



**TC06028**

**Appeal number: TC/2016/01092**

*PAYE/NICS – whether accrual credited to loan account of a director chargeable to PAYE and NICs – yes – whether possible to reverse charge by prior year adjustment to the accounts – no – appeal DISMISSED*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**VENTURA UK LTD**

**Appellant**

**- and -**

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

**TRIBUNAL:    JUDGE AMANDA BROWN  
                  DAVID BATTEN**

**Sitting in public at Taylor House, 88 Rosebury Avenue, London EC1R 4QU on  
17 July 2017.**

**Mr Fenton Higgins of Higgins Fairbury and Co, accountants, for the Appellant.**

**Ms Gill Carwardine, Presenting Officer of HM Revenue and Customs, for the  
Respondents**

## DECISION

1. This is an appeal by the Ventura UK Ltd (“the Appellant”) against:

5 (1) Two determinations issued on 10 September 2015 in accordance with regulation 80 Income Tax (Pay As You Earn) Regulations 2003 each in the sum of £5130; one for each of the tax years 2011/12 and 2012/13.

(2) A notice issued on 10 September 2015 in accordance with section 8 Social Security Contributions (Transfer of Functions) Act 1999 in the sum of £7264 for the period 6 April 2010 to 5 April 2013.

10 (3) Two notice of assessments to penalties issued on 20 June 2016 in accordance with Schedule 24 Finance Act 2007 each in the sum of £1522; one for each of the tax years 2011/12 and 2012/13.

### Introduction

15 2. The Appellant is a company which buys and sells boats. It was incorporated in 2003. There are four company directors each of whom holds an equal share of the company. In addition there is one self-employed salesman.

3. One of the directors, Mr David Buchler, is also the chairman of the company. The Tribunal were informed that his role is non-executive in nature. At some point prior to April 2010 Mr Buchler made a substantial loan to the company. The Tribunal  
20 were not shown a copy of the loan agreement and it is not clear what sum was loaned nor whether it was interest bearing. However, by reference to the “nominal activity” report as at 7 November 2013, the sum showing as due to Mr Buchler was £375,872.14 (this sum included £128,000 unpaid directors remuneration see paragraph 5 below).

25 4. Mr Higgins explained to the Tribunal that the Appellant is a small business and is conducted very informally between the shareholder directors.

30 5. Mr Buchler did not have a service contract with the Appellant. However, it appears that it was agreed that on 31 September annually his loan account was to be credited with an annual salary of £16,000. By 30 September 2013 eight such sums had been so credited.

6. On 26 September 2013 HM Revenue & Customs (“HMRC”) issued a letter advising of a check of the Appellant’s employer records for the period 6 April 2012 to 26 September 2013.

35 7. An inspection was carried out on 7 November 2013. At that inspection HMRC were told that Mr Buchler was paid £16,000 at the end of each trading year but that the amount was credited to the loan account. It was explained that no payments had in fact been made to Mr Buchler and accordingly, it was the Appellant’s understanding that no PAYE or NICs were due by the Appellant in respect of the sums credited.

8. By correspondence dated 8 November 2013 the Appellant's representative informed HMRC that the company had been unable to make any repayments on the loan nor in respect of any accrued directors fees. It was noted that the directors were "fully aware that any director's fees that [were] eventually paid to Mr Buchler [would] be subject to PAYE and national insurance in the usual way".

9. By letter dated 13 November 2013 HMRC advised the Appellant that in their view the sums credited to Mr Buchler's loan account represented earnings from employment and were subject to both PAYE and NICs by reference to the earlier of the date on which the sums were credited in the company's accounts or the date on which Mr Buchler became entitled to them.

10. On 2 January 2014 the Appellant's representative confirmed that the sums credited to Mr Buchler had been voted upon but as they had not been paid it was proposed that in the 2013 corporation tax accounts all sums credited (£128,000) would be reversed by way of prior year adjustment. That adjustment was included in the 2013 accounts and provided to HMRC on 30 June 2014.

11. HMRC took the view that the annual sums had been accrued and any attempt to reverse the accrual by prior year adjustment or otherwise was ineffective and that the PAYE and NICs remained due.

12. Further correspondence ensued with HMRC issuing the final determinations (in respect of PAYE) and notice (in respect of NICs) on 10 September 2015. Both the determinations and the notice were appealed to HMRC on 21 September 2015 and notified to the Tribunal on 19 February 2016.

13. Penalty Notices were issued on 20 June 2016, maximum mitigation was permitted by HMRC. These were appealed on 30 June 2016 directly to the Tribunal.

## 25 **Legislation**

14. Section 1 Income Tax (Earnings and Pensions) Act 2003 ("ITEPA") imposes a charge to income tax on (inter alia) employment income in accordance with Parts 2 to 7A of the Act. So far as is relevant to the present appeal Part 2 provides that employment includes employment under a contract of service including the services of a director. The charge to tax arises on both general earnings and specific employment income. The provisions are lengthy (and the detail is not material for the purposes of the present appeal) but, in short, any salary, wages or fees obtained by an employee (or director) if it is in money or money's worth, that constitutes an emolument of the employment, is chargeable to income tax (see sections 3 – 7 and 62). It also provides that the charge to tax shall be determined by reference to what is known as "net taxable earnings" where that term is defined as total taxable earnings less deductions (see sections 9 – 11). In layman's terms the amount received by an employee (or office holder) will be taken to be the sum net of tax and the PAYE and NIC obligations will sit on top of the sum retained by the employee.

15. Of critical relevance in the present appeal is section 18 ITEPA which provides:

“Receipt of money earnings.

(1) General earnings consisting of money are to be treated for the purposes of this Chapter as received at the earliest of the following times:

5 *Rule 1*

The time when payment is made of or on account of the earnings

*Rule 2*

The time when a person becomes entitled to payment of or on account of the earnings

10 *Rule 3*

If the employee is a director of a company and the earnings are from employment with the company (whether or not as a director), whichever is the earliest of:

15 (a) the time when the sums on account of the earnings are credited in the company’s accounts or records (whether or not there is any restriction on the right to draw the sums);

(b) if the amount of the earnings for a period is determined by the end of the period, the time when the period ends;

20 (c) if the amount of the earnings is not determined until after the period has ended, the time when the amount is determined.

16. NICs are chargeable pursuant to Social Security Contributions and Benefits Act 1992 (“SSCBA”). Similarly to a charge to income tax collected under the PAYE scheme in ITEPA NICs are charged on earnings, including general earnings as defined under ITEPA, of an employed earner. Certain provisions apply to directors, such as Mr Buchler, who are paid annually (regulation 8 Social Security (Contributions) Regulations 2001 (“SSCR”). Neither party referred to or relied on either SSCBA or SSCR. The Tribunal does not understand there to be any dispute between the parties as to the scope of the charge to NICs. (The only dispute between the parties is, as set out in paragraph 26 below).

30 17. The provisions of section 8 Social Security Contributions (Transfer of Functions) Act 1999 and regulation 80 Income Tax (Pay As You Earn) Regulations 2003 provide HMRC with the power to collect PAYE tax and NICs where it appears to them that there has been under payment by an employer.

### **Appellant’s submissions**

35 18. The Appellant does not dispute that Mr Buchler is an employee or a director. Nor do they dispute the quantum of the declaration and notices if tax and NIC is due.

19. The Appellant solely contend that at the end of each trading year the Appellant company, for good housekeeping reasons, and by way of an ‘aide memoir’ accrued for the payment of a sum described as an “annual fee” of £16,000 (net) to Mr Buchler. It was, so it was claimed, only ever intended that the sums would be payable when  
5 there was sufficient cash in the business initially to repay the loan and subsequently the accrued annual fees. It was claimed that the prior year adjustment undertaken in the 2013 annual accounts was simply to reverse out the accrual which was never really intended.

20. The Appellant did not claim any reasonable excuse in relation to the penalty.

#### 10 **HMRC’s submissions**

21. HMRC contend that Mr Buchler was entitled to receive the annual fees in each trading year, they were the subject of a vote by the company, and were duly credited in the Appellant’s accounts (by reference to the accrual to the loan account). On that basis the charge to income tax and NIC contributions arose in each tax year.

15 22. By reference to the provisions of the Companies Act 2006 (sections 393 and 454) HMRC contended that the accounts had been prepared on a true and fair view and that any attempt by the Appellant to restate the accounts by way of the prior year adjustment was incorrect.

23. In HMRC’s view that tax and NICs were due by reference to the sums accrued.

#### 20 **Discussion**

24. There was limited evidence available to the Tribunal however, on the basis of what was available the Tribunal considers that Mr Buchler was clearly entitled to receive the annual fees. They were credited to his loan account (indicating he was content for the cash to be continued to be used in the business) and had he chosen to  
25 do so he could have called in the loan or otherwise enforced the debt he was owed by the company. Year on year therefore (over a period of what seems to be eight years) the charge to tax and NICs arose in respect of the payments.

25. It is clear to the Tribunal that the provisions of ITEPA were clearly met on an annual basis such that the Appellant was liable to account for PAYE and NICs on the sums credited to Mr Buchler. In each of the tax years 2011/12 and 2012/13 a charge  
30 to tax and NICs arose.

26. The sole question for the Tribunal is therefore whether the prior year adjustment included in the Appellant’s accounts in the year to 30 September 2013 has the effect of eliminating the charge to tax and NICs.

35 27. It is clear that the Appellant did not restate its prior year accounts i.e. those prior year accounts have not been altered. The note in the 2013 accounts states “Prior Year Adjustment. This relates to directors emoluments which are no longer payable. These had been voted for a non-executive director over a few years but not paid. It is now agreed that the emoluments are no longer payable and the provision has therefore

5 been reversed amounting to a total of £128,000". The Tribunal takes the view that even were it possible to reverse the accrual in a way which reversed the charge to tax and NICs (and on that the Tribunal expresses no view) this prior year adjustment cannot be said to do that. All the adjustment acknowledges is that the accrual is being reversed and that sums which were payable are "no longer" payable. To the Tribunal that appears, on its face, to recognise that Mr Buchler was entitled to the payments in the year by reference to the agreement between him and the company. By the adjustment (affecting net gains and losses) Mr Buchler has absolved the company of its liability to him. He cannot absolve it of its liability to HMRC.

10 28. The language of section 18 ITEPA and the distinction between rule 2 and rule 3 appears to make clear that if the Appellant had wanted to escape the charge to income tax under PAYE and the charge to NICs Mr Buchler needed to have indicated that he did not consider the annual fees payable to him in advance of each trading year end, before the vote for accruals in his favour and before the entries in the company  
15 accounts.

### **Conclusion**

29. For the reasons given the appeal is dismissed.

30. 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  
20 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.

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**AMANDA BROWN  
TRIBUNAL JUDGE**

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**RELEASE DATE: 26 JULY 2017**