly, the tribunal considered that the connection referred to in [*Testa*] between the event and behaviour is relevant and that in the case of PDC was evident.
>
> 307. The tribunal considered; that the conditions put forward by PDC amounted to no more than a basic requirement that their tax returns should be free from careless inaccuracies; that that the conditions should be and were reviewed by HMRC who carried out their due diligence in a practical and measurable manner by using the SMART criteria to achieve the statutory objective to consider whether the penalty should be suspended; and that the inaccuracy was a 'one off' error which would not normally be suitable for a suspended penalty, and that is applicable in this case."

118. The FTT did follow the approach it had identified at FTT[289] – it looked at the causes of the inaccuracy, in particular the Appellants' not having taken advice which reflected their changed circumstances, identified that this was a one-off error, that HMRC had not identified an underlying weakness in their record keeping, etc, looked at the previous submission of accurate returns over a period of 20 years, and found that if there was no serious contemplation of further out of the ordinary events, there would be little likelihood of the proposed change of behaviour having any effect on future carelessness.

119. Whilst the FTT erred at FTT[288] and FTT[290], these paragraphs were not the basis of HMRC's decision, nor that of the FTT. The FTT did not hold, contrary to Mr Vallis' skeleton argument at [34], that the Appellants' error was a one-off event that was not likely to reoccur within the suspension period and that therefore the penalties could not be suspended.

120. Ground 3 is based on the SMART criteria being deemed to exclude the possibility of suspension in cases of one-off inaccuracies. Mr Vallis confirmed at the hearing that the Appellants' submission was that it was HMRC's application of the SMART criteria which led to this result.

121. We do not accept Mr Vallis' submissions in relation to HMRC's application of the SMART criteria.

122. HMRC did apply the SMART criteria, that any condition be specific, measurable, achievable, realistic and time-bound (as found by the FTT at, eg, FTT[294]). As the FTT identified at FTT[53], HMRC had referred to these criteria from the outset when considering whether to suspend the penalties. The FTT agreed that HMRC were acting reasonably in taking this approach, eg saying that HMRC had applied these criteria correctly at FTT[278].

123. Mr Vallis drew attention to the fact that in the correspondence HMRC referred specifically to the criteria that any condition be measurable:

> (1) In their letter of 12 July 2022, HMRC said that "as it seems unlikely that a similar careless error will occur again, I find it difficult to see how any suspension condition relating to this could be measured (as per the SMART criteria)" (FTT[65]).

(2) On 21 August 2022, the Appellants suggested that the failure (ie the carelessness which had been found) could be attributed to the advice being targeted on the transaction as a whole. They proposed a condition that they would appoint separate advisers dedicated to their circumstances and any advice would be confirmed in writing. On 14 September 2022, HMRC, having set out "the point remains that I cannot see any future careless error(s) that could be avoided by setting a suspension condition", went on to respond to the condition which had been proposed. HMRC said this was not a measurable condition, as it was not definite but rather an action that could be taken if the situation arose; and such a situation may not arise within the suspension period such that adherence could not be measured (FTT[73] to [74]).

124. We do not agree that a condition requiring a taxpayer to take advice is not measurable – it would be possible for a taxpayer to demonstrate that they had obtained advice in relation to a transaction, or that no transaction had taken place such that there was no need to obtain advice. We might therefore have been able to be persuaded that rejecting a condition on this basis was unreasonable. The difficulty for the Appellants is that HMRC did not refuse to suspend as this proposed condition was not measurable but because, even after taking account of the alternative condition subsequently proposed (which the FTT found they did at FTT[281]), HMRC concluded that they could not see any future careless errors that could be avoided; they could not see any condition that would satisfy paragraph 14(3). This reasoning was repeated in HMRC's subsequent letters, after the Appellants had proposed the condition that the Appellants have a formal minuted in-person meeting with a partner to go through each entry in the return. HMRC have not said that this was not measurable.

125. The only reference by the FTT to whether the condition was measurable was at FTT[284] where the FTT said:

> "284. The tribunal did not consider that HMRC had adopted a rigid approach and, therefore, decided that PDC's inaccuracy was a 'one off' event and automatically precluded suspension. HMRC set out their reasons with reference to the SMART criteria The promise to check with an advisor in future was not measurable and did not relate to a specific action. It could not, HMRC, say be measured."

126. Whilst the first sentence above is clearly a conclusion of the FTT and stated to be such (and it is a conclusion in respect of which the Appellants were refused permission to appeal), the remainder is a summary of what HMRC had said in correspondence. It is not a finding or a conclusion of the FTT.

127. The SMART criteria are not deemed to exclude the possibility of suspension in case of one-off inaccuracies, and the FTT did not find that this was the case; and in any event the FTT concluded that HMRC had not applied a rigid approach and that the inaccuracy being a one-off event automatically precluded suspension.

128. In conclusion, Grounds 1 and 3 do not accurately set out the basis on which the FTT had concluded that HMRC's decision to refuse to suspend the penalties was not flawed. We are not persuaded that the decision by the FTT involved the making of an error of law on these grounds, and accordingly the Appellants' appeals on these grounds must be dismissed.

GROUND 2

129. Ground 2 is that the FTT erred in concluding that there must, by virtue of paragraph 14(3), be a link between the type of inaccuracy giving rise to the penalty and any future inaccuracies, and therefore that a "one-off" error would not be suitable for a suspended penalty (see FTT[290]):

> "290. The tribunal agrees with the Testa Tribunal at [32] that the use of the word 'further' in paragraph 14(3) implies a link between the type of inaccuracy for which the original penalty has been levied and the type of inaccuracy which might give rise to further penalties and with the Fane Tribunal and the Webb Tribunal decisions that a 'one off' error would not normally be suitable for a suspended penalty."

130. Whilst Mr Vallis addressed Grounds 1 and 3 together, he addressed Ground 2 separately and we follow that approach.

Discussion and conclusions

131. Grounds 1 and 3 focused on the decision which was made by HMRC and what the Appellants submitted were the FTT's conclusions in relation to that decision. Ground 2 is based on what are said to be the FTT's conclusions on particular issues.

132. There are two related limbs within FTT[290] on which this ground of appeal is based:

(1) the use of the word "further" in paragraph 14(3) implies a link between the type of inaccuracy for which the penalty has been levied and the type of inaccuracy which might give rise to further penalties – we have set out above our conclusions that paragraph 14 does not require that there be a link between the type of inaccuracy for which the penalty in issue has been levied and the type of inaccuracy which might give rise to a penalty in the future, and that the FTT in *Testa* did not decide that such a link was implied. On this basis, the FTT did make an error of law at FTT[290] when it said that there is an implied link between the types of inaccuracy; and

(2) a one-off error would not normally be suitable for a suspended penalty – the FTT did not, contrary to the way that Ground 2 is expressed, find that a one-off error would not be suitable for a suspended penalty (which would here have resulted in an automatic conclusion that HMRC could not suspend the penalties levied on the Appellants) but said it would not normally be suitable. We do not agree, and as set out above we prefer the formulation that suspension is not automatically precluded where the careless inaccuracy which has resulted in a penalty is a one-off event.

133. Whilst we therefore find that the FTT did make an error of law in setting out these principles at FTT[290], this does not assist the Appellants as it was not material to its decision (in that we are not satisfied that it might have made a difference to the outcome). HMRC's decision was not based on a link being required between the type of inaccuracy; nor did HMRC conclude that a one-off error would not normally be suitable for suspension. The FTT found that HMRC had not adopted a rigid approach and had not decided that the one-off event automatically precluded suspension. This is a sufficient reason to dismiss the Appellants' appeal on this ground.

134. We would add that, whilst Mr Vallis submitted that the principles expressed at FTT[290] then flowed into the FTT's conclusions at FTT[304] to [306], those paragraphs are prefaced by the FTT setting out the wider circumstances, including the basis on which it had concluded that the Appellants were careless and that for decades they had submitted correct tax returns using an established communication method with their accountant, and the FTT's agreement with HMRC that the proposals to meet with a partner and go through the tax return (ie the proposal put forward on 17 October 2022) did little more than transfer what had been carried out electronically to a face-to-face meeting.

GROUND 4

135. Ground 4 is that the FTT erred in applying the rule that the conditions applied must amount to more than "the actions of a reasonable and prudent taxpayer" (see FTT[296]) and in

concluding that the proposed conditions for suspension were inappropriate as they were "no more than a basic requirement" (see FTT[273]) that future returns should be free from careless inaccuracies, where it is the purpose of the legislation to encourage taxpayers to act reasonably and prudently (ie not carelessly) and, indeed, a taxpayer can do no more than submit a return free from careless inaccuracies.

Discussion and conclusions

136. We are not persuaded that this reasoning was, on the facts, the basis of either HMRC's decision or that of the FTT.

137. The statement that a condition of suspension must be "more than just a basic requirement" was first made in these terms at [64] of *Fane*, where the FTT reasoned that if the condition was simply that, eg, the taxpayer must file tax returns for two years free from material careless inaccuracies, then paragraph 14(6) would be redundant ([61]) and it would be difficult to see how a taxpayer could satisfy HMRC that such a condition had been satisfied as required by paragraph 14(6) ([62]). We agree with this reasoning of the FTT in *Fane*.

138. HMRC did not rely on this reasoning when making its decision in respect of the Appellants. HMRC did, arguably, have this in mind in their letter of 14 September 2022 when they stated "Additionally, seeking appropriate advice where required…is a responsibility already expected of reasonable taxpayers…". That was responding to an earlier condition which had been proposed by the Appellants in their letter of 21 August 2022. The Appellants subsequently proposed a more specific condition involving a meeting to review each entry on the return before submission. That proposal was rejected, not as being not specific, or something already expected, but on the basis that HMRC could not identify a careless inaccuracy that would be avoided by setting conditions.

139. The FTT considered *Fane* (and *Eastman*) at FTT[263] to [273], at the beginning of the discussion on suspension, and concluded at FTT[273] that the conditions put forward by the Appellants were no more than a basic requirement and the decision to preclude suspension was justified and not flawed on those grounds. We consider that the FTT made an error of law in stating that the conditions were no more than a basic requirement (as the proposal made on 17 October 2022 would seem to us to be more than this).

140. The difficulty for the Appellants, however, is that the FTT then, in the following paragraph, states at FTT[274] "Even if the tribunal is wrong in categorising the conditions put forward by PDC as no more than a basic requirement, the tribunal considers that the exercise of HMRC's discretion not to suspend PDC's penalties was in any event not flawed according to judicial review principles". The FTT then went on to address HMRC's application of the SMART criteria, the previous practice of the Appellants in submitting accurate tax returns, the event being a one-off but that this had not automatically precluded suspension, and that the proposals did little more than transfer what had been carried out electronically to a face-to-face meeting. The FTT did revert to this language of "basic requirement" at FTT[307] when explaining its conclusions. However, the FTT had expressly stated that HMRC's decision was in any event not flawed on an alternative basis.

141. Mr Vallis submitted that the condition put forward by the Appellants on 17 October 2022 met the statutory requirements and the SMART criteria. We would agree that a condition that a taxpayer meet in person with their tax adviser to review each entry in their return before that return was submitted could, in appropriate cases, be specified as a condition of suspension. It would meet the SMART criteria. That, however, is distinct from finding that it would meet the statutory requirements. As both parties accepted, paragraph 14(3) focuses on the behaviour of the particular taxpayer who has made a careless inaccuracy, and here HMRC had said that they could not see any future careless errors that could be avoided by setting a condition "in this

case", effectively that this was a scenario (as envisaged by paragraph 14(3)) where no condition could be specified rather than rejecting a particular condition which had been proposed as being inappropriate; and the FTT agreed this was justified.

142. The FTT could only order HMRC to suspend the penalties if it thought that HMRC's decision not to suspend was flawed when considered in the light of the principles applicable in proceedings for judicial review; and it concluded that this threshold was not met. We agree it was right to reach this conclusion.

143. The Appellants' appeal on Ground 4 is dismissed.

DISPOSITION

144. For the reasons set out above, the Appellants' appeals on Grounds 1 to 4 are dismissed.

JUDGE JEANETTE ZAMAN
JUDGE JENNIFER DEAN

UPPER TRIBUNAL JUDGES

Release date: 7 January 2026