[2013] UKFTT 306 (TC)

TC02711

Appeal number: TC/2012/09698

INCOME TAX – HMRC enquiry into 2010 SA return – unrepresented taxpayer – HMRC seeking to amend returns for the previous two years – HMRC issuing a protective assessment for 2007-08 – taxpayer failing to pay by surcharge trigger date – whether conditions for discovery assessment met – whether tax was due so as to trigger a surcharge for late payment – Tribunal's jurisdiction considered – whether Tribunal can set aside surcharge if no underlying tax – held, no – whether Tribunal has jurisdiction to consider reasonable excuse – yes – whether taxpayer has reasonable excuse – yes – appeal allowed and surcharge set aside

FIRST-TIER TRIBUNAL
TAX CHAMBER

ADRIAN SALMON **Appellant**

- and -

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

TRIBUNAL: ANNE REDSTON (TRIBUNAL PRESIDING MEMBER)

The Tribunal determined the appeal on 11 March 2013 without a hearing under the provisions of Rule 26 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (default paper cases) having first read the Notice of Appeal dated 22 October 2012 (with enclosures), HMRC's Statement of Case submitted on 6 December 2012 (with enclosures) and the Appellant's Reply dated 4 January 2013.

DECISION

1. This was Adrian Salmon's appeal against a surcharge of £147.05 for late payment of self-assessment ("SA") tax for the 2007-08 fiscal year. The tax was assessed by way of a "protective assessment".

2. This is a long decision, and the key points are summarised here for Mr Salmon's benefit.

(1) There can only be a surcharge if there is tax to pay in the first place. HMRC opened an enquiry into Mr Salmon's 2009-10 return, and then issued an assessment to collect further tax for 2007-08.

(2) The law only allows HMRC to collect tax for earlier years if certain conditions are met. On the facts provided, it appears that these conditions may not have been met. This would mean that HMRC could not collect extra tax for 2007-08 and so should not have levied a surcharge.

(3) The Tribunal has limited powers. In particular, it does not have the power to strike out a surcharge on the basis that it should not have been levied. It can only cancel a surcharge if the taxpayer had a "reasonable excuse" for not paying the tax.

(4) The Tribunal decided that Mr Salmon did have a reasonable excuse, and set aside the surcharge.

(5) The Tribunal cannot consider whether or not HMRC should have collected extra tax from Mr Salmon for 2007-08 and/or 2008-09. This is a matter on which he may want to take advice, or which HMRC may choose to review.

The law

3. The statutory provisions relating to the imposition of surcharges are at Taxes Management Act 1970 ("TMA") s 59C. So far as relevant to this Appeal, they are as follows:

> **Surcharges on unpaid income tax and capital gains tax**
>
> (1) This section applies in relation to any income tax or capital gains tax which has become payable by a person (the taxpayer) in accordance with section 55 or 59B of this Act.
>
> (2) Where any of the tax remains unpaid on the day following the expiry of 28 days from the due date, the taxpayer shall be liable to a surcharge equal to 5 per cent of the unpaid tax.
>
> (3)-(5) …

(6) A surcharge imposed under subsection (2) above shall carry interest at the rate applicable under section 178 of the Finance Act 1989 from the end of the period of 30 days beginning with the day on which the surcharge is imposed until payment.

(7) An appeal may be brought against the imposition of a surcharge under subsection (2) above within the period of 30 days beginning with the date on which the surcharge is imposed.

(8) Subject to subsection (9) below, the provisions of this Act relating to appeals shall have effect in relation to an appeal under subsection (7) above as they have effect in relation to an appeal against an assessment to tax.

(9) On an appeal under subsection (7) above that is notified to the tribunal section 50(6) to (8) of this Act shall not apply but the tribunal may—

(a) if it appears that, throughout the period of default, the taxpayer had a reasonable excuse for not paying the tax, set aside the imposition of the surcharge; or

(b) if it does not so appear, confirm the imposition of the surcharge.

(10) Inability to pay the tax shall not be regarded as a reasonable excuse for the purposes of subsection (9) above...

4. It is clear from TMA s 59C(1) that a surcharge can only be imposed if there is "income tax or capital gains tax which has become payable by a person (the taxpayer) in accordance with section 55 or 59B of this Act."

5. Section 55 deals with cases where the assessment itself has been appealed to the Tribunal. TMA s 59B(6) reads:

"Any amount of income tax or capital gains tax which is payable by virtue of an assessment made otherwise than under section 9 of this Act shall, unless otherwise provided, be payable on the day following the end of the period of 30 days beginning with the day on which the notice of assessment is given."

6. TMA s 29 allows an assessment to be made "where loss of tax is discovered":

Assessment where loss of tax discovered

(1) If an officer of the Board or the Board discover, as regards any person (the taxpayer) and a year of assessment—

(a) that any income which ought to have been assessed to income tax, or chargeable gains which ought to have been assessed to capital gains tax, have not been assessed, or

(b) that an assessment to tax is or has become insufficient, or

(c) that any relief which has been given is or has become excessive,

the officer or, as the case may be, the Board may, subject to subsections (2) and (3) below, make an assessment in the amount, or the further amount,

which ought in his or their opinion to be charged in order to make good to the Crown the loss of tax.

(2) Where—

(a) the taxpayer has made and delivered a return under section 8 or 8A of this Act in respect of the relevant year of assessment, and

(b) the situation mentioned in subsection (1) above is attributable to an error or mistake in the return as to the basis on which his liability ought to have been computed,

the taxpayer shall not be assessed under that subsection in respect of the year of assessment there mentioned if the return was in fact made on the basis or in accordance with the practice generally prevailing at the time when it was made.

(3) Where the taxpayer has made and delivered a return under section 8 or 8A of this Act in respect of the relevant year of assessment, he shall not be assessed under subsection (1) above—

(a) in respect of the year of assessment mentioned in that subsection; and

(b) in the same capacity as that in which he made and delivered the return,

unless one of the two conditions mentioned below is fulfilled.

(4) The first condition is that the situation mentioned in subsection (1) above was brought about carelessly or deliberately by the taxpayer or a person acting on his behalf.

(5) The second condition is that at the time when an officer of the Board—

(a) ceased to be entitled to give notice of his intention to enquire into the taxpayer's return under section 8 or 8A of this Act in respect of the relevant year of assessment; or

(b) informed the taxpayer that he had completed his enquiries into that return,

the officer could not have been reasonably expected, on the basis of the information made available to him before that time, to be aware of the situation mentioned in subsection (1) above.

(6)-(9) ….

The evidence

7. The Tribunal was provided with the correspondence between the parties, and between the parties and the Tribunals Service. In addition, Mr Salmon supplied copies of his SA Statements of Account dated 23 April 2012 (Statement Number 21) and 21 May 2012 (Statement Number 22).

8. HMRC supplied:

(1) a copy of Mr Salmon's SA record showing the date he entered SA;

(2) a copy of his tax calculation notice for the 2007-08 tax year as originally submitted;

(3) copies of Mr Salmon's SA return for 2007-08 as submitted, and a further version, headed "based on revised figures";

(4) a "Notice of further assessment for the year ended 5 April 2008" dated 8 March 2012;

(5) a note of telephone conversation dated 29 October 2012 between Mr Salmon and HMRC;

(6) Mr Salmon's SA account dated 27 November 2012.

Facts

9. From that evidence, I find the following facts.

10. Mr Salmon runs a business called Bishop's Yacht Chartering and Skippering. He owns a boat which he lets out on charter; he sometimes acts as skipper. He has always dealt with his own tax affairs and never used an accountant.

11. On 4 January 2012, HMRC opened an enquiry into his SA tax return for the 2009-10 tax year. On 28 February 2012 Mrs Solari of HMRC met with Mr Salmon at his premises.

12. On 8 March Mrs Solari wrote to Mr Salmon. The letter opens as follows:

> "Thank you for meeting with me on 28 February to discuss the compliance check into your self-assessment tax return for the year to 5 April 2010."

13. The next paragraphs concern the notes of meeting, capital allowances and expense adjustments for 2009-10. Mrs Solari then says:

> "The normal time limit for issuing assessments where errors have been identified is 4 years from the end of the relevant tax year. This means that any assessment for the year ended 5 April 2008 must be issued by 5 April 2012. Although there is still one unresolved point and my amendments have not yet been agreed by you, I am today issuing the attached assessment for the year ended 5 April 2008 to protect HMRC's position and ensure that the potential tax due is not lost. The assessments and amendments for years ended 5 April 2009, 2010 and 2011 will be made once all matters are agreed."

14. Mrs Solari then says she does not intend to go back to the years before 5 April 2008, and also explains that the amendments relate to losses which have now been disallowed. The letter ends as follows:

> "I can confirm that I do not intend to seek any penalties for the offence of submitting incorrect tax returns. I accept that the errors were made despite taking reasonable care, and, as discussed when we met, that the treatment of the losses is a complex technical issue.

> Please let me have the evidence from the charter manager and your agreement to my computations, or comments as appropriate, as soon as possible."

15. Attached to the letter were six documents, namely notes of the meeting, revised capital allowances computations, 17 pages of other notes, a schedule of adjusted trading results, a tax calculation and a "Notice of further assessment for the year ended 5 April 2008."[1]

16. The Notice of further assessment charged tax of £3,493.04, and begins:

> "I am sending this assessment to you because we have found that there is additional tax due that was not previously shown on your tax return. It is now too late for us to amend your tax return so this assessment allows us to collect the additional tax."

17. Under the heading "Paying what is due" it says:

> "Please make sure that you pay the amount shown at the top of this assessment by 7 April 2007. If you do not pay all the tax that is due within 28 days of the date it should be paid, we will add a surcharge…the surcharge will be an amount equal to 5% of the amount of tax that you have not paid."

18. On 20 March 2012 Mr Salmon wrote to Mrs Solari, attaching an email from the charter manager and saying "I am trying to get some advice on this matter, and so I will respond more fully to your letter in due course."

19. On 23 April 2012, HMRC issued an SA statement of account (Number 21), showing an amount due of £3,824.57, being £3,493.04 plus interest of £331.53.

20. On 9 May 2012 Mr Solari moved some funds into his bank account.

21. On or around 21 May 2012, HMRC issued a 5% surcharge of £174.65, being 5% of the tax unpaid at 6 May 2012. On the same day, HMRC issued an updated statement of account (Number 22), showing the surcharge.

22. On 1 June 2012 Mr Salmon paid the extra tax assessed for 2007-08. On 12 June 2012 he appealed the surcharge.

23. On 29 October 2012, Mr Salmon called HMRC to discuss the 2008-09 and 2009-10 position, and in particular "what needed to be paid and by what dates." The note of call says:

> "he pointed out that he had been charged a surcharge on the 07-08 amendment – he had waited for SofA and payslip to pay and so paid late. I said that the notice of assessment stated the payment date and explained the surcharges. He said there were pages of letters to plough

[1] Of these, only the Notice of further assessment was provided to the Tribunal by the parties

> through and he could not be expected to read and understand each small bit."

Mr Salmon's submissions

24. Mr Salmon says that he is "an individual taxpayer trying to operate the self-assessment system to the best of my ability."

> "I have been paying income and capital gains tax for decades, without using an accountant, and never once had a problem until now. The problem was initiated by a demand for back tax, as a result of a particular interpretation of the rules governing business losses being set off against other income. All relevant facts were declared by myself at the time, and this has never been disputed by HMRC. It was HMRC who decided to apply this interpretation, on account of it being backed up by case law."

25. He says that the information relating to the surcharges was "hidden". Although he accepts that it was included in the papers sent with Mrs Solari's letter of 28 April 2012, he points out that there were 31 pages of attachments to that letter, saying: "HMRC Collector…merely relied on a notice issued on page 12 within a 31 page raft of paperwork." Furthermore he says that Statement Number 21 did not include any due date on its face, while surcharges are only explained on the reverse of the Statement, and HMRC never highlighted "this vital information."

26. He says "the key question in this case is what is reasonable" and concludes:

> "There has been much in the news recently about aggressive tax avoidance; measures taken by individuals purely to legally reduce their taxes to the absolute minimum. I would suggest that this is a clear example of aggressive tax collection, and should equally be discouraged."

HMRC's submissions

27. HMRC rebut Mr Salmon's suggestion that the information about the surcharges was "hidden"; they say it was clearly stated on the Notice of further assessment which was sent out on 8 March 2012. They also say that in any event, the charging of a surcharge:

> "is not dependent on the notification or otherwise on any such statement of account. Mr Salmon incurred the surcharge due to his failure to correctly attend to his payment obligations."

28. HMRC also rely on the phone conversation between Mr Salmon and HMRC which took place on 29 October 2012. They say that this shows that Mr Salmon "failed to take reasonable and proper care to ensure he fulfilled his obligations under the self-assessment tax regime."

29. Finally, they say he has no reasonable excuse and the surcharge is properly due.

Whether HMRC could assess 2007-08

30. Mr Salmon is appealing against a surcharge. TMA s 59C(1) specifies that no surcharge can be levied unless there an unpaid liability to tax.

31. On 4 January 2012, HMRC opened an enquiry into Mr Salmon's 2009-10 SA tax return. It was thus within what is known as the "enquiry window" – the period after a return has been submitted during which HMRC are allowed by law to make an enquiry.

32. Mrs Solari then re-opened the two earlier years, 2007-08 and 2008-09. HMRC are only allowed to do this if the tests in TMA s 29 are met. These provisions are set out at the beginning of this decision. In brief, HMRC is only permitted to open up earlier years if (a) they make a "discovery" that some tax has not been assessed, and (b) one of two other conditions are satisfied.

33. The threshold for a "discovery" is low – for instance, HMRC can simply change their mind on the matter in question, see *R&C Commrs v Charlton* [2012] UKFTT 770(TC) at [44]. On the facts of this case, Mrs Solari made a "discovery" relating to the losses shown on Mr Salmon's earlier returns.

34. The first of the two statutory conditions is that the insufficiency was caused by the taxpayer acting "carelessly or deliberately" (TMA s 29(4)). That condition does not apply in this case, as Mrs Solari has said that Mr Salmon made the errors "despite taking reasonable care".

35. The second, alternative, condition is that the inspector "could not reasonably have been expected, from the information made available to him, before that time, to be aware of [the insufficiency]" (TMA s 29(5)). There is extensive case law on the meaning of this provision, and in particular about the information a taxpayer needs to provide in order to prevent HMRC being able to open up earlier years under this subsection.

36. This Tribunal was not provided with any information about what consideration Mrs Solari gave to whether or not the test under TMA s 29(5) was satisfied. However, Mr Salmon says "all relevant facts were declared by myself at the time, and this has never been disputed by HMRC."

37. If this is, in fact, the position, then HMRC are unable to make an additional assessment for 2007-08, because the condition at TMA s 29(5) has not been met. As Moses LJ said in *Tower MCashback LLP v R&C Commrs* [2010] STC 809 at [24]:

> "There are statutory limitations as to the time at which the sufficiency or otherwise of the information must be judged. These provisions underline the finality of the self-assessment, a finality which is underlined by strict statutory control of the circumstances in which the

> Revenue may impose additional tax liabilities by way of amendment to the taxpayer's return and assessment."

38. In *Hankinson v R&C Commrs* [2010] UKUT 361, STC 2640, a case which also involved a "protective assessment", the Upper Tribunal (with whom the Court of Appeal agreed) said at [24] that:

> "The purpose of the new s 29 is to protect the taxpayer who has made an honest, complete and timely return from a late assessment."

39. This is echoed in the recent case of *R&C Commrs v Charlton* [2012] UKFTT 770(TC) at [56], where the Upper Tribunal said:

> "The ability of HMRC to make a discovery assessment is balanced by the protection afforded to a taxpayer who, before the enquiry window closes, makes an honest and complete return."

If the assessment was invalid

40. If the assessment were invalid as a matter of law, because the requirements of TMA s 29 were not met, this would mean that there was no 2007-08 underpayment. The next question is whether the Tribunal has the jurisdiction to allow the appeal on the basis that if there is no underpayment, there can be no surcharge.

41. The question of the Tribunal's jurisdiction to allow an appeal on the basis that there was, in fact, no liability to tax, was recently explored in the case of *O'Kane v R&C Commrs* at [55]-[77]. In that case I decided that the Tribunal did not have the jurisdiction, because its power to allow the appeal is limited by statute to cases where the taxpayer has a reasonable excuse for not paying the surcharge.

42. For the same reasons as in *O'Kane*, it is not possible for this Tribunal to allow Mr Salmon's appeal on the basis that there was no underlying tax liability. If the Tribunal had that jurisdiction, it might have been necessary to direct an oral hearing and/or the provision of further evidence.

The nature of a "protective assessment"

43. In Mrs Solari's letter of 8 March 2012, she says she is raising the assessment "to protect HMRC's position and ensure that the potential tax due is not lost." This is commonly termed a "protective assessment".

44. I have considered whether any special statutory provisions apply to a "protective assessment".

45. At the Upper Tribunal in *Hankinson*, Counsel for the taxpayer argued that the scheme of self-assessment "rendered it impossible for HMRC officers to make speculative, or protective, assessments." HMRC's counsel countered by saying that a

protective assessment was "not a term of art" and the only relevant provisions were those in TMA s 29.

46. The Upper Tribunal (Warren LJ and Judge Bishopp) did not explicitly address this point, but their decision can only be understood on the basis that they accepted HMRC's case. In other words, they held that the normal discovery provisions apply to "protective" assessments in the same way as they do to any other further assessment.

47. In the VAT context, Parker LJ came to the same conclusion in *Courts v R&C Commrs* [2004] EWCA Civ 1527 at [102]:

> "a 'protective' assessment, in the sense of an assessment which is made in order to protect the commissioners' position in the event of a subsequent appeal being decided in their favour…, is nonetheless an assessment. As such it will, when notified, create a debt (see s 73(9)). The fact that no steps will be taken to recover the debt so created pending the occurrence of a future contingency cannot, in my judgment, affect the fact that an assessment has been made."

48. From this it follows that, if the assessment was properly made under s 29, then the statute provides no special rules and the normal time limits for payment apply, unless HMRC take steps to suspend collection.

The jurisdiction of the Tribunal to consider reasonable excuse

49. Under TMA s 59C(9)(a) the Tribunal has an explicit statutory jurisdiction to consider whether a person has "a reasonable excuse for the default."

50. In *O'Kane* at [80] to [89] I considered whether the Tribunal can exercise this jurisdiction where there is no underlying tax (ie because the assessment on which the surcharge is based is itself invalid). For the reasons set out in that decision, I concluded that it can.

Whether Mr Salmon has a reasonable excuse

51. There is no definition in the legislation of a "reasonable excuse". It has been held to be "a matter to be considered in the light of all the circumstances of the particular case" (*Rowland v HMRC* [2006] STC (SCD) 536 at [18]). The starting point is therefore the facts of the case.

The enquiry was not resolved

52. When Mrs Solari raised the protective assessment, the enquiry was still not resolved. There were open issues. The tax assessed was described by Mrs Solari as "the potential tax due".

53. Mr Salmon also understood that the issues involved in the assessment remained open: in his reply of 20 March 2012 he says "I am trying to get some advice on this matter, and so I will respond more fully to your letter in due course."

54. I note also the reference in *Courts* to HMRC standing over the tax: the judge says, in relation to that protective assessment, that "no steps will be taken to recover the debt so created pending the occurrence of a future contingency." No similar action was taken by Mrs Solari.

55. Had Mr Salmon received professional assistance at this point, he would probably have been advised to appeal the protective assessment and seek postponement of the tax due. But he is unrepresented: he describes himself as "an individual taxpayer trying to operate the self-assessment system to the best of my ability." He had no adviser to suggest that an appeal and postponement might have been a sensible course of action, and HMRC did not provide that assistance.

Awareness of the due date

56. HMRC draw attention to the fact that, among the many papers sent to Mr Salmon on 8 March 2012, the Notice of further assessment which gave a payment date and a warning about surcharges, and that there was a further warning on the reverse of the 21 April statement of account. They say Mr Salmon should have been aware of the due date for payment, and also that there would be a surcharge if the tax was not paid by the surcharge trigger date.

57. It is clear from Mr Salmon's submissions to the Tribunal that he did not see these warnings. It was not until the actual surcharge notice was issued, on 21 May 2012, that he understood HMRC were penalising him for not paying the tax levied by the further assessment.

58. It is for the Tribunal to decide if, in all the circumstances of this case, he had a reasonable excuse for his failure to pay by the surcharge trigger date.

59. I find that both Mr Salmon and Mrs Solari understood that the 2007-08 tax position was still unresolved. Discussions were continuing and Mr Salmon was seeking advice. He received many pages of information which he did his best to digest, and failed to realise that, among those pages, was a requirement to pay what he understood to be a provisional figure, by a fixed date, and that failure to pay by that date would trigger a surcharge.

60. In all the circumstances of this case, I find that he has a reasonable excuse for not paying the tax by the surcharge trigger date. In consequence, I allow his appeal and set aside the penalty.

61. As to whether there is, in fact, a liability to tax for 2007-08 and/or 2008-09 is not a question this Tribunal can decide. It will be for Mr Salmon to consider whether or not he should take professional advice, and for HMRC to reflect on whether any points merit reconsideration.

Appeal rights

62. 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.

63. 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.

ANNE REDSTON
TRIBUNAL PRESIDING MEMBER

RELEASE DATE: 17 May 2013