TC02692

Appeal number: TC/2011/05689 & TC/2011/10197

INCOME TAX – surcharge for failure to pay tax on time – reasonable excuse - application for time to pay agreement – application not finally dealt with by HMRC – whether taxpayers' reliance on expectation that HMRC would determine application gave them a reasonable excuse for late payment – yes – appeals allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

GEORGE KOFTEROS **Appellant**
LESLEY KOFTEROS

- and -

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

TRIBUNAL: SIR STEPHEN OLIVER QC

Sitting in public in London on 3 April 2013

C Moody, tax consultant, for the Appellant

Thomas Ellis, Inspector of Taxes (High Net Worth Unit, for the Respondents

DECISION

1. Mr George Kofteros ("Mr Kofteros") appeals against two self-assessment late payment surcharge notices of £25,166.39 and £25,166.39 which were issued on 1 April 2011 and 17 August 2011 respectively in relation to tax unpaid on the 2009-10 tax liability.

2. The first surcharge imposed on Mr Kofteros arises as a consequence of £503,327.85 being unpaid 28 days from the due date for payment. The second surcharge arises as a consequence of tax of the same amount being unpaid six months after the due date for payment.

3. Mrs Lesley Kofteros ("Mrs Kofteros") similarly appeals against two self-assessment late payment surcharge notices, each of £2,083.22, issued on the same dates and in the same circumstances as applied to Mr Kofteros.

Points at Issue

4. The first issue is whether and to what extent liabilities to the penalties are displaced by "time to pay" agreements.

5. The second issue arises on the basis that the tax was paid in June 2012. The question is whether, in the circumstances, there was a reasonable excuse for the failures to pay the tax on the due date.

Joint Hearing of Appeals

6. HMRC accept, in paragraph 3 of the Statement of Case, that "the same arguments, statute, principles etc. apply to both Appellants". In this connection it is relevant to mention that Mr Kofteros's appeal against the first of the surcharges was originally categorised as "basic"; it was, therefore, determined without a hearing. The First-tier Tribunal found as a fact that there had been a time to pay agreement that had subsisted until 30 September 2011 but had had insufficient evidence to determine whether the tax had been paid during the "deferral period" (see section 108(1) of Finance Act 2009). The Upper Tribunal sent the matter back for a further hearing before a differently constituted tribunal and a subsequent direction joined the hearings of the two Appellants.

Evidence

7. HMRC called Mrs Sally Burke, a Higher Officer Casework Manager in HMRC's Enforcement and Insolvency Service which is part of HMRC's Debt Management and Business "business unit" that was responsible for collection of Mr Kofteros's tax arrears.

8. Neither of the Appellants chose to give evidence. So far as their cases are concerned, I have drawn the facts from the "facts and matters relied on" by HMRC in

their Statement of Case and from matters referred to in correspondence put in evidence as well as from the evidence of Mrs Burke.

Findings of Fact

9. At the time when the tax became payable (31 January 2011), Mr Kofteros was a 5% shareholder in a company called Trueform Engineering Limited ("Trueform"). According to a letter to the Tribunal from Mr Kofteros's accountants dated 9 April 2013, *"the remaining shares were held by trustees on behalf of our client"*. Trueform's business consisted of the design and manufacture of "street furniture". The rest of the Trueform shares had been transferred by Mr Kofteros to trustees in 2007/08. The transfer had caused a disposal and a charge to capital gains tax on Mr Kofteros. The tax on that gain, due on 31 January 2009, had been the subject of a time to pay agreement pursuant to arrangements made by Mr C Moody of the accountants acting for Mr Kofteros ("the accountants") and HMRC Reading.

10. Mr Kofteros had had a "loan account" with Trueform through which he had borrowed to fund payments to a company called Purple City Limited. Mr Kofteros's total lending to Purple City had amounted to £1,670,673.

11. HMRC's Statement of Case records that Mr Kofteros's self-assessment tax return for 2009/10 contained the following entry – *"Net amount of dividend income taxed at dividend rate £1,620,000"*. The Statement of Case goes on to state that *"the payment of that dividend in March 2010 to Mr Kofteros, and other income, resulted in a charge under self-assessment of £504,523.45"*. Mrs Kofteros's return for the same period contains the entry – *"… gross dividend from UK companies £199,999"*. Nothing is said about the source of her dividend or the manner in which it came to her. The Statement of Case, however, states that *"the payment of that dividend … resulted in a charge …of £41,669 which was due to be paid by 31 January 2011"*.

12. The Statement of Case refers to an explanation given by the accountants in a letter of April 2010 that Mr Kofteros had - "borrowed from his loan account with Trueform … to fund payments to Purple City Ltd. [His] total lending to Purple City Ltd amounted to £1,670,673 and it is claimed that Mr Kofteros was unable to recover any of that amount. [His] borrowing from Trueform resulted in his loan account (also described as his current account) with that company being overdrawn".

13. In a letter of 21 July 2011 to the Tribunal, the accountants, through Mr Moody, explained that – "A dividend was declared in March 2010 from Trueform … which was due to our client as beneficial owner of 90% of the shares of the company. Our client received no cash as the payment was used to extinguish his overdrawn current account with the company". (That throws no light on the source or application by Mrs Kofteros of her dividend.)

14. On 27 January 2011, Mr C Moody of the accountants wrote to HMRC in Reading (Berkshire Recovery). The letter referred to the earlier time to pay agreement (made with Reading - see paragraph 9 above) and explained that the purpose of his writing was *"to apply for a TTP mainly for the 2009/10 liability"*. The letter

concluded with the words – "W*e would like to apply for TTP to cover the net liability of £540,000 by spreading this over 36 months … with monthly payments of £15,000"*.

15. HMRC Reading responded by letter of 21 February requiring more information in order to consider the time to pay application. Mr Moody of the accountants (who had also been in touch with HMRC Shipley in that connection on 15 February) wrote back on 10 March providing Reading with statements of Mr Kofteros's assets and liabilities and of monthly income and expenditure.

16. On 10 March, the accountants provided Reading with a statement of Mr Kofteros' assets and liabilities. The "known" value of "properties" was shown as £2.5 million. The value of his "businesses", which included his 5% shareholding in Trueform, was recorded as "unknown". Liabilities came to £3,743,000. Of that amount, he is recorded as owing £1,758,000 to "Turin Film Partnership"; the balance relates mainly to mortgage debts.

17. The Reading office referred the "time to pay"application letter of 27 January 2011 to Debt Management Croydon. On 21 February 2011 Debt Management Croydon wrote to the accountants requesting details of Mr Kofteros's financial position urgently saying – "*If you chose (*sic*) not to comply with our request you will leave us with little option other than to consider distraint action"*.

18. On 23 March 2011, Debt Management Croydon and Mr Moody of the accountants had two telephone conversations following which Debt Management Croydon wrote saying – "*Unfortunately, from the information provided, I am unable to agree to your payment proposal. However, an extensive revised proposal may be considered. As discussed I will continue with Distraint action against your client. … If you feel I should not proceed then please do not hesitate to contact me."*

19. The accountants (through Mr Moody) replied to Debt Management Croydon on 5 April providing further information. The letter makes the point that – "*Most important is the fact that there are advanced negotiations for a sale of all of the shares in Trueform. This is strictly confidential information. Once the sale takes place then the tax liability will be settled in full."* The letter went on to revise the application for time to pay from £15,000 a month to £25,000 a month and stated that the sale was expected to have been completed "*in six months time"*.

20. A late payment surcharge notice was issued by the East Kilbride High Net Worth Unit on 7 April 2011. The surcharge was for £25,166.39. This was appealed on 19 April on the basis that there was a reasonable excuse for the late payment; this being that "*we are negotiating time to pay arrangements … with Ms Gordon of Debt Management Office Croydon"*. This appeal became the subject of the "basic" category appeal proceedings referred to in paragraph 6 above.

21. The accountants learned that their letter of 5 April (to Debt Management Croydon) had been passed to Debt Management Enforcement and Insolvency Unit in Worthing ("the Worthing Unit"). Mr Moody called the Worthing Unit and, on 6 May 2011, received a letter stating, among other things, that the offer in the 5 April letter

(putting forward the revised time to pay proposal) was *"not acceptable"*. The Worthing Unit letter announced that Mr Kofteros's case had been transferred to Worthing *"to commence bankruptcy action against him"*.

22. A letter from the East Kilbride High Net Worth Unit of 16 May informed Mr Kofteros that HMRC did not think he had a reasonable excuse *"because a Time to Pay arrangement is not in place"*. The accountants then wrote to East Kilbride High Net Worth Unit requesting a review of the decision to impose a surcharge. They explained how the matter had travelled from HMRC's offices at Reading to Croydon to Worthing and, in the case of Mrs Kofteros, to Edinburgh. The letter drew the attention of the East Kilbride High Net Worth Unit to an HMRC manual that stated in relation to time to pay proposals, among other things, that – "*where the arrangements cannot be agreed then provided that any information requested is supplied within a reasonable time scale then the surcharge should be stood over"*.

23. The accountants (in a letter from Mr Moody of 3 June) took up the Worthing Unit's rejection (in The Worthing Unit's letter of 6 May) of Mr Kofteros's revised time to pay proposal. (Apparently Debt Management Somerset had issued a statutory demand under section 268(1)(a) of the Insolvency Act 1986 and tried to serve it on Mr Kofteros on 2 June.) Referring to Worthing's rejection of the proposed revised timescale for the time to pay arrangement, the accountants asked the Worthing Unit to *"reconsider your proposed course of action as there has now been an offer to acquire all the shares in Trueform Engineering which would mean that the tax liability would be cleared in full once the sale goes through. The offer envisages completion in 8 to 10 weeks, so by mid August 2011"*. The letter concludes with these words – *"Our proposed TTP would therefore be four further payments of £25,000 …"*.

24. Worthing spoke to the accountants on 8 June asking for evidence that the offer to purchase Trueform had been made. On 15 June the accountants sent the draft heads of agreement to Worthing and wrote – "*I trust you will now reconsider our revised time to pay arrangement"*.

25. Eight days later, on 23 June 2011, a telephone conversation took place between Mr Moody of the accountants and the Worthing Unit. The same day Mrs S Burke of the Worthing Unit wrote to the accountants as follows – *"As discussed, I confirm that now your client has been served with a Statutory Demand, I am prepared to defer further action until 30 September 2011 as requested. … Whilst your client's proposal that he pays £25,000 per month in the meantime is not acceptable, ether on a formal or an informal basis, I confirm that any part payments that he wishes to send will be accepted generally on account of his debt"*.

26. Within four days of receiving Mrs Burke's letter, the accountants (through Mr Moody) were writing to HMRC in Cardiff (in a fax addressed to a Mr C de Benedictis dated 27 June). Referring to Mrs Burke's letter, the accountants say that the letter *"…confirms that our client now has until the end of September 2011 to pay the 2009/10 liability"*. The fax was followed, on 4 July 2011 by a letter from Cardiff to Mr Moody of the accountants. The letter came from the Charity Assets & Residence High Net Worth Unit and it announced that the decision of the East

Kilbride High Net Worth Unit (rejecting Mr Kofteros's reasonable excuse defence to the surcharge) was upheld on review. The review letter stated that – "… *formal agreement of a time to pay arrangement is essential in order for a 'reasonable excuse' argument to succeed. In your client's case no arrangement has ever been agreed with an officer of Revenue and Customs"*.

27. Apparently the arrangements for the sale of Trueform were delayed in September. On 26 September 2011, Mr Moody writes to Mrs Burke of the Worthing Unit to explain that the acquiring company's funding facilities were being held up by its bank. The next day, Mrs Burke writes to inform Mr Moody that *"… the original statutory demand is technically invalid…and … no petition will be filed before 11 November 2011 to enable payment to be made"*. (East Kilbride High Net Worth Unit were in touch again with the accountants on 18 October 2011.)

28. On 7 November 2011 Mr Moody writes to Mrs Burke saying that an update on progress will be provided "next week". Referring to a telephone conversation about of the previous week, Mr Moody's letter says – *" … you agreed to give our clients until 30 November before taking this further."*

29. A telephone conversation between Mr Moody of the accountants and Mrs Burke of the Worthing Unit took place on 30 November. A letter of 20 December 2011 followed in which Mr Moody records Mrs Burke's agreement to *"give our client a further four weeks to settle the tax debt in view of the particular circumstances"*. These were the sudden death of the chairman of the purchasing company, GIL Investments, with the result that all transactions involving GIL Investments were "put on hold". The letter explains that three possible new offers had been made and that he would be in touch with an update as soon as possible.

30. According to Mrs Burke's evidence, nothing further was heard by the Worthing Unit until March 2012. (The Statement of Case records that East Kilbride High Net Worth Unit, through Mr Thomas Ellis, was in touch on 17 January.)

31. On 5 April 2012, the Worthing Unit wrote to Mr Kofteros informing him that he would shortly be served with a Statutory Demand and that, in the absence of payment in full within 21 days, the bankruptcy petition would be filed.

32. On 25 June 2012 the sum of £503,480 was paid to HMRC. I understand that this came out of the proceeds of sale of the entire share capital of Trueform.

33. From the oral evidence of Mrs S Burke I am satisfied that the Worthing Unit had at no time been concerned with the time to pay application, so far as that related to the workings of section 108 of Finance Act 2009. "Time to Pay", in the context of the responsibilities of the Worthing Unit, related to the statutory requirements of section 268 of the Insolvency Act 1986. That explains, for example, The Worthing Unit's response, on 23 June 2011, to Mr Moody's request (of 15 June) for reconsideration of the revised application for time to pay. Nothing said or written by the Worthing Unit should, as the Worthing Unit understood its role, be construed as having to do with section 108.

Section 108 of FA 2009

34. A taxpayer in the position of Mr Kofteros is not liable to a late payment penalty if he has failed to pay his tax by 31 January but has made a request to an officer of HMRC for payment to be deferred and an officer "agrees that payment of that amount may be deferred for a period ('the deferral period')". See section 108(1) and (2). But (by subsection (3)), if the taxpayer breaks the agreement by failing to pay the amount by the end of the deferral period and a notice has been served on him specifying the penalty, he becomes liable (at the date of that notice) to the specified penalty. Subsection (6) deals with the situation where an agreement has been varied and directs that section 108 applies to the agreement as varied.

35. Was there ever a section 108 agreement?

36. The judge who decided the matter on the papers (i.e. Mr Kofteros's liability to the first surcharge) had not had the benefit of Mrs Burke's oral evidence. He decided (in paragraph 23 of the decision released on 16 April 2012) that he was "*left in no doubt on the true and proper construction of* the *events that have happened as set out in the correspondence to which I have referred, at time to pay negotiation culminated in Mrs burke agreeing that the appellant had until 30 September to pay in full, bearing in mind the on account payments of £25,000 that he had* made*."* The Statement of Case (provided by East Kilbride High Net Worth Unit on 18 January 2013) states that – "*HMRC accepts the decision of [the judge] which said that HMRC had given Mr Kofteros time to pay the tax and that the time was until 30 September 2011. … Using the principles in the decision by [the judge], HMRC accepts that there was a further time to pay agreement to a later date of 11 November".*

37. Whether there had been a time to pay agreement providing for a deferral period to either 30 September or 11 November 2011 becomes academic in the light of the fact that the tax was not paid until June 2012. There is no evidence of any agreement that varied an original agreement and created a deferral period extending to June 2012.

Reasonable Excuse within TMA section 59C(9)

38. Section 59C(9) enables the tribunal to set aside the imposition of the surcharge if it appears that "throughout the period of default, the taxpayer had a reasonable excuse for not paying the tax". Section 59C(10) states that "inability to pay the tax shall not be regarded as a reasonable excuse…".

39. The reasonable excuse relied upon by Mr Kofteros and Mrs Kofteros, as I understood Mr Moody's argument, was that throughout the period from 31 January 2011 until June 2012 they had a reasonable excuse. This was based on the fact that the accountants had applied for time to pay (to Berkshire Recovery in Reading on 27 January 2011, to Debt Management of Croydon on 5 April and to the Worthing Unit in May). The circumstances, including the then current negotiations for the sale of Trueform, had been explained to HMRC. HMRC had, in consequence, deferred "further action" (according to the letters from the Worthing Unit of 23 June and 27

September 2011). In so doing, it was reasonable to assume that HMRC had addressed and then deferred making decisions on the time to pay applications as well as deciding to defer bankruptcy proceedings. Once HMRC had been informed about the death of the chairman of the acquiring company, both matters were left on hold. In the event, a satisfactory conclusion resulted when payment was made in full in June 2012. That, observed Mr Moody, reflected the good judgment of the Worthing Unit.

40. I have found this an unusually difficult case. The circumstances are unusual. The contentions for Mr and Mrs Kofteros are not based on "inability to pay". The sale of Trueform was the plan. That was intended to be the means of unlocking the funds to pay the tax. The actual excuse, as I understood it, was the taxpayers' reasonable expectation that HMRC would clearly and unequivocally respond to the repeated applications for time to pay under section 108. Negotiations for the sale of Trueform had been continuing throughout the period from January 2011 until June 2012. It was, I think, reasonable for Mr and Mrs Kofteros and their advisers to have concluded that their section 108 applications were respectable and could be successful. It was reasonable for them to have expected that the applications would be handled by officers who were not solely concerned with progressing bankruptcy proceedings. Here, however, the narrative of the events summarised in paragraphs 14 to 31 above shows the section 108 applications being passed on, without any final decision being communicated to Mr and Mrs Kofteros, from Reading to Croydon to Worthing to East Kilbride and to Cardiff. No doubt each place had a different part to play. Nonetheless, I have concluded that Mr and Mrs Kofteros had a reasonable excuse. They were, as I have explained, entitled to assume that their applications were based on reasonable grounds and that the applications (and revised applications) would be addressed and, until addressed, HMRC's decisions regarding payment would be kept on hold.

41. Reinforcing this conclusion are three factors. The first is the conclusion of the judge when he dealt with the appeal on paper. His analysis of the correspondence alone led him to conclude that there had been an actual agreement for time to pay, at least until 30 September 2011. Whether his actual decision were to be upheld on its merits is not in point; however, bearing in mind that he had not had the benefit of hearing Mrs Burke's evidence, there was nothing unreasonable about that conclusion. Second, the Statement of Case, which under the Tribunal Rules is required to contain the facts and matters on which HMRC rely, appears to endorse the judge's conclusion on that point. Those two factors give credibility to the assertion that Mr and Mrs Kofteros had reasonable grounds for expecting that a time to pay arrangement would be reached. Third, given the acceptance of both the judge and, with reservations, by the compilers of the Statement of Case that there had been a time to pay agreement on those lines, it is reasonable to assume that, had HMRC been called on to address the section 108 position after November 2011, HMRC would have allowed matters to remain "on hold". Whoever was then responsible for the section 108 decision would, in order to enable those involved in the negotiations for the sale of Trueform to come to terms with the impact of the death of the chairman of the acquiring company, have taken the same sensible and pragmatic decision as was taken by the Woking Unit in relation to bankruptcy proceedings.

Conclusions

42. For the reasons given above, I allow both appeals.

43. 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.

SIR STEPHEN OLIVER QC
TRIBUNAL JUDGE

RELEASE DATE: 2 May 2013