



TC06187

Appeal number: TC/2017/00790

*CAPITAL GAINS TAX – penalty for failure to pay tax on time –
insufficiency of funds as a result of an escrow arrangement – whether or not
a reasonable excuse – yes – appeal allowed*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

MARK PEARSON

Appellant

- and -

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

TRIBUNAL: JUDGE TONY BEARE

**Sitting in public at Taylor House, 88 Rosebery Avenue, London EC1R 4QU on
12 October 2017**

Mr J. Black QC for the Appellant

Mr S. Goulding, Officer HM Revenue and Customs, for the Respondents

DECISION

1. This decision relates to an appeal by the Appellant against a late payment penalty for the tax year of assessment ending 5 April 2015 in the amount of £91,644.00.

2. There is no disagreement between the parties as to the relevant law or the relevant facts in this case. The dispute relates solely to how the relevant law should apply on the basis of the relevant facts.

The law

3. Both parties agree that:-

(a) pursuant to sub-section 59B(4) Taxes Management Act 1970, the Appellant became liable to pay capital gains tax of £1,832,893.88 on 31 January 2016 in respect of the tax year of assessment ending on 5 April 2015;

(b) the Appellant did not discharge this liability until July 2016; and

(c) as a result of failing to make the above payment within 30 days of the date when it became due, the Appellant became liable to a penalty of £91,644.00 under paragraph 1 Schedule 56 Finance Act 2009 unless he can satisfy the Tribunal that there is a reasonable excuse for his failure (see paragraph 16 Schedule 56 Finance Act 2009).

4. Sub-paragraph 16(2) Schedule 56 Finance Act 2009 provides that:-

“(a) an insufficiency of funds is not a reasonable excuse unless attributable to events outside [the relevant taxpayer’s] control,

(c) where [the relevant taxpayer] had a reasonable excuse for the failure but the excuse has ceased, [the relevant taxpayer] is to be treated as having continued to have the excuse if the failure is remedied without unreasonable delay after the excuse ceased”.

5. So the dispute in this case turns on whether the Appellant’s failure to discharge the relevant capital gains tax liability on or before the date falling 30 days after the liability became due can be said to be the result of an insufficiency of funds “attributable to events outside [the Appellant’s] control” and, if so, whether, once that ceased to be the case, the Appellant remedied his failure without unreasonable delay.

The facts

6. The Appellant was the Chief Executive Officer and the majority shareholder in a company called Global Voucher Group Limited (“GVG”) and owned over 90% of the shares in that company. In June 2014, the Appellant sold his shares in GVG to a public company named Monitise plc (“Monitise”). In consideration for that disposal, the Appellant became entitled, either unconditionally or contingently, to a significant

number of shares in Monitise which were to be issued to him over a two year period. Taking into account deferred share issues and assuming that all contingencies were satisfied, the value of the shares in Monitise which the Appellant would receive, based on the Monitise share price at the date when the Appellant entered into the transaction, was approximately £55 million.

7. Pursuant to the sale and purchase agreement and the related escrow arrangements into which the Appellant entered at the time of the sale, the Appellant was required to maintain an escrow account to provide security to Monitise for certain contingent liabilities of the Appellant. Those agreements together required the Appellant, as soon as reasonably practicable after completion and in as many transactions as might be necessary, to sell such number of his initial consideration shares as would generate aggregate net proceeds (after deducting all applicable fees and expenses) of £13 million and then for those funds to be held in escrow pending their release in specified circumstances.

8. In the event, the Appellant sold a little under half of his initial consideration shares between 27 June 2014 and 18 September 2014. These sales raised net proceeds of approximately £6 million and those net proceeds were placed into the blocked account. It is those disposals which gave rise to the capital gains tax liability whose delayed payment led to the penalty which is the subject of this appeal.

9. Even though the proceeds raised by the initial sales were still some £7 million short of the amount which was required to be maintained in the blocked account, the Appellant did not sell any further shares in Monitise after 18 September 2014.

10. This was primarily because the Monitise share price at that stage began to fall dramatically. On 27 June 2014, a Monitise share was worth £0.5489. This fell to £0.2922 on 19 September 2014, £0.1362 by 23 January 2015, £0.069 by 17 July 2015 and ultimately £0.0279 by 2 October 2015. The price has stayed at this approximate figure ever since. The rapid fall in the value of the Monitise shares took the Appellant by surprise and, initially at least, he decided to defer further disposals in the hope that the share price might rise to a level where he could realise sufficient proceeds both to top up the blocked account to the £13 million required level and to generate funds which he could use for his own purposes, including discharging the capital gains tax liability described above.

11. At the hearing, the Appellant added that a further reason why he did not make further disposals of Monitise shares in the period after 18 September 2014 was that he was not allowed to do so because he was working in the Monitise business following the sale and, as an insider, he was subject to restrictions in that regard. Following the hearing, the Appellant provided to the Tribunal evidence of this in the form of copies of e-mail exchanges with Monitise to that effect over the relevant period.

12. The dramatic fall in the Monitise share price, coupled with the terms of the escrow arrangements, left the Appellant in a serious predicament. At the hearing, he outlined the various steps which he took in the period after September 2014 to acquire the funds by which he could discharge his capital gains tax liability. In summary,

those steps involved prolonged negotiations with Monitise in which he sought to obtain the release of the monies in the blocked account or to repurchase GVG from Monitise using borrowed monies. The negotiations with Monitise followed a tortuous path and led to the Appellant's incurring significant legal fees. In order to pay those fees and discharge an earlier tax liability, the Appellant was ultimately forced to sell his house in December 2015 and, since then, he has been living in rented accommodation.

13. In his oral evidence before the Tribunal, the Appellant explained that apart from the monies in the blocked account and his remaining shares in Monitise (which could not be used to generate cash for the Appellant because of the blocked account threshold), the Appellant's only assets were shares in some private tech companies which could not be easily liquidated.

14. In addition, the Appellant had no assets to secure any funding from potential lenders. He had had a meeting with his bank but it was clear that, in the absence of his having any realisable assets, no such funding would be forthcoming.

15. The Appellant conceded that he had not contacted the Respondents prior to 31 January 2016 in order to inform them of his difficulties and seek to enter into a time to pay arrangement. He said that this was partly due to the fact that his focus at the time was very much on reaching an agreement with Monitise that would free up the resources necessary to pay the tax but largely because there was no schedule to which he could commit in relation to paying the liability. He knew that he would not be able to discharge the liability until he had reached an agreement with Monitise and he did not know when the negotiations with Monitise would reach fruition. For instance, he had originally thought that a deal with Monitise would be signed at the end of 2015 but, in the end, he was unable to settle his dispute with Monitise until July 2016.

16. At that point, the monies in the blocked account were released to him and he discharged the capital gains tax liability in question within a day of receiving the settlement monies.

17. In summary, as a result of his having entered into the escrow arrangements associated with the sale of GVG and the catastrophic fall in the Monitise share price in the period following his initial disposals in 2014, the liquidity position of the Appellant between the date of his initial disposals and the date when he ultimately reached his settlement with Monitise in July 2016 was such that the appellant had no means of discharging his capital gains tax liability on the due date of 31 January 2016 or between then and when he did so in July 2016. Moreover, the Appellant discharged the relevant liability as soon as he had reached his settlement with Monitise and had realised the funds with which he could make the payment.

The parties' submissions

18. In their submissions to the Tribunal, both parties agreed that, where a capital gains tax liability is not discharged on its due date because of an insufficiency of funds, the question of whether or not there is a reasonable excuse turns on whether a

reasonable competent businessman in a similar situation would have defaulted when faced by the same or a similar predicament.

19. For reasons which will become apparent further below, I do not believe that that is the correct test to apply, based on the language used in sub-paragraph 16(2)(a) Schedule 56 Finance Act 2009. However, in case my interpretation of that provision is subsequently held to be incorrect, I set out below the parties' respective arguments based on that proposition and my views on those arguments.

20. The Appellant's case is straightforward. He maintains that, when he entered into the terms of the sale and purchase agreement in June 2014, he could not reasonably have been expected to foresee the catastrophic decline in value of the Monitise share price and therefore he could reasonably have expected to be able to discharge the capital gains tax liability resulting from his disposals following the transaction out of funds realised from those disposals over and above the funds required to be maintained in the blocked account. The Appellant accepts that a diligent, competent and reasonable businessman might expect there to be fluctuations in the value of shares. However, he maintains that the radical devaluation of the Monitise shares in this case – a fall of some 95% over the period of a year - could not reasonably have been foreseen when he agreed to the terms of the escrow arrangements.

21. As regards his failure to enter into a time to pay agreement with the Respondents, the Appellant submits that, given his focus on reaching agreement with Monitise in the months preceding the due date for payment of the liability, the fact that a deal was almost reached at the end of 2015 which would have enabled him to discharge the liability on the due date and the fact that he had no fixed dates to offer the Respondents in terms of a time to pay agreement, that should not prevent him from relying on the reasonable excuse defence.

22. I had expected the Respondents, in response to the first of the above submissions to assert that the Appellant should have taken into account the remote possibility of the fall in the Monitise share price which actually occurred before agreeing to the escrow terms and therefore that his agreement to those terms fell short of the actions which a reasonable competent businessman would have taken in a similar situation. However, Mr Goulding made it plain that this was not the Respondents' case. He said that he accepted that the extent of the fall in the Monitise share price was something which no reasonable businessman in the position of the Appellant could have foreseen. However, said Mr Goulding, the Appellant would have known in the period leading up to the tax payment date of 31 January 2016 that he would not be able to discharge the relevant capital gains tax liability and that the Appellant's failure at that time to approach the Respondents and negotiate a time to pay agreement was not consistent with the standard to be expected of a reasonable competent businessman.

Discussion

23. As I said at the hearing, I think that the Appellant might well have avoided the imposition of a penalty in this case if he had kept the Respondents better informed of his position in the run up to the due date for payment of the tax liability. Whilst he
5 may have been unable to agree a time to pay arrangement with the Respondents at that time because of the state of his negotiations with Monitise, the Respondents may have reacted a little more sympathetically than they have done if they had been kept informed of the position. I think that the Appellant now accepts that he was at fault in that respect.

10 24. Nevertheless, I am inclined to accept the Appellant's submission that, insofar as the standard to be applied is that of the reasonable competent businessman, the Appellant does have a reasonable excuse for his default.

25. It is clear from the evidence given by the Appellant that, over the period between September 2014 when the share price began to fall and the date when the
15 Appellant ultimately discharged the liability in question, the Appellant was using every means at his disposal to free himself from the consequences of the obligations into which he had entered at the time of the sale of GVG. Both parties agree that the catastrophic fall in the Monitise share price was not something which a reasonable competent businessman could have predicted and I am satisfied that the Appellant did
20 as much as he could to mitigate the consequences of that.

26. Moreover, although I think that the Appellant made an error in failing to contact the Respondents before the date when the liability became due, I do not think that his doing so would have helped him to discharge the liability any sooner than he did. The Appellant was in the middle of intense and protracted negotiations with Monitise and
25 had no way of knowing if or when those negotiations would reach a successful conclusion. He initially had grounds for believing that the negotiations would conclude by the end of 2015 – in which case, he would have been able to discharge the capital gains tax liability on its due date – but that fell through. After that, his focus, quite rightly, was in reaching a deal with Monitise that would enable him to
30 pay the tax and he had nothing to offer the Respondents until that occurred. So I consider that the decision not to contact to the Respondents but instead to focus on bringing the negotiations to a conclusion as soon as possible was consistent with the standard of behaviour which is to be expected from a reasonable competent businessman.

35 27. The above conclusion means that, if the parties are correct in their agreement that the appropriate test to apply in a case such as this is the standard of a reasonable competent businessman, I find, in favour of the Appellant, that he has acted in the same way as one would expect of a reasonable competent businessman and therefore that he has a reasonable excuse for his default in this case.

40 28. Having said that, I do not think that the parties are correct in applying a test based on what a reasonable competent businessman in a comparable situation would have done. This is because, in my view, the language used in the relevant provision

makes it clear that a failure to discharge the relevant tax liability as a result of an insufficiency of funds caused by events outside the taxpayer's control can amount to a reasonable excuse. So, in my view, the relevant test to apply in this context is to ask:

- 5 (a) whether the Appellant's failure to discharge the relevant liability on or before the date when the penalty arose was due to an insufficiency of funds; and
- (b) if so, whether the insufficiency of funds in question arose by reason of events which were outside the Appellant's control.

29. The cases cited to me by the parties in which the reasonable competent
10 businessman test was applied were cases relating to different legislation – the VAT default surcharge legislation and the provisions in Section 59C Taxes Management Act 1970, the predecessor to the provision I am considering. Those provisions simply stipulate (or stipulated) that an insufficiency of funds is not a reasonable excuse and the courts have then applied a more general test in holding that an insufficiency of
15 funds caused by circumstances which could not have been foreseen by a reasonable competent businessman can nevertheless qualify as a reasonable excuse.

30. In this case, in contrast, it is apparent that an insufficiency of funds can constitute a reasonable excuse as long as that insufficiency arises by reason of events outside the taxpayer's control.

20 31. So, turning to consider the position of the Appellant on that basis, it is quite clear based on the evidence, and both parties accept, that the Appellant's failure to discharge the relevant liability on or before the date when the penalty arose was due to an insufficiency of funds. That means that it is merely necessary to consider whether that insufficiency of funds arose by reason of events outside the Appellant's
25 control.

32. On the basis of the facts described above, I believe that the insufficiency of funds in this case did arise as a result of events outside the Appellant's control – namely, the catastrophic fall in the Monitise share price after the Appellant entered into the escrow arrangements. By the time that the Appellant made the disposals
30 giving rise to the capital gains tax liability in question, the Appellant had already entered into the escrow arrangements and set himself on a course which ultimately led to his default. One cannot say that the decision on the Appellant's part to enter into the escrow arrangements was within his control. This is because the terms on which he entered into the disposal of his shares in GVG were a matter of negotiation with
35 Monitise as the purchaser of those shares. So the Appellant was not in control of those terms unilaterally. The Appellant would hardly have agreed to the terms of the escrow arrangements if that had not been a requirement imposed upon him in the negotiations by Monitise. Moreover, even if one could say that the decision to enter into the escrow arrangements was within the Appellant's control, the escrow
40 arrangements merely created the circumstances which ultimately led to the Appellant's default. The proximate cause of that default was the catastrophic fall in the Monitise share price. If that had not occurred, the Appellant would have been able to top up the blocked account and realise sufficient proceeds from the disposal of

Monitise shares to meet the capital gains tax liability in question. As that catastrophic fall was clearly outside the control of the Appellant, I believe that the language of the statutory provision in question is satisfied.

5 33. Finally, for the sake of completeness, I would observe that the failure on the part of the Appellant to enter into a time to pay arrangement with the Respondents was also not within the Appellant's control. Apart from the fact that he was dependent on the Respondents' agreement to any proposal he might make, he was unable to offer the Respondents any timetable for making payments, given the state of his negotiations with Monitise.

10 34. For these reasons, I consider that the inability of the Appellant to discharge his capital gains tax liability by the date falling 30 days after the liability became due was caused by an insufficiency of funds attributable to events outside the Appellant's control. It was therefore a reasonable excuse within the meaning given by sub-paragraph 16(2)(a) Schedule 56 Finance Act 2009.

15 35. Moreover, as the Appellant was able to complete his settlement with Monitise only in July 2016 and paid the tax in question immediately following that settlement, I consider that the Appellant discharged his liability immediately after his reasonable excuse ceased to exist so that the language in sub-paragraph 16(2)(c) Schedule 56 Finance Act 2009 is satisfied.

20 36. For the above reasons, I uphold the Appellant's appeal against the penalty.

25 37. 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.

30 **TONY BEARE**
TRIBUNAL JUDGE

RELEASE DATE: 25 OCTOBER 2017