[2019] UKFTT 31 (TC)

TC06927

Appeal number: TC/2017/03422

Corporation tax – company's failure to notify chargeability to tax – late returns penalties under Schedule 41 Finance Act 2008 – Schedule 18 Finance Act 1998 – director's loans – penalties under Sections 455 and 458 Corporation Tax Act 2010 – s 7(3) Schedule 4 – whether reasonable excuse – no – whether special circumstances – no – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

STARFLEX CONTRACTORS LIMITED **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE MICHAEL CONNELL
MEMBER JOHN WILSON

Sitting in public at Tribunals Service Tax, Alexandra House, 14-22 The Parsonage, Manchester on 9 July 2018

Mr Andrew Taylor of Whitnalls Chartered Accountants for the Appellant

Mr Paul Eyles, Officer of HMRC, for the Respondents

DECISION

The Appeal

1. This is an appeal by Starflex Contractors Limited ('the appellant') against HMRC's decision to charge penalties of £10,840.28 under Schedule 41 Finance Act ('FA') 2008 for failure to notify the appellant company's chargeability to tax in respect of each of the tax periods ending 2 December 2011, 31 December 2011, 31 December 2012, 31 March 2013, and 31 March 2014. Of this, £5,524.98 is no longer under dispute. The balance of £5,315.30 is the subject of this appeal and that part of the total penalties as relates to the failure to declare timeously amounts due under s 455 Corporation Tax Act ('CTA') 2010.

Background

2. The appellant company was incorporated on 3 December 2010. It manufactures bedroom furniture and is based at Knowsley Industrial Park, Kirby, Liverpool. Mr John Law is the company's sole director, appointed on 31 January 2011.

3. The appellant company's tax return for 2010-11 was due twelve months after the end of its accounting period. A penalty is payable if the return is filed late. There is a separate deadline for a company to pay its Corporation Tax, which is usually nine months and one day after the end of the accounting period.

4. The appellant also failed to file its returns or pay tax due on time for the following four years.

5. Tax Returns for the company's accounting periods ended 2 December 2011 and 31 December 2011 were only received by HMRC on 10 July 2015; accounts for the accounting period ended 31December 2012 and 31 March 2013 were only received on 6 March 2015 and the accounts for the accounting period ended 31 March 2014 were only received on 9 June 2015.

6. The company's accountants, Whitnalls, who were not appointed until 2015, explain that the company was suffering from poor cash flow in the early years and the sole director was pre-occupied with building up the business. There was also confusion as to the accounting period ends, particularly with regard to the earlier years.

7. The accounts for the first periods of trading to 31 December 2011 and 2012 were simply overlooked as there was a delay in finalising each year's figures. The year to 31 March 2013 (i.e. a fifteen month period) was based on one set of Financial Statements. The 2013 return and the return to 31 March 2014 were late due to the fact that the accounts for 2011 and 2012 were waiting to be finalised.

8. On 8 October 2015, shortly after the company had filed all the outstanding returns, HMRC opened enquiries into all the returns under Paragraph 24(1), Schedule 18 of the

Finance Act 1998. An analysis of the Director's Loan Account covering the period 3 December 2010 to 31 March 2014 was requested.

9. Pursuant to the provisions of s 455 CTA 2010, if a director takes a loan from the company, the loan must be repaid within nine months of the end of the company's Corporation Tax accounting period. If the loan is not paid within this period the company must pay Corporation Tax at 32.5% of the outstanding amount, or 25% of the loan (where made before 6 April 2016). Interest on the Corporation Tax is added until the Corporation Tax is paid or the loan is repaid. The Corporation Tax can be reclaimed, but not interest.

10. HMRC informed the appellant company that under Schedule 41 FA 2008, penalty assessments were due for the late returns/failure to notify chargeability and penalties were also due under s 455 CTA 2010 in respect of director's loans.

11. On 17 March 2016, following correspondence with Whitnalls, outstanding amounts for the Director's Loan Account were agreed as for each year ending as follows:

- 2 December 2011 - £60,635,
- 31 December 2011 of £6,269,
- 31 December 2012 of £70,316,
- 31 March 2013 of £8,488.

12. The table below shows the revised Corporation Tax, Corporation Tax penalties, and s 455 penalties charged by HMRC on the Appellant. Those penalties marked with an asterisk were prompted disclosures. HMRC regarded all years as non-deliberate.

APE	Date Returns received late	PLR	Revised CT	Revised s455 tax	Penalty %	CT Penalty	Section 455 Penalty
2 December 2011	10 July 2015	£15,158.75	Nil	£15,158.75	20%*	Nil	£3,031.75
31 December 2011	10 July 2015	£1,567.25	Nil	£1567.25	20%*	Nil	£313.45
31 December 2012	6 March 2015	£26,791.60	£9212.60	£17579.00	10%	£9212	£1,757.90
31 March 2013	6 March 2015	£4,719.80	£2597.80	£2122.00	10%	£2597	£212.20
31 March 2014	9 June 2015	£43,439.40	£43,439.40	Nil	10%	£43439	Nil

						£55249	£5,315.30

13. The agent agreed that there had been a failure to notify to HMRC the company's chargeability to tax within twelve months from the end of each year's accounting period, but asked for the penalties under s 455 CTA 2010 to be cancelled as there had been no actual loss in tax revenue (from the failure to notify) "*as over the years the tax effect is neutral as each year negates the other and the only matter arising would be in respect of interest*". The agents said *"It would appear that technically, you are correct in your statements, but we would have thought that substance over form would prevail in cases such as this where indeed there has been no lost Revenue to HMRC whatsoever".*

14. HMRC explained that penalties for 'failure to notify' cannot be waived, but as a compromise the penalties would be downgraded from deliberate to non-deliberate and full reductions for quality of disclosure would be given. The penalty maximum was therefore 30% of the potential lost revenue ('PLR'). The years to 31 December 2011 and 2014, were regarded as 'prompted' and the years 2012 and 2013 unprompted, therefore attracting penalties of 20% and 10% respectively.

15. On 4 January 2017, HMRC issued a penalty notice in the amount of £10,840.28 for the company's failure to notify liability to tax for each the accounting periods. Only the s 455 penalties of £5,315.30 were disputed.

16. On 24 March 2017, HMRC, after receiving an appeal and subsequent request for a review, issued their review conclusion upholding the assessment. Officer Greg Carson who conducted the review referred to Paragraph 7(3) Schedule 41 FA 2008 which states that any tax liability remaining unpaid twelve months after the end of the relevant accounting periods, due to a failure to notify, constitutes PLR for Schedule 41 FA 2008, failure to notify penalty purposes. This includes amounts that are charged to Corporation Tax under the legislation at s 455 CTA 2010 for the year.

17. He added that Paragraph 7(4) Schedule 41 FA 2008 excludes taking into account relief subsequently being due under s 458 of CTA 2010 in the calculation of Corporation Tax liability remaining unpaid twelve months after the end of the relevant accounting periods due to the company's failure.

18. Officer Carson said that any amounts reported as overdrawn in respect of a director's loan account at the end of the relevant accounting period, which are caught by the legislation at s 455 CTA 2010, would be included as PLR for Schedule 41 FA 2008 penalties purposes. The agent's submission that there is no PLR for Schedule 41 FA 2008 penalty purposes, because the s 455 CTA liability only arises due to timing issues and having being subsequently been repaid, was technically incorrect. The legislation specifically disallows taking into account relief due because of repayment of director's loans in subsequent periods.

19. The Officer summarised the Corporation Tax liability for the relevant accounting periods, as agreed with the company's agent, as follows:

Accounting Period	3 Dec 2010 to 2 Dec 2011
Revised CT:	£Nil
Revised S455 Tax:	£15,158.75

Accounting Period	3 Dec 2011 to 31 Dec 2012
Revised CT:	£Nil
Revised S455 Tax:	£1,567.25

Accounting Period	1 Jan 2012 to 31 Dec 2012
Revised CT:	£9,212.60
Revised S455 Tax:	£17,579.00

Accounting Period	1 Jan 2013 to 31 Mar 2013
Revised CT:	£2,597.80
Revised 5455 Tax:	£2,122.00

Accounting Period	1 Apr 2013 to 31 Mar 2014
Original CT:	£43,439.40
Original 5455 Tax:	£Nil

20. The Officer said that whereas the agent says that the penalties arise solely because of s 455 CTA 2010 liability charged in relation to overdrawn director's loan accounts, the figures above show this to be incorrect.

21. On 19 April 2017, the appellant notified its appeal to the Tribunal. The grounds of appeal as stated in the Notice of Appeal and in the appellant's skeleton arguments to the Tribunal, as stated by Whitnalls are:

> "1. The Appellant does not dispute the corporation tax penalties for late notification of the actual corporation tax liability. Our appeal is based on the levying of penalties under Section 455 Corporation Tax on Overdrawn Director's Loan Account in the sum of £5,315.30 when there has been no revenue loss to HMRC.
>
> 2. Whilst Section 455 Corporation Tax should have been applied and paid at the relevant times, this would have been repaid to the company in the fullness of time, hence the tax neutrality of the situation should itself lead to the fact that a penalty is not required.
>
> 3. The fact that the Director's Loan Accounts were since brought back into credit and that therefore there is no PLR to HMRC constitutes special circumstances.
>
> 4. Whilst accepting HMRC's arguments with regard to technical matters and case law quoted, some form of leniency could be shown by either removing the penalties completely in this instance or by way of a reduction. A special reduction was not considered or offered to the Appellant by HMRC, nor did they request details of special circumstances applying.
>
> 5. The Appellant has never been given the opportunity of having the penalty suspended. HMRC, by their own admission, have reduced the seriousness of the penalty from a deliberate act to non-deliberate. Therefore, it would have been more equitable if penalties

arising in this regard could have been suspended with the Company agreeing to comply for a period of 12 or 24 months. They were never given this opportunity.

6. The penalties are inequitable."

Evidence

22. The bundle of documents prepared by HMRC consisted of:

(1) Correspondence between HMRC and the appellant's agent.
(2) Closure notices, Discovery notices and Notices of Appeal.
(3) Copy financial accounts and computations for each year in question.
(4) A copy director's loan account summary.
(5) A witness statement by Kevin Cross, the HMRC Officer who had conduct of the matter and determined the penalties
(6) Skeleton arguments by both parties

Relevant legislation

23. The relevant legislation is contained in:

Schedule 18 Finance Act 1998

2(1) A company which-
(a) is chargeable to tax for an accounting period, and
(b) has not received a notice requiring a company tax return,
must give notice to the Inland Revenue that it is so chargeable.

(2) The notice must be given within twelve months from the end of the accounting period.

(3) A company which fails to comply with this paragraph is liable to a penalty not exceeding the amount of tax payable for the accounting period in question that remains unpaid twelve months after the end of the period.

(4) In computing the amount of unpaid tax for this purpose, no account shall be taken of any relief under section 419(4) of the Taxes Act 1988 (relief in respect of repayment, etc. of loan) which is deferred under subsection (4A) of that section.

Finance Act 2008 Schedule 41

Paragraph 1

A penalty is payable by a person (P) where P fails to comply with an obligation under Paragraph 2 of Schedule 19 to Finance Act 1998.

Paragraph 6

6(1) This paragraph sets out the penalty payable under paragraph 1.
6(2) If the failure is in category 1, the penalty is-

(a) for a deliberate and concealed failure, 100% of the potential lost revenue.
(b) for a deliberate but not concealed failure, 70% of the potential lost revenue, and
(c) for any other case, 30% of the potential lost revenue.

Paragraph 7

7(3) in the case of a relevant obligation relating to corporation tax and an accounting period, the potential lost revenue is (subject to sub-paragraph (4)) so much of any corporation tax to which P is liable in respect of the accounting period as by reason of the failure is unpaid 12 months after the end of the accounting period.
7(4) In computing the amount of that tax no account shall be taken of any relief under section 458 of CTA 2010 (relief in respect of repayment etc. of loan) which is deferred under subsection (5) of that section.

Paragraph 12

12(1) Paragraph 12 provides for reductions in penalties under paragraphs 1 to 4 where P discloses a relevant act or failure
12(2) P discloses a relevant act or failure by-
(a) telling HMRC about it,
(b) giving HMRC reasonable help in quantifying the tax unpaid by reason of it, and
(c) allowing HMRC access to records for the purpose of checking how much tax is so unpaid.
12(3) Disclosure of a relevant act or failure-
(a) is "unprompted" if made at a time when the person making it has no reason to believe that HMRC have discovered or are about to discover the relevant act or failure, and
(b) otherwise, is "prompted".
12(4) In relation to disclosure "quality" includes timing, nature and extent.

Paragraph 13 Schedule 41 Finance Act 2008 says:

13(1) If a person who would otherwise be liable to a penalty of a percentage shown in column 1 of the Table (a "standard percentage") has made a disclosure, HMRC must reduce the standard percentage to one that reflects the quality of the disclosure.

Paragraph 20 states:

(1) Liability to a penalty under any of paragraphs 1, 2, 3(1) and 4 does not arise in relation to an act or failure which is not deliberate if P satisfies HMRC or (on appeal) the First-tier Tribunal that there is a reasonable excuse for the act or failure.

(2) For the purposes of sub-paragraph (1)-

(a) An insufficiency of funds is not a reasonable excuse unless attributable to events outside P's control,

(b) where P relies on any other person to do anything, that is not a reasonable excuse unless P took reasonable care to avoid the relevant act or failure, and (c)

where P had a reasonable excuse for the relevant act or failure but the excuse has ceased, P is to be treated as having continued to have the excuse if the relevant act or failure is remedied without unreasonable delay after the excuse ceased.

Corporation Tax Act 2010

Section 455

'Charge to tax in case of loan to participator'
(1)This section applies if a close company makes a loan or advances money to-

(a) a relevant person who is a participator in the company or an associate of such a participator,

(b) the trustees of a settlement one or more of the trustees or actual or potential beneficiaries of which is a participator in the company or an associate of such a participator, or

(c) a limited liability partnership or other partnership one or more of the partners in which is an individual who is-

(i) a participator in the company, or

(ii) an associate of an individual who is such a participator.

(2) There is due from the company, as if it were an amount of corporation tax chargeable on the company for the accounting period in which the loan or advance is made, an amount equal to [F2such percentage of the amount of the loan or advance as corresponds to the dividend upper rate specified in section 8(2) of ITA 2007 for the tax year in which the loan or advance is made]

(3) Tax due under this section in relation to a loan or advance is due and payable in accordance with section 59D of TMA 1970 on the day following the end of the period of 9 months from the end of the accounting period in which the loan or advance was made.

Section 458

458(5) Relief in respect of the repayment, release or writing off may not be given under this section at any time before the end of the period of 9 months from the end of the accounting period in which the repayment, release or writing off occurred.

Discussion and Conclusion

24. The appellant accepts that penalties are properly chargeable under Schedule 18 Finance Act 1998. It only appeals the s 455 penalties and says that these are inequitable and that a reduction should have been applied or the penalties waived on the grounds that there were special circumstances. The appellant also asserts that a suspension of the penalties should have been considered.

Assessment of the penalties

25. HMRC considered the reductions allowed for disclosure at paragraphs 12 and 13 of Schedule 41 FA 2008 and allowed full reductions to the penalty for 'telling, helping and giving', as evidenced in the penalty schedules sent to the company. This reduces the penalties for failure to notify from the maximum of 30% of PLR to 20% of PLR and 10% of PLR for prompted and unprompted disclosures respectively. This is the maximum reduction HMRC could have allowed to the company.

26. Paragraph 7(3) Schedule 41 FA 2008 provides that in the case of a relevant obligation relating to Corporation Tax and an accounting period, the PLR is (subject to sub-paragraph (4)) so much of any Corporation Tax to which P is liable in respect of the accounting period as by reason of the failure is unpaid 12 months after the end of the accounting period. Section 7(4) provides that in computing the amount of that tax, no account shall be taken of any relief under s 458 of CTA 2010 (relief in respect of repayment etc. of loan) which is deferred under subsection (5) of that section.

27. Section 458(5) CTA 2010 provides that relief in respect of repayment, release or writing-off may not be given under this section at any time before the end of the period of 9 months from the end of the accounting period in which the repayment, release or writing off occurred.

28. Paragraph 7(3) Schedule 41 FA 2008 states that any tax liability remaining unpaid 12 months after the end of the relevant accounting periods due to a failure to notify constitutes PLR for Schedule 41 FA 2008 failure to notify penalty purposes. This includes amounts that are charged to Corporation Tax under the legislation at s 455 CTA 2010 for the year.

29. Furthermore, paragraph 7(4) Schedule 41 FA 2008 excludes taking into account relief subsequently being due under s 458 of CTA 2010 in the calculation of Corporation Tax liability remaining unpaid 12 months after the end of the relevant accounting periods due to the company's failure.

30. Therefore any amounts reported as overdrawn in respect to director's loan accounts at the end of the relevant accounting period which are caught by the legislation at s 455 CTA 2010 will be included as PLR for Schedule 41 FA 2008 penalties purposes. The legislation specifically disallows taking into account relief due because of repayment of director's loans in subsequent periods.

31. The penalty notice has been properly issued in accordance with the requirements at Paragraph 16 Schedule 41 FA 2008. The appellant was notified in the penalty notice and the notice states the periods for which the penalty is being charged.

Special circumstances

32. Paragraph 14 Schedule 41 FA 2008 allows special reduction to failure to notify penalties where special circumstances arise. There are no special circumstances surrounding this case.

Reasonable Excuse

33. The legislation at Paragraph 20 Schedule 41 FA 2008 allows the Tribunal to withdraw all or part of the disputed penalties if it is satisfied that the appellant has a reasonable excuse.

34. There is no statutory definition of reasonable excuse. However, case law does give some guidance. Judge Redston in *Perrin* [2014] TC 03614 reviewed the authorities including the decisions of Judge Brannan in *Coates* [2012] TC 02154 and Judge Medd in *Clean Car Co Ltd* [1991] BVC 568 stated that:

> "The task of this Tribunal combines the tasks of judge and jury: we must decide whether there is a reasonable excuse for the failure. We agree with Judge Medd and Judge Brannan that the correct way of doing this is to ask:
>
> Was what the taxpayer did a reasonable thing for a responsible trader conscious of and intending to comply with his obligations regarding tax, but having the experience and other relevant attributes of the taxpayer and placed in the situation that the taxpayer found himself at the relevant time, a reasonable thing to do?
>
> It is on that basis that we approach this case. When we refer to the reasonable taxpayer we are using that phrase as shorthand for a responsible person with the same experience and other relevant attributes of the taxpayer and placed in the same situation as the taxpayer."

35. The appellant has stated that the loss of tax to HMRC was minimal. This does not constitute a reasonable excuse for the failure to file tax returns.

36. The appellant submits that all outstanding amounts have been paid to HMRC. Whilst this is true, it is Parliament's intention that the legislation at Schedule 41 FA 2008 discourages and therefore penalises failures to notify chargeability to HMRC. Parliament's intention is clear through the legislated penalty position, that no relief is to be given for subsequent payment of outstanding sums once, for the purposes of Schedule 41 FA 2008 'failure to notify' penalties, the outstanding amounts become PLR.

37. The effectiveness of the legislation would be negated should penalties be withdrawn when liability is subsequently paid. HMRC therefore have to enforce the legislation strictly in order to facilitate Parliament's intentions.

Whether penalties inequitable

38. The penalties have been imposed in accordance with the conditions laid out in statute.

39. The First-tier Tribunal has no jurisdiction to consider a penalty is unfair. The Upper Tribunal in *Hok* 12012] UKUT 363 (TCC) gives guidance on the use of unfairness as a ground of appeal at para 36:

36 "It is important to bear in mind how the First-tier Tribunal came into being. It was created by s 3(1) of the Tribunals, Courts and Enforcement Act 2007, "for the purpose of exercising the functions conferred on it under or by virtue of this Act or any other Act". It follows that its jurisdiction is derived wholly from statute. As Mr Vallat correctly submitted, the statutory provision relevant here, namely TMA s 1008, permits the tribunal to set aside a penalty which has not in fact been incurred, or to correct a penalty which has been incurred but has been imposed in an incorrect amount, but it goes no further. In particular, neither that provision nor any other gives the tribunal a discretion to adjust a penalty of the kind imposed in this case, because of a perception that it is unfair or for any similar reason. Pausing there, it is plain that the First-tier Tribunal has no statutory power to discharge, or adjust, a penalty because of a perception that it is unfair.

In charging the penalty HMRC have given full and proper regard to the reductions that the statute permits."

Suspension

40. There is no provision for suspension of a penalty under Schedule 41.

41. For the above reasons, we must dismiss the appeal and confirm the penalties under appeal of £5,315.30.

42. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

MICHAEL CONNELL
TRIBUNAL JUDGE

RELEASE DATE: 09 JANUARY 2019