

MEDIATION OF TAX DISPUTES

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for which I have recently been listed on page 1 worldwide, or '**inheritance tax strategies**', '**tax barrister**', '**tax mediation**', and '**will disputes barrister**', for which I have recently been listed on pages 2 and 3.

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Glossary

AAB Anti-Avoidance Board.

ADR Alternative Dispute Resolution.

BATNA Best alternative to a negotiated agreement.

BTCIP Business Tax Contentious Issues Panel.

CDR Collaborative Dispute Resolution.

CRM Customer Relationship Manager.

CTISA Corporation Tax, International, Stamps and Anti-Avoidance.

Customer	This term used by HMRC in the Guidance and Commentary and means the taxpayer.
DRU	Dispute Resolution Unit.
FA	Finance Act.
HMRC	Her Majesty's Revenue and Customs.
HRCP	High Risk Corporate Programme.
LBS	Large Business Service.
LLP	Limited Liability Partnership.
LPP	Legal Professional Privilege.
LSS	Litigation and Settlement Strategy.
MCRP	Managing Complex Risks Programme.
NICs	National Insurance Contributions.
PAYE	Pay as You Earn.
PTCIP	Personal Tax Contentious Issues Panel.
SAO	Senior Accounting Officer.
TDRB	Tax Disputes Resolution Board.
TPB	Transfer Pricing Board.
TPP	Transfer Pricing Panel.
VAT	Value Added Tax.
WATNA	Worst alternative to a negotiated agreement.

Why ADR is needed

‘Cases slide inevitably towards a hearing at a tribunal, but:

- *from a client’s perspective, there is nothing good about litigation: irrespective of the outcome, it is costly, time-consuming and stressful – and it is all the more unsatisfactory if you lose; and*
- *from HMRC’s perspective, the appeal process is equally costly and time-consuming for an overstretched department which is under severe external pressure to work smarter and faster. Moreover in a fact based case, a decision is unlikely to add much value in elucidating the law.*

For these reasons, litigation should be the route of last resort for both sides...Tax ... is an area bedevilled by confrontation, positional negotiating and adversarial stances. HMRC, taxpayers and advisers have all contributed to this state of affairs. The outcome has been restrictive and aggressive legislation and a substantial breakdown in trust between all sides, to everyone’s disadvantage. Alternative dispute resolution is not a panacea for all of these problems, but it is certainly a step along the road to working together better which confers obvious advantages. HMRC are to be congratulated in having taken that first step. Our job is to persuade ourselves and our clients that we should walk along that road too.’ ‘It’s good to talk’ by Andrew Gotch and Hui Ling McCarthy, Taxation Magazine, 19 April 2012.

‘There were nearly 27,000 tax disputes waiting to be heard by the First Tier Tax Tribunal in 2012-2013 up from just 13,456 in 2009-2010) and it takes an average of 70 weeks just to get a hearing. This is locking up billions of pounds in uncollected tax: for 2011-2012, HMRC estimates that GBP 7.2 billion of the

tax gap arises from taxpayer error of failure to take reasonable care. ADR is seen as part of the answer to raise revenue and reduce the backlog of court cases for HMRC, but it can also benefit taxpayers... As 34% of the SME and individual cases and 35% of the large or complex cases accepted in the pilot [disputes] were resolved, HMRC saw the pilot as a success. We would agree. After a successful two-year trial of ADR, HMRC expects resolution rates to improve following ADR being rolled out nationally on 2 September 2013. ADR seems to be successful so far, as the most recent statistics on ADR applications between 1 April 2013 and 14 January 2014 show 79% of SME cases were resolved within 120 days. They also show 83% of the large and complex cases that went to ADR were resolved and there is evidence to suggest that simply applying for ADR motivates large companies and their HMRC relationship managers to sort disputes out before they need to get a mediator involved.'

'Broken Stalemates' by Dawn Register, Director in the Tax Investigations Team at BDO LLP in London, published in the STEP Journal, March 2014.

In 2014, in the SME sector alone, an estimated 4,600,000 taxpayers can use mediation in resolving a tax dispute with HMRC.

How counsel can add value

'In England and Wales the conduct of litigation and the client relationship is primarily managed by the solicitor who usually brings in Counsel to help with specialist legal advice and risk management to represent the client at trial. The role of any legal representative at a commercial mediation as advisor and supporter can be a very real force for settlement and not an obstacle to progress. Counsel at mediation have an equal or potentially greater role than the instructing solicitor through their objectivity, distance and authority with the client and often with the solicitor... Counsel who proactively take this role assist the mediator enormously in neutralising the emotion and tension brought

to the mediation by the party, some or all of which has inevitably filtered through to the solicitor who is so much closer to the client and the detail of the case. In addition some solicitors tend to the mistaken belief that their clients are paying them to express the same hostility that the client himself may feel towards the opposition...' which is why counsel add value where a solicitor is lacking in confidence, seniority, stature or ability. 'Representing Clients in Mediation – Hopes and Expectations' by Charles Middleton-Smith, presented at the SCMA training event, 'Making Mediation Work' held at Linklaters in London, 29th April 2014.

This guide

This guide is an A-Z reference manual for accountants, CTA's, non-specialist legal practitioners, and students. It is a work in progress and will be periodically updated and revised. Meanwhile I welcome any comments and contributions for inclusion, which will be fully accredited. The guide contains extracts from HMRC guidance and commentary on the mediation of tax disputes, and adopts the same definitions including 'customer', which HMRC use interchangeably with 'taxpayer' to refer to the taxpayer.

Introduction to mediation

Mediation is a flexible process conducted confidentially in which a neutral person actively assists parties in working toward a negotiated agreement of a dispute or difference with the parties in ultimate control of the decision to settle and the terms of resolution.' The Centre for Effective Dispute Resolution (www.cedr.com).

The goal in mediation is to reach a settlement which is owned by the parties, and which is practical and sustainable. Any agreement which is reached in principle is then recorded in a settlement agreement.

The unique and distinguishing feature of mediation *'is the central role of an independent third party, the mediator, of facilitating a settlement agreement between the disputants. Experience has shown that, in cases where a dispute may prove difficult, if not impossible, for the parties to resolve between themselves, the presence and assistance in their search for the settlement, of a third party trusted by both parties and acceptable to both parties, and most particularly the presence and assistance of a trained or experienced mediator, can immeasurably facilitate the negotiation process and increase the prospects of success. That is the rationale for mediation from other negotiating processes...In revenue mediations, as in revenue settlements generally, the merits have a very significant part to play. The mediator and the advocates must understand the underlying legal principles and issues.'*ⁱ

The costs of the mediator are likely to be shared equally between the parties, but each party will usually bear his own professional costs.

Mediation can take place at any stage in a dispute, and there is little downside to the process, as all work and preparation involved is likely to be of direct relevance to and use in litigation, in the event that the issue is not resolved by ADR.

The psychology of mediation

'The magic of mediation is in involving a third party neutral who changes the dynamics of the negotiation. The third party can act as a buffer, if there is a relationship issue. He or she can act as a process manager, the person who asks the tough questions and sometimes makes the practical suggestions to, for instance, identify the missing information. Sometimes it's just a question of needing a third pair of eyes to steer the communication process between the parties. Without getting overly Freudian, individually we are not always very good at conflict. When we go head to head, it can become personal. We are not

always good at taking a step back and trying to do some problem solving. That is where a trained mediation professional can help. ' Graham Massie, Director, Centre for Effective Dispute Resolution.ⁱⁱ

Mediation models, whether or not they adopt a psychological approach, or have a psychotherapeutic or counselling input, are based upon the premise that all disputes are affected and influenced by psychological or emotional principles – or what the layman might refer to as '*psychological barriers*'. All disputes involve injury to feelings, so few disputes will be without their emotional element. The object of mediation is to help the parties arrive at a satisfactory solution to their conflict – a settlement that is acceptable to each of them. In the psychotherapeutic paradigm of mediation, the aim in conflict solving is to transcend the antagonistic and emotional stance and move the parties from their initial confrontational position to a more reasonable platform. Hence they can enter into some form of working alliance, and through this achieve a resolution which is '*good enough*' for each of them.

When parties resort to mediation, their most common motivation is a strong desire to triumph. Similarly the mediator will equally wish to triumph by achieving a settlement. But of course, all parties cannot triumph simultaneously. Each of the opposing parties aspires to achieve the maximum benefit from the mediation and the mediator seeks to conclude an agreement between the parties, thereby avoiding litigation. Allowing due respect to the notions of '*positive thinking*' and '*win-win*' attitudes, all parties in the configuration cannot win. The parties, therefore need to reformulate what they expect to achieve from the mediation and what they mean by '*winning*' or by achieving their objective. The '*must win*' stance fails to take into consideration some of the universal limitations that the world imposes on the parties, so that such a stance is neither realistic nor sustainable.

The mediator and the parties in dispute are all in a relationship in which they are intertwined, sharing the same limitations in the world. They all face individual decisions as to how to respond to these constraints. The confronting parties both believe that they are justified and that they have every right to win. The mediator, on the other hand, also carries a strong agenda: a desire to conduct the mediation to a successful conclusion. All these motivations form part of the building blocks of the expectations of the mediation.

One important practical rule in mediation that arises from this is that the mediator should consider the parties at the mediation table as individuals, instead of merely as representatives of companies, institutions or nations. In whatever representative capacity the parties attend the mediation, they nevertheless remain individual people, governed by their own outlook and their own individual '*self-concept*' and self esteem. By recognising these characteristics in each of them, mediators can soon discover the true underlying motives of the parties and their dispute.

One of the most important elements of the mediation process is the exploration of the covert reasons for the dispute, as well as the overt. The parties will have developed rigid values and belief systems as their overall strategy for survival in an uncertain world. These can emerge in the dispute as perhaps just a single particular belief. But this might simply be one aspect of an overall overt strategy for achieving a '*winning position*'. Beneath this may lie many other diverse motivations: pride, jealousy, anger, hurt, envy, kudos, arrogance, greed, vanity, the protection of identity, self-esteem and numerous other hidden driving forces. These may be precipitated by corporate policies, internal office politics, rivalry between colleagues, family culture or a host of other influences.

Frequently, the parties may not even recognise that the real conflict is hidden and very different to what they express it to be. They may not understand or

recognise their own true underlying motives: they may believe they are simply seeking proper redress or compensation, whereas in fact they are expressing anger and hurt, and a desire to see the other party punished and humiliated.

The psychotherapeutically informed mediator will thus firstly enable the parties to discover their hidden true motivations and to explore them. Secondly, this mediator will help the parties recognise that they are mutually trapped in a situation which is reciprocally destructive. Thirdly, and perhaps most importantly, the mediator will facilitate the parties to move to a realisation that the conflict could be resolved if their attitude towards it were changed – if the platform were transformed from one of antagonistic resentment and distrust to a more cooperative and trusting relationship.ⁱⁱⁱ

Collaborative strategy

The keys to success in mediation are not what lawyers argue, but identification by each party of their BATNA (best alternative to a negotiated agreement), which is a practical tool for risk management, and doing a deal measured against it. This requires preparation and planning by each party's mediation advocate. Strategy is the outcome.

A collaborative strategy assumes that the parties can work together to reach an agreement that meets the needs of both and is objectively fair. The process involves exploring the parties' underlying interests, sharing information and being creative in the options considered. The agreement will not necessarily focus on the original issues between the parties but will try to identify options for mutual gain. The strategy involves more than co-operation – it is based on mutual effort and requires advance analysis and planning.

Within the term '*collaborative*' different strands may be identified:

- a ‘*principled*’ strategy tries to achieve an outcome that is objectively fair against some external authoritative norm; and
- a ‘*problem-solving*’ strategy focuses on both parties’ real needs and interests, and tries to get a practical solution without building costs.^{iv}

The characteristic approach is:

1. working together is stressed at the start of the negotiation, and this approach is sustained throughout. A mediation advocate for the taxpayer may for example open by saying,

Thank you for meeting with us today.

I understand that the ground rules and principles governing HMRC’s participation in this mediation are...

I will be corrected if I am wrong, but what I think you say about the facts and the law is ...

It is not my job to persuade you that your arguments will not succeed at trial.

As you know we say that we will succeed.

I am not interested in having an argument with HMRC about whose view is right.

I suggest that litigation is not going to be a great outcome for either HMRC or my client. The risks are...

I am here because I believe that we can reach a principled and fair deal that is not only good for my client but also better for HMRC.

I hope that you will work with me to achieve this today in accordance with your rules and principles...;

2. each issue is approached constructively, focussing on the best possible outcome for both parties;
3. issues are likely to be approached from the point of view of needs, interests and options, rather than fault and blame;
4. both sides work to maintain an open and reasonable atmosphere; and

5. the mediation advocates are likely to emphasise objectivity, and a potential settlement is often judged against agreed criteria to test fairness.

In addition to planning potential demands and concessions in relation to individual issues, it is vital to be able to put any personal settlement into an overall context, so that you will be in a position to judge whether a particular overall set of terms should or should not be accepted. This requires comparing whatever overall deal you are able to achieve in a negotiation with the best realistic alternative there would be if no settlement were reached. This involves identifying the best alternative to a negotiated agreement ('BATNA'). If the deal you have negotiated is at least as good as your BATNA then it should potentially be accepted. If it is worse then you should probably walk away. For a legal negotiation the alternative to settlement will be going to court, so the BATNA is what the client is realistically likely to get if he were to go to court.^v

The policy and governance framework within which HMRC can decide to mediate and resolve a dispute by mediation

- HMRC's use of ADR.
- Suitability of mediation in a tax dispute.
- HMRC's Litigation and Settlement Strategy ('LSS').
- Responsibility for decision making.
- ADR.
- Collaborative working.

HMRC's use of ADR

HMRC are rolling out ADR as part of its standard business approach across the board.

'As our Litigation and Settlement Strategy makes clear, we aim wherever possible to resolve tax disputes by agreement, provided a satisfactory outcome within the law can be reached. Litigation can be time-consuming, costly and always has an element of risk. There are various options that are available before litigation.

Where taxpayers do not agree with our decision, they can ask for an internal review of the decision. An officer who was not involved in the original decision then looks again at the facts, legal position and process of the decision. The review officer decides whether to uphold, vary, or cancel the decision, in accordance with the LSS.

In line with the Government's dispute resolution commitment, taxpayers can also consider whether alternative dispute resolution (ADR) techniques will aid in reaching an agreed resolution in line with the LSS, instead of proceeding to tribunal.

ADR can be useful in some cases which are very fact-heavy where views have become entrenched. We have recently trialled the use of ADR in two pilots and we are now building on their successes as part of business as usual.

ADR is designed to overcome deadlocks in dispute resolution by establishing or re-establishing constructive dialogue. It uses an intensive, mediated, process to remove personality from a dispute, examine and agree facts, or tease out what facts are not agreed, why that is and what is needed to achieve agreement. The focus is neutral and involves collaborative engagement. It also examines the assumptions that underlie each side's view of how the law applies to those facts so that mutual understanding can be achieved.

Subject to governance processes, ADR can also bring decision-makers from both sides to the table, so that opportunities for misunderstandings are minimised. Where resolution has been reached, this has been on the basis that a

shared understanding of the facts and how the law applies has been achieved. Where the dispute remains unresolved, there is usually a better appreciation of the arguments and underlying reasons for the dispute, which makes litigation better focused.

Although resolving disputes by agreement is our preferred approach, we will take cases to litigation if an outcome consistent with the LSS cannot be achieved any other way. Around 4,300 appeals to the Tribunal were closed in 2011-12 (the latest year for which figures are available).

The majority of these were individual disputes about the facts in a specific case or the application of penalties, without wider impact or precedent value. However, each year there are also cases heard where the outcome could have significant implications for HMRC and taxpayers in general.^{vi}

Suitability of mediation in a tax dispute

'ADR may be suitable for a wide range of disputes across different taxes, particularly those which relate to transfer pricing, capital vs revenue or valuation issues. It may be particularly useful for use in long-running disputes where positions on both sides have become entrenched, with litigation or one party conceding appearing to be the only options...As tax laws are complex, tax disputes are often fact-intensive. A combination of these factors can contribute to uncertainty regarding the correct interpretation of the issues in the dispute, and thereby warrant mediation or negotiation that allows parties to search for creative solutions that fulfil the needs of both disputants.'^{vii}

HMRC's Litigation and Settlement Strategy (the 'LSS')

'Effective handling and resolution of tax disputes helps to maximise revenue flows both in ensuring that the right tax is established in particular cases, and in acting to protect the tax base and to deter non-compliance and avoidance

across HMRC's customer base. However, a dispute inevitably involves costs for both HMRC and the customer and can be very expensive, both in terms of resources and agent/legal fees.

Minimising the scope for disputes, and reducing the costs to HMRC of resolving disputes is likely also to reduce customer costs, improving the customer's experience and making the UK a better place to work and do business.

In resolving those tax disputes which do arise in a way which establishes the right tax due at the least cost to HMRC and to its customers, HMRC also needs to apply the law fairly and even-handedly.

Line management procedures, processes for risk working and compliance checks in Lines of Business, and cross-HMRC governance arrangements such as the Tax Disputes Resolution Board or Anti Avoidance Board all support a fair and even-handed approach to tax dispute resolution. But to do this they need a single framework for how tax disputes are to be handled and resolved which applies consistently across HMRC – this is the Litigation and Settlement Strategy (the 'LSS')'.^{viii}

Responsibility for decision making

The LSS is a statement of HMRC's strategy for handling tax disputes, consistent with the law and with HMRC's key objectives, and therefore the LSS applies to the handling of all tax disputes across the department. The LSS applies as much to the resolution of a dispute over a small business customer's taxable profit or turnover as it does to the resolution of a complex tax avoidance transaction involving a multinational corporation or wealthy individual. It applies whether the dispute is being considered by the Commissioners for HMRC or in a local office. And it applies whether or not there are formal governance procedures in place to assist in reaching decisions on the handling

of a particular dispute. Paragraph 6 refers to ‘decisions taken by HMRC’ in relation to disputes, and this includes decisions on:

- how disputes should be progressed towards resolution (including questions over the appropriateness of litigation, ADR, or other routes to resolution); and
- the terms on which HMRC should be ready to resolve the dispute (in the absence of a finally binding outcome from litigation).

HMRC’s Code of Governance sets out the governance and assurance frameworks for decisions in tax disputes. Depending on size and complexity, such decisions may be taken by individual HMRC officers or teams, in accordance with local Line of Business procedures, although where responsibility for decision making rests with more than one Line of Business such decisions will be made by consensus on a partnership basis.

ADR

HMRC may engage in the following types of ADR:

1. facilitated discussion;
2. facilitative mediation;
3. evaluative mediation; and
4. non-binding neutral evaluation.

Tax mediation is essentially no different to any other mediation. The key distinction between mediation in a tax context and mediation in other commercial disputes is HMRC’s status as a public body. HMRC do have a degree of discretion as to how they fulfil their obligation to collect revenues but, in contrast with commercial organisations, they also have duties to the wider

body of customers and this may, in certain circumstances, restrict their freedom to enter into a negotiated settlement of the dispute.^{ix}

Any decision by HMRC to settle a case during such a process will still be governed by the terms of the LSS and associated governance and any settlement or agreement reached as a result of ADR will be subject to exactly the same process as any other case. In rare cases, agreements may need to be provisional subject to governance processes and this will be explained as part of the ADR.

One of the fundamental principles of the LSS is that settlement of the '*right tax*' due is to be sought. Another is that disputes should be resolved in the most efficient and cost-effective method possible. ADR is supportive of LSS principles as a cost effective way of trying to reach agreement by providing a process which allows for a better shared understanding of each other's arguments or contentions regarding what is the '*right tax*'. This enables HMRC and the customer to make a more informed decision.

The LSS presupposes that disputes will be resolved collaboratively (as opposed to adversarially) wherever possible, as the most effective and efficient means (for both sides of the dispute) to arrive at the '*right*' result in a tax dispute. ADR also presupposes such a collaborative approach, therefore Collaborative Dispute Resolution (CDR) should be the norm and ADR a toolkit to be used sparingly within this normal way of working.^x

Collaborative working

Collaborative working practices are already commonplace between HMRC and many of its customers across the different customer groups.

Specific examples of a CDR approach include:

- discussing risks/transactions on a '*real time*' basis (i.e. pre-transaction or pre-return);

- applying an “*Openness and Early Dialogue*” approach which sets out the specific tax risk identified and avoids unnecessarily wide-ranging opening enquiries;
- early discussion of a particular risk which is under enquiry in order to understand fully the relevant facts and the law which might apply to those facts (e.g. a discussion of the particular risk to enable HMRC and the customer to get a shared understanding of what are the relevant facts, which will enable HMRC to tailor any subsequent information request accordingly);
- jointly agreeing a timetable with key milestones and target dates for:
 - establishing facts;
 - providing information/documentation;
 - reviewing documentation;
 - reaching decisions; and
 - testing conclusions;
- providing regular updates on progress towards key milestones;
- clarifying understandings of relevant facts;
- agreeing the form in which particular information is to be provided;
- discussing, sharing and testing of technical arguments to assess relative strengths and weaknesses in analyses;
- establishing a decision tree (i.e. agreeing the key questions which need to be answered in order to resolve a dispute);

- exploring possible alternative interpretations of the facts and relevant law that might give a different outcome from those initially proposed by HMRC or the customer; and
- working with the customer or agent to agree any additional liability.

Where a dispute has reached an apparent impasse, it is still possible for the parties to work collaboratively in order to try to unlock the process (e.g. by jointly agreeing to appointing a third party mediator. Similarly, parties should not stop working collaboratively simply because one or perhaps both, consider that a dispute can ultimately only be resolved by litigation. As such, the process of preparing for litigation should not automatically default to an adversarial process and, wherever possible, the parties should continue to work collaboratively in order to ensure that the resolution of the dispute through litigation is as efficient and cost effective as possible.

Some examples of how HMRC and the customer could continue to work collaboratively where a dispute is proceeding towards litigation might include:

- agreeing the key questions which need to be determined by the Tribunal/Courts;
- seeking to narrow down the points in dispute to be litigated;
- jointly drafting an agreed statement of facts;
- being open to discussing the potential relevance/impact of any new facts which come to light or alternative technical arguments which are identified;
- agreeing (without the need to go to a Tribunal procedural hearing) a timetable with key milestones and target dates for all preparatory steps to litigation; and
- arranging periodic meetings to discuss the case and update on progress.^{xi}

All or nothing cases

An '*all or nothing*' dispute (sometimes also called a '*binary*' or '*black and white*' dispute) is one which has only two possible outcomes, i.e. a given amount of tax is either due, or it is not.

Where a dispute relates to an all or nothing point, if HMRC believes that there are only two possible outcomes consistent with the law, they will not accept any out of court resolution that splits the difference.

However, sometimes a dispute which initially appears to be all or nothing might, after further review/discussion/testing, turn out not to be genuinely all or nothing but in fact be a case where there is a range of possible figures for what might be the right tax.

Wherever a dispute initially appears to be all or nothing, HMRC should test that initial conclusion (preferably with the customer) to explore whether or not:

- there is a range of right answers for how the law should be applied to the facts; or
- the dispute is capable of being broken down into two or more sub-disputes, each of which is capable of being separately resolved.

In this way the chances may be increased of reaching an efficient, cost effective and legally correct resolution to the whole dispute.

Where an issue is centrally project-managed, such as in cases of certain avoidance arrangements, it is likely that any proposed basis for settlement will be subject to specific governance arrangements (e.g. approval by the Anti-Avoidance Board). In such cases, where an alternative basis for settlement in what initially appeared to be an all or nothing issue is identified and approved in accordance with the relevant HMRC governance arrangements, it is expected that HMRC will communicate and accept this basis for settlement in equivalent cases with other customers (assuming they have the same fact pattern).

Some tax disputes are genuinely '*all or nothing*', but by no means all. In cases which proceed through successive layers of appeal in the Tribunal and Courts, it is not unusual for different legal interpretations to emerge. Discussions with customers and advisers, as well as discussions among tax experts and their advisers within HMRC, also frequently elicit alternative ways of approaching a particular tax dispute. This reinforces the need to spend time working together with the customer and their advisers, as well as with HMRC colleagues, to identify the range of reasonable approaches to any particular tax dispute, to make sure it is not prematurely categorised as an '*all or nothing*' dispute. Having said that, if HMRC believes a dispute to be genuinely all or nothing, then the LSS requires it either to press for full settlement, or concede in full. This reflects HMRC's position, that they will only resolve disputes out of court on terms which they believe are likely outcomes from litigation.^{xii}

Appointing a mediator

Choice of mediator is very important, because trust is key in mediation. A mediator must be able to gain the trust of the disputing parties. Some trust may be generated from the mediator's organisation, or from his personal reputation. Most importantly however, trust will be built from the mediator's behaviour during the particular mediation process.^{xiii}

The parties can agree on the appointment of a mediator or, if they cannot agree, they can ask a third party (for example a mediation service provider) to select the mediator.

The parties should discuss whether facilitative mediation, evaluative mediation or non-binding expert determination is most suitable for the particular case, and whether there are any particular individuals who might be appropriate to mediate the issue. The DRU is available to advise on what might be the most appropriate form of mediation and also help suggest a suitable mediator.

The HMRC team cannot agree a mediator without DRU approval. Once a suitable mediator has been suggested, the HMRC facilitator should contact the DRU, who will advise them on the information required before HMRC can engage the mediator. This is to ensure that there is no conflict of interest between the mediator and HMRC.

The DRU will liaise internally to ensure that HMRC are content to contract with the proposed mediator and that there are no conflicts of interest present in the engagement. This may take up to two weeks. The facilitator should advise the customer of these requirements in advance where it is proposed that a mediator be appointed. Once the DRU have completed their checks and given approval, the HMRC facilitator should sign any contracts with the mediator on HMRC's behalf.^{xiv}

Whilst there are obvious advantages to appointing a Tax expert, in some instances an expert from another field might be more suitable.^{xv}

'An experienced mediator really can design a process that suits the needs for the parties in that particular case. The mediator does, of course, need to understand what everybody is talking about, but he does not need to be an expert because it is not his job to give them the answer or his view.' Graham Massie, Director, Centre for Effective Dispute Resolution.^{xvi}

'The real prerequisite is skills in mediation to assist the parties in unearthing what it is they are concerned about. Of course, there needs to be an understanding of the tax issues, but where the mediator needs to be so expert in the tax issues that they would be in a position to decide the dispute, then I think you are in the realms of something that probably ought to be going to court.' Geoff Lloyd, Executive Director, Ernst & Young.^{xvii}

Barrister assisted mediation

This idea occurred to me in January 2014 whilst writing the first edition of the guide, and please e-mail any comments and suggestions to me at carl@ihtbar.com. In a recent discussion with two well known mediators at an international conference in London it was suggested to me that this method of mediation could also take the form of a co-mediation.

Where a mediator does not have a technical tax background, an independent tax barrister (for example a member of the Revenue Bar Association) is jointly appointed by the parties as a consultant to help the mediator understand the facts, evidence, technical tax issues in dispute and applicable legal principles.

Prior to the mediation day the barrister can also provide each party with a preliminary:

- analysis of legal merits;
- commercial analysis;
- litigation risk analysis; and
- proposed settlement methodology (i.e. a mathematical equation).

The aim ahead of the mediation day is to create a framework for negotiations, to move the parties away from a positional to a legally principled and commercially rational mindset, leading to traction within the first two hours of the mediation day and the making and discussion of settlement proposals by each party through the mediator before lunch.

Alternatively the barrister could provide these documents to the mediator for discussion in confidence with him in a pre-meeting to assist the mediator to develop bespoke mediation strategies in advance of the mediation day.

This would of course require the disclosure by each party to the barrister and mediator of a bundle (which could be limited to one lever arch file of indexed documents) at least two weeks before the mediation day.

The barrister is instructed directly by each party, does not have a contract with the mediator, and signs the mediation agreement. Each party will be represented by their own mediation advocate throughout the mediation day. If the advocate is e.g. a CTA, the tax barrister (whose duty is to assist the mediator) can with the permission of the mediator also be consulted to provide his preliminary opinion (without legal liability) about technical tax law issues. In which case the contract with the barrister will contain an indemnity.

To help the parties develop a road-map for settlement, if the contract with the barrister and mediation agreement include a provision requiring terms of settlement to contain a clause obliging the parties to keep negotiations confidential following agreement, then a barrister is set free to think outside the box and make creative proposals (for communication through the mediator). Note that the limits on confidentiality in a Revenue dispute that need careful consideration, are highlighted in an article '*Mediation in Revenue Cases*', by Sir Gavin Lightman and Felicity Cullen QC (which is available to download on the internet).

Instead of preparing position statements, each party with the assistance of the barrister can prepare (in e.g. Scott Schedule format) a side by side analysis of the facts, technical tax issues, and governing legal principles, for exchange together with a bundle of documents (also to be provided to the mediator) in advance of the mediation day.

My theory is that on the mediation day each party will then (depending upon preparation and trust), be equipped to move swiftly (i.e. in the first 2 hours) from a fixed starting point, and be open to working with each other through the

mediator (and his assisting tax barrister), to develop a practical and fair settlement using bespoke methodologies suggested by or jointly developed through the mediator with the assistance of the tax barrister.

Following a 5-10 minute open plenary and house-keeping session, in which only the mediator speaks, each party can then head off to their own respective rooms to be visited by the mediator and tax barrister, to discuss and explore their strategic interests positions and reasons, in privacy and confidence.

The objective of my method of '*Tax Barrister assisted mediation*', is to kick-start a road mapping process in the morning, that can result in the making of proposals through the mediator, leading to an agreed formula for settlement in the afternoon. Even if an overall settlement is not achieved before 5.30pm, because the process is likely to result in greater clarity and focus, this method is likely to reduce the issues in dispute and create a road-map leading to an agreed formula for settlement on another day.

It also sets the mediator free from the outset, to make the maximum use of his skills in the time available in the morning, to explore with each party, their respective underlying interests values and positions, with the aim of agreement being reached in the afternoon.

Benefits

Mediation:

- is a flexible process that can be tailored to meet the needs of each case;
- is cost effective;
- can be arranged relatively quickly;
- is a confidential and private process;

- avoids adverse precedent being set by the court;
- avoids the stress and trauma that some individuals may feel about giving evidence in court;
- is more likely to preserve a relationship than a court imposed solution because a settlement is reached by mutual agreement; and
- enables the parties to be more creative when reaching a settlement.

Negotiations can take place with the assistance of a neutral third party within a structured process. Mediators will bring their own personal attributes to the table, such as patience, empathy, ability to listen, good judgment, good communication skills, creativity, the ability to think *'outside the box'*, impartiality, authority, and the ability to command respect, all of which can help the parties to review and re-evaluate their case. The appointment of a mediator introduces an element of detachment into the negotiation process and mediation avoids the need for direct confrontation and an immediate response that occurs in face to face negotiation between the parties.

'A mediator can act as a bridge to create trust between both parties, and he or she is able to bring that extra degree of dynamism towards a resolution of the dispute that might not otherwise be there.' Geoff Lloyd, Executor Director, Ernst & Young.^{xviii}

A mediator can also:

- create a balance between the different negotiating styles and personalities of the parties and minimise the pressure that one party can feel when the other side employs a positional and confrontational negotiating style;
- encourage a more accurate and honest assessment by each party of the strengths and weaknesses of their own case;

- help the parties (and their lawyers) to work through the deadlock that can be created by purely positional or competitive negotiation by helping the parties to devise strategies that are more likely to lead to settlement;
- offer proposals that are more likely to be perceived as being attractive, than an offer made by a party directly (because arguments put forward by one side are automatically psychologically devalued by the other side), a process known as '*reactive devaluation*'; and
- provide the opportunity to reality test each party's case.^{xix}

The parties retain the right to litigate if mediation does not succeed and can withdraw from the process at any time. Even if settlement is not reached at the mediation, which HMRC recognise may require a series of meetings, going through the mediation process may help the parties to understand each other's case, narrow the issues, and in some cases, settlement may be more easily achieved after the mediation.

Bundles

The parties should co-operate in relation to the documents that are provided to the mediator and produce agreed bundles where possible. If a joint bundle of core documents has been agreed, then each party can produce for the mediator, if required, a small bundle of additional documents that they do not wish him to reveal to the other side. Care should be taken to mark this bundle as '*Strictly Confidential*' and to explicitly state that the mediator should not disclose the documents to the other side.

Choosing a date for the mediation day

Once the parties are agreed on who should be appointed they will need to agree a date for the mediation. The date should be one on which the mediator, the customer's representatives (and "decision makers") and HMRC's team are all

available, and should be far enough in advance to allow all agreed pre-mediation steps to be completed.

Mediations can be arranged and held at fairly short notice (subject of course, to the availability of the mediator and the representatives of the respective parties). However, if the parties want a particular individual it is often possible to “*hold*” an agreed date in the diary.

Parties may wish to consider agreeing a date at the outset of the ADR process, prior to the pre-mediation steps. This can help to ensure that the parties keep to the agreed timetable of the ADR process and can also help to maintain momentum in the process. However, the parties should bear in mind that it is possible that they may resolve the dispute prior to the formal mediation, therefore if a date is reserved in advance the parties need to consider and understand any potential cost implications of subsequently cancelling the mediator, which is likely to depend on each mediator’s specific terms.

Confidentiality

HMRC are required to maintain customer confidentiality throughout the entire enquiry process. However once a matter proceeds to a hearing before the tax tribunal, the dispute is no longer confidential as the hearing will normally be open to the public. In contrast both the mediation process itself and the terms of any agreement reached between the parties is confidential.^{xx}

However, there may be policy reasons (such as horizontal equity between taxpayers) that make disclosure or publication of an outcome desirable or even necessary. This might undermine the confidential basis of mediation to an extent and is one of the areas to which a lot of thought needs to be given. Where policy issues form part of the subject under negotiation, it is likely to be important that the process is, to some extent accountable and open to scrutiny. However these considerations are likely to be at odds with creative and open

discussion of matters in a mediation, and this may also tie in with matters concerning legal professional privilege. So mediation in the tax context raises some potentially unique issues.^{xxi}

The status of information provided in the course of the ADR process / Mediation, including documents drafted in preparation for and during the mediation session should be pre-agreed between HMRC and the customer. Standard confidentiality clauses can be found in the ADR process agreement and are likely to be used in the majority of cases. However, where a dispute is not fully resolved through mediation, it is possible that certain information / documentation prepared during the course of a mediation process could be beneficial in subsequent litigation (e.g. where parties narrow down points in dispute). In such circumstances, it is envisaged that the parties are likely to agree that particular information / documents could be disclosed and used in the litigation. In common with all casework, mediation proceedings and documents should be kept on a '*need to know*' basis within HMRC. Where the ADR process is being conducted through an HMRC facilitator, they will be acting as a neutral broker between the two parties but will remain an HMRC employee with the obligations which that employment brings.^{xxii}

Costs

For HMRC (and the customer) there are additional costs associated with every type of ADR in which HMRC may engage, with the exception of Facilitated Discussion.

The parties will normally bear their own costs of the mediation, however the financial cost of mediation will not be recoverable from HMRC should the customer ultimately succeed before the tax tribunal.

Disclosure

Sometimes parties will not want to disclose documents in the mediation because they feel that it will adversely affect the chances of settlement being reached. This may be so if proceedings have not yet been issued or disclosure has not yet taken place. The parties do not have to disclose anything if they do not wish to do so. However in choosing not to disclose documents they should bear in mind the provisions of the CPR and the protocols that encourage a '*cards on the table*' approach to litigation. If the document would have to be disclosed in the litigation, it may be best to disclose in the mediation. Failure to disclose crucial documents that have a major effect on the case can give rise to a risk of any settlement being overturned on the grounds of misrepresentation.^{xxiii}

Establishing and understanding the relevant facts

Tax law does not apply in a vacuum. It applies to specific sets of facts and circumstances. Therefore before a firm decision can be made on the tax consequences of a given transaction or issue, the relevant facts must first be established.

'Relevant facts' are those which have, or could have, an impact in determining the appropriate tax treatment. HMRC should seek to establish only the facts required to address the specific tax risk identified. In practice, this means that HMRC will often need to consider the possible tax law consequences in tandem with establishing the facts, to make sure that requests for factual information are indeed *'relevant'*.

No two customers or their circumstances are identical and there are often features which distinguish cases that at first appear to be similar. HMRC should consider (and, where relevant, critically examine) all the facts which are relevant to the tax risk in question, rather than looking for particular evidence

that supports an initial assumption about a risk. It is important to distinguish a fact, which is generally capable of being supported by evidence, from a belief or assumption. Most facts should be capable of being supported by evidence.

Historically, a significant proportion of cases in dispute that were not suitable to be taken to Tribunal were those with insufficient evidence documented on the file.

There may be instances of facts which turn on the customer's view of why something was done. Oral evidence may be presented at a Tribunal as well as documentary evidence (where such evidence exists). An example of this may be oral evidence presented by a customer showing a commercial purpose for a series of transactions to which the tax consequences were incidental.

Establishing and understanding the relevant facts includes understanding what evidence may be presented orally, if the case were to get to Tribunal, and understanding how the Tribunal might balance potentially competing evidence in order to make findings of fact on the basis of the *'balance of probability'*.

In avoidance cases, it is often important to establish that transactions have in fact been implemented in the way needed to give the tax advantage claimed.

A common challenge in disputes is for HMRC to determine the most efficient and effective way of establishing the relevant facts and identifying the relevant information required to reach a decision on what is the right tax.

Even after having identified a potential tax risk, HMRC may not know which facts are going to turn out to be relevant in resolving that risk. Where the risk is a generic one (for example, whether a customer's accounting records or systems are not sufficiently robust), opening questions may need to be widely drawn.

But where the risk relates to the tax treatment of a particular transaction, a widely drawn request for information can lead to a significant amount of non-relevant information being provided. This can be time-consuming and costly,

not only for the customer (in searching for/ providing the information/documentation) but also for HMRC (in having to review everything provided, much of which might have limited or no relevance to helping to resolve the dispute).

Wherever possible, HMRC should therefore aim to discuss and agree with the customer what are the relevant facts and how these should be established – for example though obtaining original documentation, site visits, discussions with relevant individuals, etc – to develop a robust tax analysis.

This discussion should be founded on a high degree of disclosure and co-operation from the customer and an acceptance by HMRC of the practical constraints – including cost, time and accessibility – that may limit what can reasonably be provided.

Similarly, HMRC should also seek to identify and (where possible) agree with the customer the amounts of tax in dispute.

Overall, HMRC's approach to establishing facts will depend on the nature and extent of the potential tax risk posed by the customer/transaction in the particular case.

However, it is recognised that there can be a reluctance from some taxpayers to provide information and they can take an approach of providing the minimal possible at each request. This may be exacerbated by any lack of understanding as to why HMRC require the information and this makes it all the more important that HMRC should explain why information is needed wherever possible.

In some cases there may also be a dispute over whether or not particular information or documents are relevant to an enquiry. HMRC will seek to reach agreement with the customer on what is relevant, wherever possible. In the

absence of agreement, the key test for any request is whether, in HMRC's view, the information or documents are reasonably required for the purpose of checking the tax position.

Where needed, HMRC will consider using statutory powers to obtain information, and in cases where there is agreement on documents (or categories of documents) to be produced, that agreement will be reflected in the content of the information notice. In certain cases the person receiving an information notice may appeal against it.

The approach '*HMRC best practice – fact finding*' (for which there is a separate entry below) seeks to balance the following three factors:

1. the need for HMRC to have a good understanding of the facts before it reaches firm conclusions on what it believes to be the right tax;
2. the need for requests for information to be well targeted, confined to the relevant facts, and framed with a view to making the fact-finding process as cost effective as possible for both HMRC and the customer; and
3. the need to ensure that tax avoidance is not accepted as successful unless HMRC is satisfied that the relevant tax planning has indeed been implemented as described or is not open to other approaches (e.g. abuse of law principle).

Whilst widely drawn information requests are appropriate in certain cases, in the majority of cases it will be more efficient and effective for HMRC to try to work collaboratively with the customer and set out neutrally (and where possible agree):

- what facts need to be established in order to address the tax risk and resolve the dispute. In complex cases, this could take the form of agreeing a decision tree which sets out the relevant factual questions; and

- where certain facts are not clear or known, the best way of establishing those facts, and what information/documentation is likely to be available (and necessary) to help evidence the facts. In some cases, particular documents or other evidence might be essential in order to establish particular facts, whereas in others there may be various different routes to establishing the relevant facts. For example, where adequate business records have not been retained, the caseworker may be able to review the customer's private financial affairs to ascertain the correct level of profit.

The best approach for doing this will vary from case to case, but could include:

- initial meeting to discuss the potential tax risk/issue;
- presentation by the customer (e.g. summary of transaction, timeline, background, etc);
- meeting with particular individuals (e.g. owner of the business, those involved in implementing a transaction, etc);
- on site meeting (e.g. where the risk concerns a particular business asset, such as a piece of plant and machinery); and
- providing an initial tranche of documentation where this is readily available (e.g. copy of sale and purchase agreement, legal documents for a transaction, etc).

In large and/or complex cases, the benefits of a well-targeted fact-finding process are particularly significant. In such cases, it is often helpful to have an initial high level discussion of the risk, and the likely technical arguments, in order to ensure that requests for information are suitably framed and limited to facts likely to be relevant to the resolution of the dispute.^{xxiv}

Evaluative mediation

This is similar to facilitative mediation, but with the mediator offering an opinion as a specialist. Some commentators regard this as an inappropriate method of ADR in a tax dispute, because it duplicates the role of the tribunal and court.

Evaluative mediation is a process in which the mediator will try to bring the parties together in exactly the same way as in facilitative mediation, but also providing his/her view of the matter as a specialist in the subject matter of the dispute.

It is possible to have a combination of the two approaches in which facilitative mediation is attempted first, with evaluative mediation following if the initial approach is not successful. However, HMRC would only see this approach as suitable in limited tax cases where the issue is not tax related but determination of the issue has tax consequences, if both parties are willing to consider the strength of their case in the light of the expert's view.^{xxv}

Facilitated discussion

Facilitated discussion is a process in which an HMRC externally trained and accredited mediator facilitates bringing the parties together but offers no opinion on the merits of the arguments being advanced. Sometimes this involves a trained mediator also being provided by the customer's side to join with the HMRC mediator and facilitate together. The facilitator(s) may challenge each side as to how their dispute may play out in front of the Tribunal. The HMRC facilitator may or may not be a specialist in the subject matter of the dispute but will not have had any prior involvement in working on the case as part of the case team. If the customer also provides a facilitator it is expected that they will similarly not have previously worked on the case. The

main difference between facilitated discussion and facilitative mediation is that the people brought in to help the disputing parties are not independent of the disputing parties, but will work neutrally.^{xxvi}

Facilitative mediation

The mediator attempts to bring the parties together but without offering an opinion on the merits of each side's arguments.

Facilitative mediation is a process in which an independent external mediator is jointly engaged by HMRC and the customer to try to bring the parties together but offers no opinion on the merits of the arguments being advanced. The mediator may challenge each side as to how their dispute may play out in front of the Tribunal. A facilitative mediator may or may not be a specialist in the subject matter of the dispute but will have no connection with either party.^{xxvii}

Governance

Unjustified refusal to engage in ADR has been seen by the Court as a reason to award costs against the refusing party. For this reason, it is important that the appropriate governance is in place so that HMRC can record and demonstrate the decision-making process in cases where an external ADR request has been refused.

HMRC guidance states,

'Other governance processes and procedures (e.g. HRCP, Counter Avoidance Group, Contentious Issues Panels, MCRP, etc) should be followed as usual.

In the interests of consistency and best practice, the DRU should be informed of any case where ADR has been requested or is being actively considered.

ADR is not a route to bypass any of the existing governance arrangements such as AAB, CIP, TDRB, etc. All normal governance applies to any agreement reached within ADR. ^{xxviii}

HMRC

HMRC was established by the Commissioners for Revenue and Customs Act 2005 (CRCA), and is a non-Ministerial Department. This status ensures that the administration of taxes is, and is seen to be, impartial and independent from political influence.

HMRC is led by the Commissioners for Revenue and Customs, who derive their powers and functions from the CRCA. Led by the Chief Executive, the Commissioners are responsible for the collection and management of revenue, which includes direct and indirect taxes, duties and national insurance contributions. The Commissioners also have ultimate responsibility for every decision made in HMRC, although Officers make day-to-day decisions on their behalf. Officers make their decisions within an overall governance framework established when the Department was formed.

HMRC best practice - fact finding

The following outlines HMRC's best practice approach to fact finding in large and/or complex cases where both HMRC and the customer are working collaboratively.

1. High level opening discussion of the issues

1.1 As the customer should be familiar with the facts and documentation, this will usually start with the customer's analysis of the issue, and the filing position taken, to establish a fuller understanding of the nature and amount of tax risk involved. Both

parties could then, on a without prejudice basis, and based on the customer's outline of the relevant facts, discuss what the key technical areas of debate are likely to be.

1.2 From this agree a comprehensive list of the relevant areas of agreement and issues in dispute.

1.3 Agree an initial prioritisation of the issues and timetable for progressing towards decision point.

2. Identify the relevant factual information needed (where not already provided)

2.1 Discussion of the relevant areas of factual uncertainty, what facts need to be established to address that uncertainty, and how those facts may be established most cost effectively for both HMRC and the customer.

2.2 From this agree what documents and information should be made available and timetable for documents and information to be provided and reviewed. This should take into account the reasons why information is needed, the availability of information, and any anticipated difficulties in obtaining the information, and (where information is not readily available) any alternative ways of establishing the relevant facts. It should also take into account the lead time needed for information to be gathered and collated.

2.3 if there are legal, confidentiality or other constraints which make providing information difficult then explanations should be provided to assist HMRC understand the difficulties and to explore alternative ways of addressing the tax risk.

Examples include:

- *Documents that are covered by legal professional privilege*
- *Information that is not in the possession of the taxpayer and that they do not have the power to obtain.*

3. *Provision and review of relevant information*

3.1 *The customer and HMRC should make best endeavours to adhere to an agreed timetable for the provision and review of information. Disagreement over the status or availability of some documents should not be allowed to hold up the timetable for the provision of others.*

3.2 *Once HMRC has reviewed the information and there have been detailed discussions of the technical analysis, if HMRC believes it requires supplementary information it will explain its reasons.*^{xxxix}

HMRC's mediation checklist^{xxx}

HMRC case

- 1.1 *List evidence – witnesses, documents, reports, statements, etc.*
- 1.2 *List financial liability for each point in dispute (including interest, penalties, etc)*
- 1.3 *List strengths and weaknesses for each point in dispute*
- 1.4 *Clarify what, if any, parameters for negotiation are there on the issue in dispute (i.e. HMRC's 'red', 'amber' and 'green lines'):*
 - **Red:** *no movement possible*
 - **Amber:** *can be pushed a little*
 - **Green:** *reasonably flexible*

1.5 Calculating potential settlement range:

- *What would HMRC ideally like?*
- *What would HMRC accept?*
- *What is HMRC's bottom line?*
- *At what point would HMRC walk away?*

How did HMRC value the case? (including consideration of non-financial aspects)

- *What is the best alternative to no agreement (BATNA)?*
- *What is the worst outcome to no agreement (WATNA)?*
- *How much will it cost to go to trial?*
- *How long will it take?*
- *What are the % chances of winning in court?*
- *What does the other party consider its % chance?*
- *What questions or line of argument do you want the mediator to put to the other party?*

1.6 Identify HMRC's core interests and needs with relation to the other party, assessing alternative ways in which they can be met. This could include commitments in relation to aspects other than the particular issue / dispute in mediation.

Customer's case

2.1 List their evidence

- 2.2 *What are their likely arguments regarding liability on each point in dispute?*
- 2.3 *List the strengths and weaknesses of their case*
- 2.4 *Consider (or guess) the basis of their demands*
- 2.5 *Consider (or guess) the basis of their offer*
- 2.6 *How else may they have valued their demand (including non-financial aspects)?*
- 2.7 *How else may they have valued their offer (including non-financial aspects)?*
- 2.8 *Try to identify the customer's core interests and needs, and assess whether they can be met within the bounds of LSS.*

Considering all dimensions of the dispute

- 3.1 *Something may have financial cost for one party which does not impact the other party in the same way – i.e. an offer by HMRC to undertake complex calculations may not incur extra financial cost for HMRC, but may save the customer incurring hours of adviser fees. Conversely, a customer may have access to sophisticated document management systems which could save HMRC resource time.*
- 3.2 *Burden of proof can be a significant factor, especially in fact-based disputes. How important is it to each party?*
- 3.3 *What else can be brought to the negotiating table? This does not mean contemplating 'package deals', but considering what other issues / disputes could be considered simultaneously, and what other aspects of the relationship between HMRC and the customer could be usefully discussed. Some things may be worth more to the customer than expected,*

for example receiving certainty on a transaction before a key accounting date.

Things that the mediator will need to know

- 4.1 *A clear, concise background to the case, with all points in dispute highlighted.*
- 4.2 *Are there any unique features of the case which the mediator should be aware of?*
- 4.3 *What was the outcome of previous negotiations?*
- 4.4 *Have any without prejudice offers been made? What was the basis for refusal / acceptance?*
- 4.5 *Are there any issues HMRC considers to be 'red herrings' which the mediator should be aware of?*
- 4.6 *Would a chronology of events help the mediator?*
- 4.7 *If legal proceedings have already commenced, does the mediator need to see relevant documents?*
- 4.8 *What stage of disclosure has been reached? In mediation there are no formal rules of disclosure – it is important that the mediation process does not get bogged down with unnecessary documentation.*
- 4.9 *What are the particular points of fact or law which the parties agree / disagree? It is likely to be helpful to provide the mediator with some or all of the documents prepared by the parties during the pre-mediation steps – what is to be provided should be agreed between the parties.*

Mediation case-team – roles and responsibilities

- 5.1 *Identify all the individuals who will need to be at the mediation session, remembering that it may go on long beyond the end of a normal working day.*
- 5.2 *Identify any individuals who will need to be available 'on-call'.*
- 5.3 *Agree a clear decision-making process which enables a decision to be taken on the day.*
- 5.4 *Allocate roles and responsibilities to members of the mediation case team: for example, monitoring the other party's non-verbal communication; deciding who makes the opening statement at the first joint session; who is responsible for drafting responses, etc. A brief role-play rehearsal of difficult discussions likely to come up is well worth considering.*

Witnesses of fact and expert evidence

- 6.1 *Expert witnesses are not usually called during mediation sessions. However, this is a matter which should be agreed by the parties prior to the mediation.'*

Interaction with the appeal/litigation process

If HMRC and a customer agree to use ADR in a case after a formal decision has been made by HMRC, it is important that the customer also separately considers (and actions) any appeal of the HMRC decision within the relevant time limit. Failure to follow the legal process can mean that an alternative answer reached as part of the ADR process cannot be legally implemented.

Once an appeal to the Tribunal has been made, it is up to the parties to discuss and agree how to manage the ADR process and work in relation to any potential future litigation. Depending on the particular case and, for example, how much

work has already been undertaken in relation to potential future litigation, the parties may wish to:

- temporarily '*park*' work relating to the litigation process in order to allow the parties to commit fully all time/ resource to the ADR process. However, it is important to guard against ADR unnecessarily delaying the litigation process;
- work the ADR process and litigation as a "*twin track*" approach. This approach is likely to be more relevant to indirect tax cases and could impact the ability of one or both parties to commit to the ADR timetable. However, such an approach might be appropriate where, for example, the parties have already undertaken a significant amount of work in preparing for litigation and a date has already been set for the case to be heard by the Tribunal (or Court). In such circumstances, assuming the ADR process can be completed prior to the date of the hearing, the parties may wish leave the date of the hearing in the diary in order to provide some momentum/ impetus to the ADR process and to allow the litigation process to be used as a "back stop" if the parties are not able to resolve fully the dispute through the ADR process;
- where an appeal has been notified to the Tribunal, liaise with the DRU and Appeals and Review caseworker or Solicitor as to the appropriate actions to inform the Tribunal Service that ADR has been engaged.^{xxxix}

Legal professional privilege

Legal Professional Privilege (LPP) protects communications between a legal advisor and their client from disclosure, where they were conducted for the purpose of receiving legal advice (both oral and in writing) and documents that are created for the dominant purpose of gathering evidence for use in legal

proceedings. In order for LPP to be maintained, the information must remain confidential and not have been disclosed to third parties.

‘Confidentiality and privilege are absolutely key factors in the success of mediation so that the parties can be confident that what takes place in a mediation will not become public knowledge or become evidence in proceedings, of whatever kind. There is not a special mediation privilege relating to commercial mediation. At the moment, the protection conferred on mediation stems from the without prejudice principle, which renders without prejudice documents and negotiations inadmissible in evidence and those documents privileged from disclosure. There are a number of cases involving privilege in mediation which have come before the courts in recent years, and these have generally involved established exceptions to the without prejudice rule, which have been utilised to enable the court to look at what would otherwise be privileged material, both as to documents and other evidence...there is no clear category of privilege for mediators at present... We consider that, in broad terms, without prejudice privilege will be upheld in the ordinary course, but that, if there is impropriety, or if the reaching of agreement needs to be established, or if there is a good reason for applying one of the established exceptions to the without prejudice principle, it will not.’^{xxxii}

In order for both sides to be able to test fully the strength and weaknesses of their respective arguments, it will be necessary to share relevant technical analyses, some (or all) of which might be based on legal advice. It is unlikely to be necessary for HMRC to share a copy of any of its legal advice which may have been obtained (e.g. advice from Solicitor’s Office or Counsel) directly with a customer. Similarly, it is unlikely that HMRC should need to see a copy of any legal advice obtained by a customer, although some customers may decide to waive LPP and provide HMRC with copies of legal advice which they

have obtained. However, HMRC should not interpret a decision by a customer not to waive LPP over a legal document as a sign of non-collaboration.

Regardless of whether or not a customer has provided HMRC with any such documents, HMRC would not normally waive LPP in respect of confidential legal advice which has been obtained.

Rather than providing copies of any documents which might be subject to LPP, HMRC's approach will typically be to prepare and provide customers with a separate summary of its key arguments and technical analysis. If any such summary includes any reference to legal advice having been obtained, the following paragraph should always be included:

“This analysis has been confirmed by legal advice and is being provided on a “without prejudice” basis. For the avoidance of doubt, in providing this to you, HMRC is not waiving Legal Professional Privilege in relation to any specific legal advice or documents which may have been used or referred to in preparing this summary.”

Before any such summary is provided to a customer, it should be reviewed/approved by the relevant technical specialist(s) and Solicitor's Office.

It is possible that the legal advice which HMRC has obtained might be:

- specific advice based on the facts of a particular case; or
- generic advice regarding HMRC's view on the interpretation of particular areas of the law.

In either circumstance, it is possible that the legal advice obtained could help to inform HMRC's general approach to these matters or its interpretation of specific statutory provisions/case law. However, particular care should be taken

before relying on any legal advice which is not based on the customer's specific facts and circumstances.^{xxxiii}

LSS

HMRC's Litigation and Settlement Strategy (LSS) was first published in 2007 and refreshed in 2011 and 2013. It sets out the basis on which HMRC will reach agreement in a tax dispute and emphasises the benefits of a collaborative approach in achieving a resolution.

HMRC will only resolve a tax dispute consistently with:

- the law, whether by agreement with the customer or through litigation; and
- HMRC's objectives of efficiently determining and collecting the correct tax to maximise revenue flows, while reducing costs and improving the customer experience.

The LSS encourages HMRC staff to:

- minimise the scope for disputes and seek non-confrontational solutions;
- base case selection and handling on what best closes the tax gap;
- resolve tax disputes consistently with HMRC's considered view of the law;
- subject to that, handle and resolve disputes cost effectively – based on the wider impact or value of cases across the tax system and across HMRC's customer base;
- ensure that the revenue flows potentially involved make any dispute worthwhile;

- in strong cases, settle for the full amount HMRC believes the Tribunal or Courts would determine, or otherwise litigate;
- in *'all or nothing'* cases, not split the difference; and
- in weak or non-worthwhile cases, concede rather than pursue.

The LSS reflects all three of HMRC's key strategic objectives by considering:

- the overall effectiveness of disputes handling (to maximise revenue flows);
- how to reduce the scope for disputes arising and settle those that do arise as quickly and efficiently as possible (to improve customer experience); and
- the efficiency of disputes handling (to reduce costs).

The two key elements of HMRC's approach to tax disputes are:

1. supporting customers to get their tax right first time, so preventing a dispute arising in the first place; and
2. resolving those disputes which do arise in a way which establishes the right tax due at the least cost to HMRC and to its customers, which in most cases will involve working collaboratively.

Resolving disputes *'cost effectively'* does not mean HMRC making compromises on what it believes to be the right tax liability consistent with the law. It means securing the right tax liability consistent with the law, fairly and even-handedly across all customers, in a way which minimises unnecessary costs. This means that HMRC's concept of cost-effective dispute resolution may be different from the generally understood concept of cost-effective resolution of a purely commercial dispute. The following factors are likely to be

relevant to HMRC's consideration of what may or may not be '*cost effective*' in relation to the resolution of a particular tax dispute:

- the potential tax at stake in the current year(s), as well as any prior or future years, for that particular customer;
- the potential tax at stake in any year(s) for other customers (including the wider impact of any HMRC intervention, such as through behavioural responses);
- an assessment of the potential impact/effort or cost/benefit analysis of the different ways of taking forward the dispute (or not taking forward the dispute);
- an assessment of the strength of HMRC's view; and
- overall assessment of whether taking a particular course of action (e.g. litigation) is likely to be a better use of HMRC's resources than taking forward other activity which might otherwise be undertaken (likely to be relevant to governance bodies or Directors and Director Generals).

The LSS covers the whole life cycle of a dispute and therefore applies from the very beginning of any compliance activity. In many cases, the nature of the approach taken and the extent to which the parties work together can significantly influence the overall efficiency and effectiveness of HMRC's compliance activity.^{xxxiv}

Any decision by HMRC to settle a case during such a process will still be governed by the terms of the LSS and associated governance and any settlement or agreement reached as a result of ADR will be subject to exactly the same process as any other case. In rare cases, agreements may need to be provisional subject to governance processes and this will be explained as part of the ADR.^{xxxv}

Mediation agreement

Once the parties have agreed on who should be appointed, in order to appoint a particular individual, a separate formal mediation agreement will need to be entered into by both parties and the appointed mediator.

The mediation agreement represents the contract between the mediator and the parties appointing him. It sets out the terms on which the mediator is appointed and the scope of the mediation.

Typically the mediator will be able to provide the parties with a standard template formal mediation agreement, however, it is recommended that the terms of this agreement are discussed with and reviewed by the DRU. The facilitator is responsible for signing the formal mediation agreement on behalf of HMRC (this is for logistical purposes and allows the DRU to track who is authorised for which mediation).^{xxxvi}

The terms for a mediation are sometimes referred to as '*ground rules*' or '*protocols*'. There is no one set of ground rules and different approaches are or can be appropriate in different circumstances. Ground rules are important because they shape how the process will be conducted. They can also start to educate the parties about their ability to agree on matters at an early stage in discussions.^{xxxvii}

Mediation process and day

The format of the day will generally be set out for the parties by the mediator during any pre-meeting or conference call.

However, in outline, a '*typical meeting day*' would generally involve the following steps:

1. welcome from the mediator in separate rooms;

2. plenary opening statements from both sides – length agreed in advance (typically maximum of 10-20 minutes);
3. brief responses to opening statements;
4. parties return to separate rooms and the mediator holds separate sessions with both parties, alternating between the two;
5. the mediator's role is to challenge assumptions and strengths / weaknesses of positions held by both parties, help to clarify the parties' interests and needs underlying their negotiating positions, and provide a channel of communication. Whilst often the two parties may not speak directly to each other between the end of the opening session and the next plenary session, this is in the control of the mediator who may consider it beneficial to get parts of the teams together to discuss particular issues. It is generally open to either party to suggest a plenary or partial meeting but up to the mediator to arrange one if he thinks it will advance resolution;
6. any movement or offers to the other party is usually made by the mediator;
7. each party's conversations with the mediator are confidential and the mediator does not relay any information to the other party without express permission;
8. the parties come together in plenary when both sides are ready to talk face to face – this is usually at the stage when agreement in principle is reached/ imminent; and
9. when an agreement has been reached, it is documented (in outline) and signed by the parties immediately.

Mediator strategies

‘Mediators can use various strategies. They may start with the simple issues as a way of getting agreement on these, or they may hone straight in on the big issues in order to try to remove the biggest obstacle to resolution, thereby making the remaining stages of the process seem straightforward. A mediator will often encourage the parties to list all the options for resolution open to them. A mediator will also use strategies such as reality testing, to force the parties to be realistic about their approach. They may also ask the parties to conduct a cost/benefit analysis. One thing that parties need to remember is that the usual arrangement is that the parties can say whatever they want to the mediator in the break-out room, and this must be kept confidential from the other side. Of course, parties can request that a mediator discloses specific matters to the other side. Another approach is for the ground rules to provide that everything is for disclosure unless specifically kept confidential. This would not be our preference as a matter of default, but it is for consideration. In most cases the mediator will use deadlines to attempt to force the parties to take steps towards negotiation.’^{xxxviii}

Non-binding neutral evaluation

Non-binding Neutral Evaluation uses a neutral third party who is an expert in a particular field to provide a non-binding opinion. This may be suitable in limited tax cases where the issue is not tax related but determination of the issue has tax consequences, if both parties are willing to consider the strength of their case in light of the expert’s view.^{xxxix}

Position statements

Whilst a successful mediation is not a forum for legal debate it can be constructive to settlement to acknowledge weaknesses in the substantive law or

evidence. In a large or complex case the mediator may ask each party to provide him with a statement setting out their case. The document is primarily intended to ensure that the mediator is fully briefed on each side's case. The statements are also usually disclosed to the other party, so they form an important tactical function of giving the opposing party an insight into the strengths of the other side's case, and what they hope to achieve from the mediation.

Preparation

Proper preparation is vital. Representatives must remember that they are preparing for peace discussions and they should co-operate in the preparation for them.

Preparation must be proportionate and relevant to both the nature and the scale of the dispute and to the resources available to the parties, whether time, money or effort. Rarely are they infinite, The cloth therefore has to be cut according to the means.

'Parties need to rebalance their preparation. The tendency is that parties spend too much time and effort polishing up their case instead of working out:

- *what settlement they can live with;*
- *how doable it is;*
- *what one side can give the other side to help the other side, in turn give the first side what they want.*

We concentrate on three areas:

1. *specific topics which must be considered with the client, so that they do not cause problems at the mediation, such as authority;*

2. *settlement strategy, including a PMA (Pre-mediation analysis), so that the representative and his client know where the client is now and where he wants to get to; and*
3. *negotiation plan, i.e. working out how to get to where the client wants to be.*

PMA is intended to develop the mutual recognition of reality: your side's reality and the other side's. It is a structured examination with the client of:

- *the risk/reward ratio of litigation;*
- *the cost/benefit ratio of settlement;*
- *the impact of winning or losing at trial;*
- *the impact of settling or not settling;*
- *the client's current and foreseeable needs and resources;*
- *the client's risk profile; and*
- *how settlement might be structured to suit the client's needs and also the other side's.*

It can be more helpful to do some worked examples with the client of his net cash position. For most clients, what is most important for them to know is how much money they will end up with. This is a simple calculation that can be worked out for three different scenarios:

- *a good day in court;*
- *a bad day in court; and*
- *a middle day in court.^{xxl}*

Professor Andrew Goodman, Barrister, LL.B.(Soton), MBA, FCI.Arb., FInstCPD, FRSA, CEDR mediator and arbitrator, the convener of the Standing Committee of Mediation Advocates (www.mediationadvocates.org.uk), and the author of the second edition of *'Mediation Advocacy'*, emphasises and warns that,

'The ambivalent, uncertain or unprepared mediation advocate may become antagonistically involved in the dispute; or he may consider that settlement in mediation is a purely commercial matter for the client in which he does not need to participate as a lawyer. This is true of that breed of litigator who sees himself as a hired gun and finds it difficult to assume a conciliatory role even as a negotiator.'

[Whatever personal thoughts a lawyer may have about mediation, to be an effective mediation advocate he needs to] *put the client's interest first*, [and] *can only do this by:*

- *keeping an open mind;*
- *forming an understanding of the process;*
- *learning about the procedure;*
- *being prepared in all aspects of [his client's] case [facts, evidence, law, true intentions, the settlement options available, and sufficient knowledge of the costs];*
- *understanding that the legal framework of the dispute may be only one aspect of the parties' interests;*
- *being receptive to solutions which are outside the legal framework of the dispute; [and]*

- *using the mediator as a tool with which to obtain a benefit for [his] client, rather than seeing him as an obstacle.*

A lawyer or other mediation representative who has a negative attitude about the process or about being there, will not be difficult to spot:

- *he is likely to display unfamiliarity with, or ignorance of, the procedure or mediator and uncertainty over the lawyers' role or the behaviour of the mediator;*
- *he will monopolise the private sessions giving his client no chance to air private thoughts or grievances;*
- *he may well adopt the stance (or reveal his belief and advise) that to apologise or express regret is an expression of liability, express concern about having to compromise on a matter of principle, exaggerate the need to preserve face or avoid loss of face (including his own rather than that of his client), give wildly optimistic advice to his client and over rely on his initial advice.*

Such a representative is a liability: he sees only what he wants to see; he finds it difficult to acknowledge or understand his client's loss, anger or frustration; he does not consider it his role to deal with the client's goals or non-legal risks, e.g. the impact of litigation bringing adverse publicity, irretrievable lost management time, and other hidden costs.

Such a lawyer concentrates on legal questions and may miss entirely the important commercial interest, not only of his client, but those of the other side that might prompt an advantageous settlement.

He is the sort of advocate who will use vague language and clichéd expressions in the mediation, such as 'there are no guarantees' or 'who knows what the

judge will do’ – when he should be specific and advise his client about the risks involved in litigation.

Equally dangerous is the lawyer who is too sure of himself. He neglects relevant information. He ridicules good suggestions because they have been made by the other side or by the mediator.

He may consider that his client has already invested too much time and money in the conflict to settle in mediation; or he may have given bullish advice before and be fearful of challenging his own client in a private session to re-adjust the unrealistic expectations held by the client which are likely to be exposed in the process as it continues.^{xli}

Pre-meetings with the mediator

These are meeting between the mediator and the parties’ professional advisors only. The purpose of meeting is to encourage progress and to limit the so-called ‘*eleventh hour effect*’, which refers to the parties waiting until the last hours of a session to make concessions, hoping that the other will blink first.^{xlii}

Refusal to mediate

The CPR Practice Direction – pre-Action Conduct, which applies where no other practice direction or protocol is required, states that one of its aims is to ‘*enable parties to settle the issue between them without the need to start proceedings*’ (paragraph 1.1(1)), and it goes on to state that this aim is to be achieved in part by encouraging the parties to consider using a form of ADR (paragraph 1.2(2)). The practice direction specifically states that unreasonable refusal to consider ADR is an example of non-compliance (paragraph 4.4(3)). It also requires that the initial letter of claim should set out the form of ADR that a claimant deems most suitable, and seek the defendant’s consent.^{xliii}

First Tier Tribunal (Tax Chamber) Rules, r.3(1) and Upper Tribunal Rules, r.3(1) also provides that the tribunal should seek, where appropriate:

- (a) to bring to the attention of the parties the availability of any appropriate alternative procedure for the resolution of the dispute; and
- (b) if the parties wish and provided that it is compatible with the overriding objective, to facilitate the use of the procedure.

Any decision to refuse mediation at any point in time should be objectively reasonable on the facts of the particular case and the party refusing it must be prepared to explain and justify this to the court. If a refusal is judged to be unreasonable, an adverse costs order may be made against the party.

The court can do a number of things to make a reluctant party consider mediation. In particular:

1. the court can offer strong judicial encouragement to the parties to mediate their dispute. However the court will not compel parties to mediate if they are unwilling to do so;
2. the court can make an ADR order directing the parties to consider ADR, in particular mediation. This is rapidly becoming part of the standard pre-trial case management directions;
3. although the courts will not mandate parties to use mediation against their will, in some cases, the courts can direct the parties to make contact with a mediator to consider mediation. Although the court may compel the parties to consider mediation, it will not compel them to mediate if they do not wish to do so;

4. the court can stay proceedings (assuming that proceedings have been issued) and direct the parties to attempt to resolve the dispute by ADR;
5. the court may be able to assist the parties to resolve their dispute by mediation by making appropriate orders for advanced disclosure of information or documents relating to one or more issues in the case on the application of one or both parties; and
6. if one or both parties have acted unreasonably in refusing to use mediation to resolve the dispute, the court may mark its disapproval in the form of adverse costs orders.^{xliv}

Despite the various rules and changes, the key element in compulsion to mediate is litigation costs. This has been used for a long time as a means of compelling suitable litigation behaviour. The same compulsion has now been applied to mediation after the decision of the Court of Appeal in *Halsey v Milton Keynes General NHS Trust* [2004]. This compulsion operates by potentially overturning the presumption that the successful party should be awarded its costs where that party had unreasonably refused an offer of mediation. It should always be remembered that *Halsey* does not act in any way to penalise an unsuccessful party further; that party is already being penalised as a result of losing the case. The principles of *Halsey* have also been directly expressed in procedural rules and extended further. For example, the CPR Practice Direction – Pre-Action Conduct, allows the court to penalise a party who has not followed the requirements of the practice direction by forcing the payment of costs by the successful party, even on the small claims track, or forcing the payment of costs on an indemnity basis (paragraph 4.6).

While the main, and best known form of compulsion is costs-based, it is not the only means of forcing ADR. The CPR Practice Direction – pre-Action Conduct, allows for the court to sanction those who breach it in a material sense by

disallowing, reducing or increasing (to a maximum of 10% over the base rate) the amount of interest payable on any money judgment (paragraph 4.6(4)-(5). These penalties can be applied to both winning and losing parties and so operate outside the usual system of cost sanctions.

The same practice direction (at paragraph 4.6(1)) also allows for the courts to stay proceedings where there has been a breach until steps which ought to have been taken, are taken, therefore allowing a party to seek a stay for the purposes of conducting a mediation with relative ease.^{xlv}

Risk assessment

The lawyers acting for each party should ensure that a full risk assessment is carried out in relation to their client's case before the mediation. In particular they should identify their client's objectives and plan a route map for how these can be achieved in the mediation. This is likely to involve a detailed analysis of the legal and factual merits of the case, the evidence that is available to support the case and the further evidence that could be obtained, consideration of how the client's case on each issue could best be argued and what arguments can be put forward to refute the claims made by the opposing party. This will also include selection of the appropriate negotiation styles and strategies that could usefully be employed during the mediation, planning offers and concessions to be given or demanded, and the calculation of each party's BATNA and WATNA against which the merits of any offer can be assessed.

It is also important to ensure that a full cost review is carried out before the mediation and the relevant figures are brought to the mediation. A breakdown should be available of the costs and expenses that have been incurred up to the date of the mediation, and the further costs that are likely to be incurred to take the matter to trial, including the likely amount of irrecoverable costs.^{xlvi}

Role of the mediator^{xlvi}

- organising the mediation process
- acting as a facilitator during the process
- acting as intermediary between the parties

Organising the mediation process

Before the mediation

When appointed, the mediator will usually contact the parties (or their lawyers) and will explain, in a pre-mediation meeting, or by telephone, the nature of the mediation process, how they should prepare for it, his function and the role that the parties will play in the mediation. He will also advise the parties about the costs of the process. He will discuss with each party who should attend the mediation, and will check that the attendees for each party have authority to settle the case. He will also set the timetable for events that need to happen prior to the mediation.

At the mediation

- Chair the meetings and manage the process.
- Set the agenda for the mediation by suggesting the order in which issues should be negotiated, and amend it if necessary as the mediation progresses.
- Control the form that the mediation follows on the day (and discuss with the parties and/or decide whether any modifications should be made to the process to meet the needs of the case or the parties).
- Decide when discussions should take place in joint or private meetings.

- Impose or suggest a time limit for delivery of opening statements in the initial joint meeting.
- Decide whether further joint meetings should take place during the negotiation phase in addition to the opening joint meeting.
- Prevent interventions by the other side during their opening statement of the opposing party.
- Ensure parity, as far as possible, in the amount of time he spends in private sessions with each party.
- Control the form of questions that one party may put to the opposing party in the opening joint session.

Acting as a facilitator

The mediator will assist the parties to negotiate with one another in a more effective manner than they would be able to achieve on their own. The mediator will do this in the following ways:

- gather information from the parties both at the pre-mediation stage and during the mediation about the issues in dispute and their needs and interests;
- help the parties to identify the legal and factual issues, and their underlying needs and objectives;
- help the parties to listen to each other and communicate more effectively with each other;
- discourage or defuse confrontational or aggressive communications between the parties that will hinder negotiations, and reframe them if necessary;

- encourage the parties to analyse the strength and weakness of their own case and the case presented by the other side;
- perform the role of *'reality-checker'*, perhaps by assuming the role of *'devil's advocate'*, if the parties are unrealistic in their assessment;
- encourage the parties to think about their BATNA and WATNA, and ensure that they have carried out a full risk analysis, including the costs (and irrecoverable costs of proceeding to trial);
- review the negotiations that have already taken place between the parties, and encourage each party to reflect on why they failed and how they can change their position to move the matter forward;
- encourage brainstorming and the generation of options for settlement, including the identification of common ground between the parties; and
- create and use strategies and options to end deadlock between the parties.

Acting as intermediary

The mediator will act as the *'go-between'* or *'shuttle-diplomat'* during private meetings of the parties. He will convey offers, concessions and information, rejections, concessions and counter-offers from one party to another. He will enable the parties to negotiate through him as intermediary, rather than with each other face to face. He will keep a record of any agreement reached on individual issues as the negotiation progresses, as this will help with drawing up any final overall settlement agreement.

Role of the mediation advocate

'Unlike the representative function of counsel at trial, the mediation advocate is not present principally to convey his client's case to the mediator and the other side. He has an equally important role as his client's adviser. He must protect

his client's best interests, as he sees them, while at the same time trying to make the process work. Occasionally these responsibilities conflict. The advocate must continually evaluate the case and its progress in the mediation. He must stand up to an overzealous mediator, when necessary. And while focussing on his client's legal interests, he must think laterally if a solution is to be found to overcome resistance while accommodating his client's legal position.

When in joint session the advocate will usually either present the argument or support the decision maker in presenting it ...[the advocate] should avoid up-beat submissions, but express confidence in the merits balanced with an emphasis on attending the mediation in good faith and with the intention of finding a solution.

Advocacy during private sessions is equally different from trial work. A confrontational style is out of place. Consistent with defending your client's position, your mindset should be that the dispute is a problem to be solved not a conflict to be won. Therefore you need a constructive, problem solving approach.

You may need to overcome the mediator in caucus because he exerts a powerful influence. Allow him as a neutral to act instinctively. But be prepared to go back to the plenary session, to meet the lawyers on the other side, assist technical experts in a session confined to their discipline, and above all to view the process flexibly. This includes allowing discussions between clients and, where different, between principal decision-makers. For a lawyer to let go of his client in this way is difficult, but you must learn to let go at the right time.

You will need to support your client throughout the negotiation process: be a friend and supporter to the decision-maker when times get tough.

Consider inventive solutions as ways to overcome deadlock. Try to avoid entrenched positions: encourage your client to keep his temper under control, and as a last resort encourage him to stay when he talks of leaving. ^{xlviii}

Settlement

Documenting the agreement

It is vital to record the terms agreed in writing at the end of the mediation. Even where the terms are relatively straightforward and the parties trust each other, it is very risky to leave the outcome as an oral contract. It is all too likely that memories of what was agreed will differ, or that one party may on reflection seek to change a detail and the agreement will be lost. A settlement agreement is essentially a contract, and will be bound by contractual principles.

It is likely that, for the majority of tax disputes going through an ADR process, the intention of both parties will be to try to resolve the dispute if possible.

Where HMRC and the customer are able to reach an agreement or a proposed agreement through ADR which will be subject to governance, it is important that the agreement is documented and signed by both parties on the same day and noted as being subject to HMRC internal governance. At this time, it is possible that the parties may not be able to agree the detailed calculations of liability that flow from the terms agreed, but this should not prevent the parties from documenting the key points or principles agreed. The document might include reference to terms and conditions outlined in the ADR process agreement and / or formal mediation agreement. Where litigation proceedings have already begun, a settlement agreement may be made by consent order (also known as a ‘Tomlin order’) under Rule 34 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. This allows the settlement to take effect immediately, without the 30-day ‘cooling-off’ period provided for in s54 TMA 1970/ s85 VATA 1994. It may be advisable to initially document heads of

agreement on the day, with a consent order to follow so that the terms can be reviewed / agreed by Solicitor's Office.

As an alternative, and in cases where litigation proceedings have not begun, the settlement will need to be formalised in the same way as for any out of court settlement of the tax matters in dispute (e.g. contract settlement or s.54 TMA 1970 agreement for direct tax disputes, or s.85 VATA 1994 agreement for VAT disputes). Here too, it may be advisable to initially document heads of agreement on the day, with the formal settlement process to follow once reviewed / agreed by Solicitor's Office again, subject to any HMRC internal governance requirements.

What happens if only partial agreement is reached?

Generally, discussions and any negotiations in an ADR process are on a without prejudice basis and therefore any partial agreement on any matter of substance will not be recorded. However, it may be the case that during ADR, progress is made in narrowing particular points of disagreement or in clarifying facts and the parties may agree that it is useful to document these points (e.g. for use in subsequent litigation).

What happens if no agreement is reached?

This should be pre-agreed between the parties and is likely to be set out in either the ADR process agreement or the formal mediation agreement. As with any tax dispute, if HMRC and the customer are not able to resolve the dispute through bilateral discussion then – unless either party concedes the issue – it is likely that the dispute will ultimately need to be resolved by litigation.^{xlix}

Sharing and testing views/arguments

HMRC does not have a monopoly on understanding how tax law applies to a particular set of facts. Therefore, where HMRC has worked collaboratively with

a customer to establish the relevant facts in relation to a particular transaction, HMRC will want to similarly work collaboratively to understand fully the tax law which might potentially apply in order to determine the appropriate treatment.

Where a tax return has been filed, a discussion is likely to start with the tax treatment adopted by the customer and will explore the analysis/relevant law which the customer considers supports the treatment adopted. Where a tax return has not been submitted (e.g. discussion of a transaction is in real time), an appropriate starting point might be an open discussion between HMRC and the customer regarding the various technical provisions which could apply.

In either case, HMRC should be open about sharing with a customer its preliminary views as to the potential analysis/law which it considers might apply to a particular transaction.

In cases where specialist advice is required, it will be helpful for HMRC to have obtained an understanding of the customer's technical analysis in advance of requesting the specialist advice, so that this can be considered in detail and any clarifications sought/detailed response provided. However it is generally not appropriate to consider jointly instructing Counsel for advice, as Counsel's role is to advise each party on the particular merits of their arguments, not to act as arbiter.

Before reaching a considered decision, HMRC should seek to ensure it has:

- a full understanding (and, where necessary, has clarified) the customer's view as to the relevant facts and appropriate technical analysis;
- clearly articulated (whether in writing or at a meeting) its preliminary view to the customer as to potential alternative technical analyses which might apply;

- actively sought to test the relative strengths/weaknesses of the respective technical analyses which might apply (both with the customer and also internally with other HMRC team members);
- obtained any specialist advice required; and
- made an informed assessment as to the strengths/weaknesses of the potential technical analyses which might apply.

In many cases, it can be helpful to have a meeting with the customer in order to discuss respective views and arguments. A meeting can help to avoid protracted exchanges of correspondence and can also help both parties get a better understanding of the other's position. In order to ensure any meeting is as productive as possible a detailed agenda should be agreed between the parties well in advance so that both are clear on the specific areas/risks to be discussed, can prepare adequately and ensure that appropriate individuals attend the meeting.

The aim of ensuring that HMRC fully understands the customer's view and has fully tested its own arguments is to ensure that HMRC does not pursue disputes where it lacks strong arguments. Equally, where HMRC decides to pursue a dispute, it helps to focus on the strongest arguments; on occasions good technical arguments can be undermined by being mixed with poor/weaker ones and such an approach can help to avoid this.

Having reached an initial conclusion, tested it and reached a considered decision, HMRC should either:

- advise the taxpayer that it accepts the analysis (i.e. risk is resolved or dispute is dropped), or
- set out the basis of its technical arguments/analysis which it intends to pursue further (together with any explanations/ clarifications required).

However, even after HMRC has reached a considered decision it will continue to be open to considering the impact of any new information and/or analysis

since, in certain circumstances, this may provide the basis for resolving a dispute.

Where HMRC's position on a tax dispute depends on the outcome of other disputes turning on the same issue, HMRC should bring that to the customer's attention.¹

Splitting the difference

Splitting the difference does not give a result consistent with the law, so is not something HMRC can entertain.

In connection with the reference in guidance on LSS (paragraph 16) to ADR, it should be noted that mediation is not about '*splitting the difference*'/compromising, but about supporting the parties in reaching agreement, where they are able to do so. It follows that HMRC will not be able to compromise on a genuinely '*all or nothing*' dispute simply because that was being addressed as part of a mediation.

Suitable cases

The most suitable cases for mediation are those which are substantially fact dependent and where matters of principle are not or not absolutely central to the dispute.

HMRC has adopted a policy of being relatively open-minded about the types of cases in which mediation may be suitable. ADR should generally be considered in all cases that are headed for litigation or are otherwise protracted. More specifically, ADR may be appropriate where any or all of the following points apply:

1. the parties are seeking to work collaboratively but:

- 1.1 it is proving difficult to pin down the essential point(s) of disagreement,
- 1.2 HMRC and the customer appear to be at cross purposes, or
- 1.3 there is uncertainty about the other party's position, underlying rationale or process for resolving disputes;
2. collaborative working relationships appear to have broken down and ADR may help to restore them;
3. the point at issue appears to be '*all or nothing*' but there is a possibility that structured discussions might uncover (an) alternative approach(es) which would enable HMRC to resolve the dispute in accordance with the terms of the LSS;
4. the point at issue appears to be '*all or nothing*' but there may be some misunderstanding or disagreement over how the facts ought to be weighted in coming to a decision;
5. the dispute may be able to be resolved by having a wide ranging discussion of the issues on a non-prejudicial basis (although this would not entail setting off issues against others in a '*package deal*');
6. a narrowing or clarification of the facts or issues in the dispute is necessary. This may be particularly useful in fact-heavy disputes such as transfer pricing;
7. agreement is needed on what facts are relevant and should be disclosed to progress resolution of a dispute;
8. out of court settlement is likely to be preferable to determination by the Tribunal/ Courts, for example, because:

- 8.1 it is likely to result in a quicker and more cost effective resolution of the dispute or part of the dispute;
 - 8.2 evidentiary difficulties for one or both parties increase the risks of proceeding to Tribunal; or
 - 8.3 complex or unique facts mean that a potentially costly and time-consuming judicial determination would be of little or limited precedent value.
9. Cases can still be considered for ADR even if the parties initially feel that the dispute turns exclusively on points of law. ADR can uncover a wider range of possible solutions than those generated by a traditional negotiation process, or assist in understanding what ‘*weight*’ should be given to conflicting facts, generating an LSS compliant result without the need to go to Tribunal.
10. ADR can help to resolve one or more issues in dispute with the same customer. This could include situations where issues are intertwined or one issue impacts on another. It may also include situations where there are a number of entirely separate issues – in such cases considering a number of disputes simultaneously may help to unlock the resolution process. Where there is more than one dispute between a customer and HMRC, the LSS provides that each dispute must be considered and resolved on its own merits, not as part of any overall “*package deal*”. As a matter of process, however, it may be that a number of unrelated disputes will be resolved at the same time (each on their own merits), for example as part of a process of bringing a customer’s tax affairs up to date.

ADR can also be used to try to resolve certain aspects within a dispute, such as factual arguments over what information is relevant, or narrowing either points

for litigation or subsets of points of law or fact under dispute, for instance issues of valuation.

When attempting to resolve a dispute through the ADR process, it is desirable to strive to resolve all aspects of the dispute, including any interest, penalty and/ or payment issues.

Even in an '*all or nothing*' case which HMRC is prepared to litigate because it has high expectations of success, the ADR process might offer both parties some potential value added compared with litigation. This is the idea of using negotiation to enlarge the pie rather than simply carving it up. The sort of things which could be important to a customer, over and above their position on the point of substance, could include:

1. the need to be listened to and have their position or point of view taken seriously;
2. opportunity to engage with HMRC specialist(s) as well as a CRM or other case owner;
3. possible recognition of their motivation in relation to the transaction in question;
4. certainty as a result of retaining control over the detailed outcome; and
5. impact on how they are perceived by HMRC in future.

This might mean that even where HMRC see the particular point in dispute as '*all or nothing*' in terms of negotiating positions, the dispute as a whole could be susceptible to a range of outcomes in terms of the underlying needs and interests of the parties.^{li}

Timing

The stage at which a particular tax dispute may be suitable for mediation will vary from case to case. There is no hard and fast rule as to when mediation should be attempted.

However, as a general rule, ADR should only be considered when both sides have attempted to explore fully the facts and their respective technical arguments. As such, ADR should not be seen as (or sought to be used as) a substitute for collaborative working/ discussions as part of the usual enquiry process.

ADR can help to focus areas of disagreement in long-running, complex disputes. Where disputes turn on points of law, case-teams should seek legal advice before considering ADR. Case-teams are encouraged to critically evaluate advice received from Counsel with the help of HMRC Solicitor's Office.

In cases where it is proving exceptionally difficult to reach agreement on the relevant facts, or where there is a breakdown in collaboration over what factual disclosure is needed to elicit the relevant facts, there may possibly be a role for ADR in helping to unblock this aspect.

ADR can be considered either before or after the issuing of a formal decision by HMRC.^{lii}

If further information or documentation needs to be obtained to enable an evaluation of the strengths and weaknesses of each party's position to be assessed, there is no reason why the parties could not agree that this should be done in advance of mediation, or as part of the agreed mediation procedure.

Rarely will it be appropriate to mediate as soon as HMRC have opened an enquiry. In many instances the existence of an enquiry does not necessarily

mean that there is even a dispute – it is simply a case of HMRC checking the accuracy of the customer’s return. Once the issues have become apparent and it is obvious that there is a substantive dispute between the parties, mediation can be considered.^{liii}

Unsuitable Cases

Mediation is voluntary, so it will not be suitable where the customer or HMRC do not wish to pursue this option. If a case does not fall within any of the parameters set under the entry headed ‘*Suitable cases*’ below, then this significantly increases the likelihood that HMRC will not agree to mediate.^{liv}

ADR should only be considered in cases where the process is likely to add value. Therefore, in general, ADR is unlikely to be appropriate if the benefits of using it in the particular case (and how it might help the parties resolve a dispute) cannot be clearly identified, articulated and agreed between the parties.

More specifically, ADR is unlikely to be appropriate where any of the following points apply:

- the customer does not work with HMRC in a collaborative manner or on the specific dispute has indicated that they do not wish to try ADR;
- it would be more efficient to have an issue judicially clarified so that the precedent gained can be applied to other cases;
- resolution can only be achieved by departure from an established ‘*HMRC view*’ on a technical issue, and no exceptional facts or circumstances exist to justify a departure from the law or practice;
- there is reason to suspect lack of integrity on the part of the customer, whether or not criminal proceedings are envisaged;

- there is doubt over the veracity or strength of evidence provided and HMRC wish to test it by cross-examination in a public tribunal; and
- an appeal has been listed for hearing at the Tribunal and entering into an ADR process would result in that hearing being postponed.^{lv}

HMRC internal guidance states that, *'ADR should not be entered into within an existing dispute resolution process unless there is a possibility of adding to or creating efficiencies. For example, cases in HRCP are already utilising mediation techniques in certain areas and increasingly a collaborative approach is being adopted across risk working/ compliance checks more generally. Equally, an issue within HRCP governance could potentially 'fast-track' to an ADR session if much of the preparatory work has already been done.'*^{lvi}

LSS Paragraph 18 states,

'Where HMRC believes that it is likely to succeed in litigation and that litigation would be both effective and efficient, it will not reach an out of court settlement for less than 100% of the tax, interest and penalties (where appropriate) at stake. It therefore follows that, if the customer is unwilling to concede in such cases, HMRC will seek to resolve the dispute by litigation as quickly and efficiently as possible.'

Therefore a dispute that turn on points of law may not be suitable for mediation.

Without prejudice rule

The without prejudice rule and exceptions to it apply to communications passing between the parties made in the context of a mediation, so these cannot be relied on or referred to in subsequent court proceedings if the mediation is unsuccessful. The without prejudice rule is often specifically stated in the mediation agreement between the parties and is further strengthened by a

confidentiality clause. The court will uphold these clauses and grant an injunction to restrain a party from referring to any part of the discussions that took place during the mediation.

In mediation, the following communications will be protected from disclosure by operation of the without prejudice rule:

- any oral or written communications made specifically for the purposes of settlement, such as position statements, correspondence about the mediation, offers or concessions whether made before, during or after the mediation;
- any communications passing between parties and the mediator before, during or after the mediation with a view to exploring settlement; and
- communications created for the purpose of trying to persuade the parties to mediate.

The rules will protect communications aimed at settlement which pass between the parties themselves or between their respective lawyers and it is also likely to protect communications passing between the parties and the mediator. It will also operate to protect investigations carried out as part of the mediation process.^{lvii}

Who within HMRC decides whether or not ADR is appropriate in a particular case

Proposing mediation

Either party to a dispute can propose mediation.

The customer

Where the customer wishes to propose ADR, they should inform the CRM or case-owner and notify the DRU. The CRM/case-owner should discuss with the

customer what may be the potential benefits of using ADR as well as with all internal HMRC stakeholders involved in the issue. The DRU will liaise with the CRM or case-owner to help them understand what is being proposed and assist in articulating the potential benefits or downsides of an ADR approach. Where the CRM or case-owner and the DRU agree that ADR would be appropriate, they will authorise the agreement of the customer's suggestion and make appropriate arrangements to take the process forwards and inform the ADR Panel that the decision to accept the customer's proposal for ADR has been agreed.

Where it is considered either by the CRM/case-owner or by the DRU that ADR is not appropriate, the DRU will arrange for the request to be presented to the ADR Panel for them to make a formal decision on behalf of HMRC. The ADR Panel consists of the Head of the Dispute Resolution Unit, the Director Tax Professionalism and Assurance, the Director LBS and the General Counsel and Solicitor. This decision will be communicated to the CRM / case-owner and to the customer.

HMRC

Where an HMRC CRM or case-owner or member of their team considers ADR may be appropriate, they should obtain consensus from the case team, and all other internal stakeholders and inform the DRU before approaching the customer. The DRU will want to understand what the potential benefits of such a process may be. If the DRU concur with the suggestion, they will arrange for a formal decision to be made by the ADR Panel after which the CRM or case-owner as appropriate is authorised to suggest ADR to the customer, who can accept or decline the offer. If the customer requires more information about the process before making a decision, they should be referred to the DRU. In some cases, if agreed with the case team, it may be more appropriate for the DRU or

an HMRC facilitator to make the approach to the customer, for example, where it would be beneficial to emphasise the impartial nature of the ADR process.

Should the DRU not agree that ADR is appropriate, they will not authorise the CRM or case-owner to make the suggestion and will refer the request to the ADR Panel for a formal decision.^{lviii}

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Disclaimer

The information set out above is only intended as a general guide, and is provided on the basis of no liability for the information given. If you want advice about English law upon which legal reliance may be placed you can instruct Carl Islam to provide it.

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xxvi	Guidance, p.5.
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