TC02906

Appeal number: TC/2012/08958

Income Tax - Application to appeal out of time - Dispute about basis of accounting for receivables - Application granted

FIRST-TIER TRIBUNAL
TAX CHAMBER

S. MAHMOOD t/a ELITE CLAIMS **Appellant**

- and -

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

TRIBUNAL: JUDGE HOWARD NOWLAN
MEMBER: JANE SHILAKER

Sitting in public at 30-31 Friar Street, Reading on 27 August 2013

Barrie Dobkin of B & M Dobkin, Accountants, on behalf of the Appellant

Paul Reeve of HMRC on behalf of the Respondents

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DECISION

This Application led to a very confused hearing, and it will be somewhat difficult to summarise the outcome and our reasons for the decision that we have reached clearly.

2. The confusion extended even to the subject matter of the hearing. The Respondents correctly understood that the Application was an opposed Application by the Appellant to bring Appeals in relation to two years of assessment, 2002/2003 and 2004/2005, when the Appellant was seriously out of time for commencing such Appeals. In a somewhat extraordinary manner the Appellant's representative appeared to believe that he was appearing in order to conduct the substantive Appeals, on the basis that he had already filed valid Applications to Appeal in due time and a very long time ago.

3. Whilst the point that we must decide is whether to allow the Appellant to appeal out of time for the two periods of assessment, it will be clearest if we first explain the nature of the disputes for the two relevant periods, and principally that for the later period 2004/2005.

The disputes for the two periods

4. The dispute in relation to the year 2002/2003 related to the minor question of whether HMRC had failed to allow full relief for expenses and for mortgage interest when increasing the assessment in respect of the Appellant's rental income.

5. The dispute in relation to the year 2004/2005 was considerably more complex. By that date the Appellant had commenced a business of providing various services to drivers, often taxi drivers, who had been involved in "no-fault" car crashes. The services appeared to involve introducing the drivers to a firm of solicitors that would consider progressing their claims on a "no win-no fee" basis, and also the provision of suitable cars while the claimant's car was being repaired. We were given no details of the cars owned or leased by the Appellant in order to provide these cars on a rental basis, but we were told that the Appellant was able to provide suitable cars, often for taxi drivers, and sometimes the Appellant provided limousines. The Appellant's fee income appeared to consist of three elements. One was an introductory fee of approximately £600 that was payable for effecting the introduction of a crash-victim to the firm of solicitors, which barely featured in the dispute. The second element was the entitlement to 25% of any recoveries by the driver in respect of personal injury claims, but payable only of course if any such amount was both claimed and received. The third amount (which occasioned the dispute) was a charge for renting a car to the accident victim whilst his car was being repaired.

6. It appeared to have been the Appellant's practice to produce a rental contract for the provision of the car, but until the point when the insurance company (presumably the insurance company for the other driver) had admitted fault, no financial sum was inserted into this agreement for the rental charge. When the insurance company admitted liability, figures were then inserted into the rental agreement, and those amounts were then claimed from the insurance company. Insurance companies often

refused to pay the full amounts claimed, and on many occasions the Appellant eventually accepted lower, and sometimes much lower, amounts of rental income from the insurance companies.

7. No dispute related to the possible 25% share of injury receivables payable to the Appellant. HMRC accepted that those should only be recognised for accounts purposes when settlements had been reached and payments received. The dispute focused instead on the rental receivables. The Appellant's accountant had drawn up the Appellant's accounts, and tax return figures for the period 2004/2005, by including only the amounts eventually received from the insurance companies, and by recognising those amounts only when the insurance companies had actually agreed to pay the eventually agreed amount. In contrast HMRC had contended that in order to comply with UK GAAP the Appellant should initially have recognised receivables in respect of car rental, once the figures had been inserted into the rental contracts and submitted to the insurance companies for payment, then making bad debt claims in following periods if only reduced amounts were eventually received.

8. The year 2004/2005 was the Appellant's first year of trading, so that HMRC contended that provided the accounts were consistently drawn up in the manner claimed to be required by HMRC, some income might be accelerated as a timing matter, but ultimately (and provided the same accruals basis was followed in succeeding periods) the Appellant would always end up being taxed only on the net amounts eventually received. At some stage, HMRC appeared to have been under the impression that Mr. Dobkin had agreed that future accounts should be drawn up on the basis contended by HMRC to be the only correct basis, and if this understanding had been correct it would have been consistent with the expectation that the Appellant would no longer wish to dispute the adjusted figures, advanced by HMRC in respect of the first year, namely 2004/2005.

9. The effect of HMRC's substitution of the accruals basis for the cash basis that the Appellant's accountant had initially adopted for accounts and tax return purposes was to increase the assessable income for the period 2004/2005 by approximately £75,000.

10. On 3 March 2011, HMRC issued their closure notice for the 2004/2005 period, increasing the taxable profits by the amount just referred to. Somewhat over a year later, Mr. Dobkin responded on behalf of the Appellant to a demand from HMRC's debt management enforcement unit demanding payment of the tax in accordance with HMRC's adjusted figures, Mr. Dobkin saying:

> *"As you will recall when you raised the assessment I informed you that I did not believe that the assessment was correct and that I would be reviewing our clients' records for all years and would contact you when I had finished although this would take some time."*

11. HMRC responded by treating Mr. Dobkin's letter as an attempt to appeal against the assessment, and HMRC pointed out that it was slightly in excess of 11 months late, and that so far as HMRC could see, there was no reasonable excuse to justify HMRC granting leave to appeal out of time.

The circumstances surrounding the Appellant's claims that appeals had already been made

12. Dealing with the simple point first, Mr. Dobkin established that he had entered an appeal on behalf of the Appellant in relation to HMRC's original assessment of rental income for the period 2002/2003. This was undisputed. That had been followed by a period of considerable discussion at the end of which HMRC altered the original assessment and issued a revised assessment for a reduced figure, the accompanying letter making it clear that if the Appellant wished to appeal against the revised assessment, notice of appeal should be given within 30 days. None was ever given in response to that letter from HMRC, but Mr. Dobkin's contention before us was that the appeal against the original assessment remained a valid appeal, and it had certainly not been settled by agreement. HMRC claimed, in response, that a fresh appeal had to be made in respect of the revised assessment, and that plainly no such appeal had been made.

13. There was equivalent, but different, confusion in relation to the more significant period, namely 2004/2005. Mr. Dobkin first asserted that he had given notice of an appeal in relation to this period, and he referred us to a letter that appeared to support this claim. HMRC then pointed out however that, at the relevant time, no assessment had been made at all. Mr. Dobkin then referred to the wording in his later letter that we quoted in paragraph 10 above, and claimed that HMRC must have realised that he had indicated in a phone call that he intended to appeal. HMRC said that they had no record of any such phone call, even if they were to accept that an appeal could be commenced in such an informal manner.

The law in relation to late appeals

14. Our understanding of the relevant law is that HMRC themselves have power to admit a late appeal, after the normal 30-day period, but only if they are satisfied that the taxpayer had a reasonable excuse for being late, and that the appeal had been made within a reasonable time after that excuse ceased to be a factor. In contrast we, as the Tribunal, can grant leave for a late appeal even when the taxpayer has been unable to assert any reasonable excuse. We should however consider, and balance, a number of factors. We should consider the importance of requiring parties to adhere to statutory time limits, all in the interests of achieving finality in litigation. We should consider the overall justice of allowing or rejecting the application, the likelihood that the appeal might succeed, and the possibility that the parties might have difficulty in producing evidence after a long period of delay.

HMRC's contentions

15. HMRC advanced some strong contentions. They contended that strictly no valid appeals had been commenced in relation to either year. They suggested that it was extraordinary that the Appellant's accountant had ignored the intimation in the revised assessment for 2002/2003 that clearly indicated that an appeal should be raised in relation to that revision within 30 days. They contended that it was extraordinary that an accountant might think that an appeal had been raised in respect of 2004/2005 in reliance on a notice of appeal issued before there had even been an assessment, and equally extraordinary that we should be asked to treat an appeal as

having been commenced by the suggested phone conversation (of which HMRC had anyway no record) that we referred to in paragraph 13.

16. HMRC also claimed that an appeal would anyway be pointless for two reasons. Firstly, they claimed that their contention about the requirement to adopt an accruals basis of accounting in relation to the rental figures presented to insurance companies was manifestly correct, such that any appeal would be bound to fail. Secondly, since in succeeding periods assessments would be reduced insofar as the Appellant later accepted reduced amounts in settlement of its rental claims from insurance companies for the 2004/2005 period, the Appellant would suffer no hardship.

The Appellant's contentions

17. The Appellant continued to argue that the whole of the Appellant's business was conducted on a "no win – no fee" basis, and that it was therefore appropriate to recognise all the income only on a cash basis. In support of this, and adding to the confusion, we were shown an agreement that was said to support the "no win – no fee" claim, but on looking at it, it seemed to be completely irrelevant because it was a standard agreement that claimants were expected to enter into with the relevant firm of solicitors in respect of that firm's services and charges, and it seemed to have no bearing on the Appellant's services. We chose not to look at other possibly more relevant agreements that were later produced and that had neither been produced to the Respondents nor the Tribunal prior to the hearing. They were long and would require considerable study, which would need to be undertaken by the Tribunal later if the Appeal was to proceed, but they were too involved for us to consider at this preliminary stage.

The problematic point

18. It then emerged, and it is possible that HMRC had been unaware of this point prior to the hearing, that whilst HMRC had thought that Mr. Dobkin had prepared the Appellant's accounts on an accruals basis for all later years, all later accounts had in fact been prepared on the cash basis that Mr. Dobkin contended remained correct. HMRC had instituted no enquiries in relation to any of these later years from 2005/2006 to the current date, so that the basis of accounting adopted by Mr. Dokbin had not been disputed, and most of the years were presumably no longer open to adjustment. Two obvious consequences will result from the fact that all later accounts were prepared on a cash basis, should the Appellant have no opportunity now to contest the additional £75,000 of income added by HMRC to the assessable income for the period 2004/2005. In so far as amounts included in those accruals were actually received in the following periods in cash (and then recognised in the accounts) those amounts would have been taxed twice. And insofar as amounts included in the £75,000 of accruals in 2004/2005 were never received, the later cash basis of accounting would have failed to reduce the assessed income on account of the ultimate non-receipt. It therefore followed that:

- if Mr. Dobkin was correct in his claim that the cash basis remained appropriate, then it was only by allowing the appeal for 2004/2005 to proceed and by the Appellant prevailing in that appeal that the Appellant would avoid these two unfortunate consequences; and

- if Mr. Dobkin's claim was wrong, such that even a late appeal for 2004/2005 would have to be dismissed, the Appellant would still end up being taxed on £75,000 more income than it ultimately received. HMRC might well respond by saying that that would only result from the fact that Mr. Dobkin would have continued to prepare the accounts on a cash basis, when they thought that he had accepted HMRC's proposition that they should be prepared on an accruals basis. Nevertheless, the Appellant would still suffer something of an injustice, albeit possibly one of its own making or its accountant's making.

Our decision

19. Our first conclusion is that there was no valid subsisting appeal in relation to either the period 2002/2003 or 2004/2005. We were not addressed fully in relation to whether the pre-existing valid notice of appeal in relation to the initial assessment made for 2002/2003 remained a valid appeal, and so our conclusion in relation to that point is a tentative one. For reasons that will emerge, this seems to us to be immaterial, and we continue with the proposition that there is at present no valid subsisting appeal for either period.

20. We also accept that no reasonable excuse existed for the late appeal for 2004/2005 and for the 2002/2003 period if Mr. Dobkin was to be taken to be applying for leave to appeal out of time for that year as well. No reasonable excuse was suggested, beyond the suggestion that Mr. Dobkin had been busy, and had at some point had a dispute with his wife, but neither appeared remotely credible as a reasonable excuse for the simple failure to file Notices of Appeal.

21. There are, however, two reasons why we decide to allow the late appeals for both relevant periods. The logic relates principally to the period 2004/2005, but if we allow a late appeal in relation to that year, it is a small step to allow the appeals for both years.

22. The first fact that has influenced us is that Mr. Dobkin appeared at the Tribunal with a substantial lever-arch file of paperwork in which he suggested that he had produced revised figures for all years. The significance of this, not that we looked at any of the papers, was that the matter was clearly now being treated seriously, and the application to make a late appeal was not just an excuse to delay finalising matters.

23. The more material factor that has influenced us, however, is the fact that, because the accountant has persisted in the belief that the cash basis is the appropriate basis on which to recognise all receipts, and because all later accounts have been prepared on that basis, it is only by allowing the late appeal that the Appellant has any chance of avoiding what will otherwise be the inequity of being taxed on £75,000 more income than it will ultimately have received. Insofar as the Appellant's contentions for the period 2004/2005 may ultimately fail, and it prove impossible for the parties to agree adjustments for all later periods because those periods are no longer open, HMRC may well contend that any inequity has resulted from the actions of the Appellant and its accountant, and that HMRC cannot be responsible for this.

24. The outcome, however, of refusing the late application to appeal for the period 2004/2005 would still produce a result (namely an indisputable debt for the extra tax plus interest in respect of the 2004/2005 period) that nobody could treat as remotely satisfactory. It is perfectly possible that it would result in the Appellant having to cease his business, or being unable to pay the tax. When the tax is indisputably owed, or the tax is due in respect of profits that were plainly actually received, there is then no occasion to grant leave to appeal out of time. But when, in this case, the debt would relate to the element of income (taking all years together) that would ultimately never have been received, we consider that we should do everything that we can do to enable the parties to avoid that result.

25. We accordingly grant leave for late appeals to be made in respect of both periods.

26. We advance no opinion as to whether, should the Appellant's contentions in relation to the period 2004/2005 prove to be wrong, there is any way in which adjustments can be made for later periods in order to avoid what appears to us to be a resultant and inevitably unfortunate outcome. If the parties could negotiate a settlement on these terms without the Appeal for 2004/2005 having to proceed before the Tribunal, this would be the ideal outcome. Naturally we have no influence over whether that result can be achieved.

Right of Appeal

27. 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.

HOWARD M. NOWLAN
TRIBUNAL JUDGE

RELEASE DATE: 30 September 2013