[2018] UKUT 0100 (TCC)

Appeal number: UT/2016/0240

INCOME TAX and NATIONAL INSURANCE CONTRIBUTIONS (NICs) – calculation of gross remuneration in an amount which, after deduction of PAYE and NICs, would equal and extinguish liability of director to company on director's loan account – company insolvent and unable to pay tax and NICs – whether tax deducted by company – whether director received relevant payments knowing that the company had wilfully failed to deduct PAYE – regulation 72, Income Tax (Pay As You Earn) Regulations 2003 – whether company failed to deduct and pay primary NICs and the director knew that the company had wilfully failed to pay – regulation 86, Social Security (Contributions) Regulations 2001

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Appellants**

- and -

STEPHEN WEST **Respondent**

TRIBUNAL: SIR GEOFFREY VOS, CHANCELLOR OF THE HIGH COURT
JUDGE ROGER BERNER

Sitting in public at The Royal Courts of Justice, The Rolls Building, Fetter Lane, London EC4 on 12 and 13 March 2018

Ms Laura Poots, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Appellants

Mr Tony Slater, TS Tax Limited, for the Respondent

DECISION

1. This is an appeal by the Commissioners for Her Majesty's Revenue and Customs ("HMRC") against the decision of the First-tier Tribunal (Judge John Clark and Ms Sandi O'Neill) ("FTT"), on the casting vote of Judge Clark (Ms O'Neill having dissented), to allow Mr West's appeal against HMRC's directions with respect to PAYE, and a consequent assessment and amendment in relation to income tax, and decisions with respect to national insurance contributions ("NICs"), arising in the circumstances we will describe.

2. Judge Clark in the FTT refused permission to appeal, but in this tribunal permission was given by Judge Herrington.

Background

3. Mr West was, from 2003, the sole director and shareholder of Astral Telecom Limited ("Astral"). Astral was put into creditors' voluntary liquidation in 2011, with a deficiency on the joint liquidators' Statement of Affairs of £146,611. That statement showed that PAYE and NICs totalling £99,886 were owing at that time to HMRC.

4. For a number of years, Mr West had drawn money from Astral during the year and this had been recorded in a director's loan account ("the Loan Account"). At the end of each year, Astral would pay Mr West a small amount of remuneration and a larger dividend, thereby extinguishing the Loan Account.

5. There was a change to this pattern from the accounting period ended 30 April 2007 onwards. Although salary and dividends continued to be paid to Mr West, the amount outstanding on the Loan Account was not extinguished at the end of each year, and it in fact increased for several years. For the year ended 30 April 2010, Mr West was paid a salary of £5,715 and received a dividend of £51,000. The amount left outstanding on the Loan Account as at 30 April 2010 was £40,719.

6. Towards the middle of 2011, Mr West became concerned about the state of Astral's business. He sought advice from an insolvency practitioner in June of that year, and he was advised to put Astral into liquidation. The insolvency practitioner also advised Mr West that Astral could not pay him dividends for that year (the year to 30 April 2011) as there were insufficient available profits, and that payment to him would have to be wholly by way of salary.

7. Mr West instructed his accountant to prepare a set of accounts for the liquidation of Astral. He also instructed his accountant to prepare accounts showing an amount of director's remuneration which, after deducting PAYE and NICs, would offset the amount outstanding on the Loan Account. At that time the amount outstanding on the Loan Account was £129,150.

8. Mr West received no further money from Astral. Draft management accounts for the period 1 May 2010 to 26 July 2011 were prepared and sent to him at the end of July 2011. Those accounts showed director's remuneration of £202,976 and employer's NICs of £26,061. Among the amounts shown as owing to creditors was the sum of £99,886 in respect of "Tax and NIC". The Loan Account of £129,150 was extinguished by the credit of the net amount of the director's remuneration after deduction of PAYE and NICs. Mr West signed these accounts and used them as the basis for his instructions to the liquidators.

9. For both the periods in question, 2010-11 and 2011-12, forms P35 (employer annual return) were filed with HMRC. HMRC's P14/P35 internet filing report for 2011-12 showed a liability for PAYE and NICs of £69,409.43. Judge Clark also found, at [70] of the FTT's decision, that a supplementary P35 for 2010-11, which was submitted late on 31 January 2012, showed a liability for PAYE and NICs of £39,308.43.

10. The gross remuneration and tax deducted were entered in Mr West's tax returns, which were signed by him.

11. HMRC began enquiries in February 2013, and those enquiries resulted in HMRC taking the following steps on 2 October 2013:

(a) HMRC issued directions that Astral was not liable to pay the outstanding PAYE amounts in respect of the years 2010-11 and 2011-12, under regulation 72 of the Income Tax (Pay As You Earn) Regulations 2003 ("the PAYE Regulations"). The effect of those directions was to render Mr West liable to pay those amounts.

(b) HMRC made decisions that Mr West was liable to pay the primary Class 1 NICs not paid by Astral, under regulation 86 of the Social Security (Contributions) Regulations 2001 ("the NIC Regulations") and section 8(1)(c) of the Social Security Contributions (Transfer of Functions) Act 1999 ("SSC(TF)A").

(c) In relation to income tax, for 2010-11 HMRC issued an assessment, and for 2011-12 they issued a closure notice amending Mr West's self-assessment for that year.

12. The amounts for which Mr West became liable as a result of those steps can be summarised as follows:

Year	**Earnings**	**PAYE**	**NICs**
2010-11	£59,413	£16,285.60	£4,352.98
2011-12	£69,737	£20,863.80	£4,775.24
Totals	£129,150	£37,149.40	£9,128.22

13. The earnings figure employed by HMRC was not the gross amount of the director's remuneration shown in the draft management accounts, but the net amount, after deduction of PAYE and NICs, which had extinguished Mr West's Loan Account. That arose following certain correspondence between HMRC and Mr West, as a result of which HMRC had written to Mr West stating that they were prepared to recalculate the PAYE liability by treating as his income the amount of the repayment of his Loan Account of £129,150 rather than the figure for director's remuneration in the draft management accounts of £202,976.

14. We should also note that the steps taken by HMRC at the relevant time resulted in additional tax being payable (subject to Mr West's appeal) for both 2010-11 and 2011-12. As recorded by the FTT at [38], HMRC did not pursue an argument that there was a failure to operate PAYE during 2010-11. HMRC's position both before the FTT and in this appeal is that deduction and payment should have been made wholly in 2011-12, when the credit was made to Mr West's Loan Account.

The legislation

Income tax

15. Under the PAYE system, the employer is liable to deduct tax in accordance with regulation 21(1) of the PAYE Regulations:

> "On making a relevant payment to an employee during a tax year, an employer must deduct or repay tax in accordance with these Regulations by reference to the employee's code, if the employer has one for the employee."

16. The employer is then liable to account to HMRC for those deducted amounts (regulation 68 of the PAYE Regulations).

17. A "relevant payment" is defined, by regulation 4 of the PAYE Regulations, subject to certain exceptions which do not apply in this case, to mean a payment of, or on account of, net PAYE income. Net PAYE income is, in the circumstances of this appeal, the same as PAYE income (there are no relevant deductions as provided for by regulation 3). PAYE income is defined by section 683 of the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA") relevantly to include PAYE employment income, namely any taxable earnings from an employment determined in accordance with section 10(2) of ITEPA. In the case of a UK resident employee, the full amount of any general earnings which are received in a tax year is an amount of taxable earnings from the employment in that year (section 15(2) of ITEPA).

18. The meaning of "payment" for the purposes of the PAYE Regulations is given by section 686 of ITEPA:

> "(1) For the purposes of PAYE regulations, a payment of, or on account of, PAYE income of a person is treated as made at the earliest of the following times—
>
> *Rule 1*

The time when the payment is made.

Rule 2

The time when the person becomes entitled to the payment.

Rule 3

If the person is a director of a company and the income is income from employment with the company (whether or not as director), whichever is the earliest of—

(a) the time when sums on account of the income 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 income for a period is determined before the period ends, the time when the period ends;

(c) if the amount of the income for a period is not determined until after the period has ended, the time when the amount is determined.

…

(2) Rule 3 applies if the person is a director of the company at any time in the tax year in which the time mentioned falls.

(3) In this section "director" means—

(a) in relation to a company whose affairs are managed by a board of directors or similar body, a member of that board or body,

(b) in relation to a company whose affairs are managed by a single director or other person, that director or person, and

(c) in relation to a company whose affairs are managed by the members themselves, a member of the company,

and includes any person in accordance with whose directions or instructions the company's directors (as defined above) are accustomed to act.

(4) For the purposes of subsection (3) a person is not regarded as a person in accordance with whose directions or instructions the company's directors are accustomed to act merely because the directors act on advice given by that person in a professional capacity."

19. Section 686 effectively mirrors section 18 ITEPA, which provides corresponding rules to establish when general earnings are treated as received so as to be taxable earnings for a particular tax year by virtue of section 15(2).

20. The personal tax return of an individual is required, by section 9 of the Taxes Management Act 1970 ("TMA"), to include a self-assessment, including an assessment of the amount the individual is chargeable to income tax for the year of assessment. Payments on account of income tax are credited by section 59B(1) TMA. As regards PAYE, provision for adjusting the total net tax deducted, and thus the amount of the credit, is made by regulation 185 of the PAYE Regulations, which

includes an adjustment to the actual total net tax deducted in the case of tax treated as deducted, as follows:

> "(1) This regulation applies for the purpose of determining—
>
> …
>
> (b) the difference mentioned in section 59B(1) of TMA (payments of income tax and capital gains tax: difference between tax contained in self-assessment and aggregate of payments on account or deducted at source),
>
> …
>
> (2) For those purposes, the amount of income tax deducted at source under these Regulations is the total net tax deducted during the relevant tax year ("A") after making any additions or subtractions required by paragraphs (3) to (5).
>
> …
>
> (5) Add to A any tax treated as deducted, other than any direction tax, but—
>
> (a) only if there would be an amount payable by the taxpayer under section 59B(1) of TMA on the assumption that there are no payments on account and no addition to A under this paragraph, and then
>
> (b) only to a maximum of that amount.
>
> (6) In this regulation—
>
> "direction tax" means any amount of tax which is the subject of a direction made under regulation 72(5), regulation 72F or regulation 81(4) in relation to the taxpayer in respect of one or more tax periods falling within the relevant tax year;
>
> "relevant tax year" means—
>
> …
>
> (b) in relation to section 59B(1) of TMA, the tax year for which the self-assessment referred to in that subsection is made;
>
> …
>
> "tax treated as deducted" means any tax which in relation to relevant payments made by an employer to the taxpayer in the relevant tax year—
>
> (a) the employer was liable to deduct from payments but failed to do so, or
>
> …
>
> "the taxpayer" means … the person whose self-assessment is referred to in section 59B(1) of TMA (as the case may be)."

21. It is thus the case that the creditable tax under section 59B(1) TMA generally includes PAYE tax which the employer was liable to deduct under the PAYE

Regulations whether or not the employer has in fact deducted that tax. But this is subject to a number of exceptions for certain amounts of PAYE, collectively referred to as "direction tax". One such exception is that which HMRC applied in this case, namely regulation 72 of the PAYE Regulations, which relevantly provides:

> "(1) This regulation applies if—
>
> (a) it appears to the Inland Revenue that the deductible amount exceeds the amount actually deducted, and
>
> (b) condition A or B is met.
>
> (2) In this regulation …
>
> "the deductible amount" is the amount which an employer was liable to deduct from relevant payments made to an employee in a tax period;
>
> "the amount actually deducted" is the amount actually deducted by the employer from relevant payments made to that employee during that tax period;
>
> "the excess" means the amount by which the deductible amount exceeds the amount actually deducted.
>
> …
>
> (4) Condition B is that the Inland Revenue are of the opinion that the employee has received relevant payments knowing that the employer wilfully failed to deduct the amount of tax which should have been deducted from those payments.
>
> (5) The Inland Revenue may direct that the employer is not liable to pay the excess to the Inland Revenue.
>
> (5A) Any direction under paragraph (5) must be made by notice ("the direction notice"), stating the date the notice was issued, to—
>
> …
>
> (b) the employee if condition B is met.
>
> …
>
> (6) If a direction is made, the excess must not be added under regulation 185(5) or 188(3)(a) (adjustments to total net tax deducted for self-assessments and other assessments) in relation to the employee.
>
> …"

22. If a valid direction is given under regulation 72, under the self-assessment system the employee will not be entitled to credit for the amount which should have been, but was not, deducted by the employer. The employee will accordingly be liable for income tax on the taxable earnings without the benefit of that tax credit.

23. The employee has two rights of appeal in this respect. The first, by regulation 72C of the PAYE Regulations, is an appeal against a direction notice under regulation 72(5A), namely when condition B in regulation 72(4) is met:

"(1) An employee may appeal against a direction notice under regulation 72(5A)(b)—

(a) by notice to the Inland Revenue,

(b) within 30 days of the issue of the direction notice,

(c) specifying the grounds of the appeal.

(2) For the purpose of paragraph (1) the grounds of appeal are that—

(a) the employee did not receive the payments knowing that the employer wilfully failed to deduct the amount of tax which should have been deducted from those payments, or

(b) the excess is incorrect.

(3) On an appeal under paragraph (1) that is notified to the tribunal, the tribunal may—

(a) if it appears that the direction notice should not have been made, set aside the direction notice; or

(b) if it appears that the excess specified in the direction notice is incorrect, increase or reduce the excess specified in the notice accordingly."

24. The second, and corresponding, avenue of appeal is against an assessment or amendment to a self-assessment under section 31 TMA. The powers of the FTT on such an appeal are set out in section 50 TMA as follows:

"(6) If, on an appeal notified to the tribunal, the tribunal decides—

(a) that the appellant is overcharged by a self-assessment;

…

(c) that the appellant is overcharged by an assessment other than a self-assessment,

the assessment or amounts shall be reduced accordingly, but otherwise the assessment or statement shall stand good.

(7) If, on an appeal notified to the tribunal, the tribunal decides

(a) that the appellant is undercharged to tax by a self-assessment

…

(c) that the appellant is undercharged by an assessment other than a self-assessment,

the assessment or amounts shall be increased accordingly."

National insurance contributions

25. Class 1 NICs are divided into primary Class 1 contributions and secondary Class 1 contributions (see section 1 of the Social Security Contributions and Benefits Act 1992 ("SSCBA")). In both cases such contributions are payable when, in any tax week, earnings are paid to or for the benefit of an earner in respect of an employment of his (section 6(1) SSCBA). The term "earnings" includes any remuneration or

profit derived from an employment, and "earner" is construed accordingly (section 3(1) SSCBA). Earnings-related contributions are calculated by reference to the gross earnings from the employment in question (regulation 24 of the NIC Regulations).

26. Primary contributions are the liability of the earner (section 6(4)(a) SSCBA), but that is subject to paragraph 3 of Schedule 1 SSCBA, under which the secondary contributor, normally the employer, is liable in the first instance to pay the earner's primary contribution, and the liability of the earner is excluded.

27. Paragraph 3(1) of schedule 1 to the SSCBA provides:

> "(1) Where earnings are paid to an employed earner and in respect of that payment liability arises for primary and secondary Class 1 contributions, the secondary contributor shall (except in prescribed circumstances), as well as being liable for any secondary contribution of his own, be liable in the first instance to pay also the earner's primary contribution or a prescribed part of the earner's primary contribution, on behalf of and to the exclusion of the earner; and for the purposes of this Act and the Administration Act contributions paid by the secondary contributor on behalf of the earner shall be taken to be contributions paid by the earner."

28. Paragraph 3(1) of Schedule 1 SSCBA does not, however, apply and the earner's liability for primary Class 1 contributions is consequently not excluded, if regulation 86 of the NIC Regulations applies. Regulation 86 relevantly provides:

> "(1) As respects any employed earner's employment—
>
> (a) where there has been a failure to pay any primary contribution which a secondary contributor is, or but for the provisions of this regulation would be, liable to pay on behalf of the earner and
>
> …
>
> (ii) it is shown to the satisfaction of an officer of the Board that the earner knows that the secondary contributor has wilfully failed to pay the primary contribution which the secondary contributor was liable to pay on behalf of the earner and has not recovered that primary contribution from the earner;
>
> …
>
> the provisions of paragraph 3(1) of Schedule 1 to the Act (method of paying Class 1 contributions) shall not apply in relation to that contribution.
>
> …"

29. Regulation 86 can apply only in relation to a failure to pay a primary contribution where the secondary contributor "has not recovered that primary contribution". The only means whereby such a contribution may be so recovered is by a deduction from earnings (paragraph 6 of Schedule 4 to the NIC Regulations).

30. Where there has been no deduction from earnings, and the conditions in paragraph 86 of the NIC Regulations are met, the earner will be liable to pay the

primary Class 1 contributions. The earner has a right of appeal against a decision of HMRC in that respect. The decision is one to which section 8(1)(c) SSC(TF)A applies, and the right of appeal arises by virtue of section 11 of that Act. The FTT's jurisdiction is set out in regulation 10 of the Social Security Contributions (Decisions and Appeals) Regulations 1999 ("the NIC Decisions and Appeals Regulations"):

> "If, on an appeal under Part II of the [SSC(TF)A] … that is notified to the tribunal, it appears to the tribunal that the decision should be varied in a particular manner, the decision shall be varied in that manner, but otherwise shall stand good."

The FTT's decision

31. As we have noted, the decision of the FTT was not unanimous. In those circumstances, by article 8 of the First-tier Tribunal and Upper Tribunal (Composition of Tribunal) Order 2008, it fell to Judge Clark, as the presiding member, to exercise a casting vote. Having done so, it is his decision that is the subject of HMRC's appeal.

32. We shall examine Judge Clark's reasoning in more detail below, but by way of introduction we can summarise the FTT's decision quite shortly.

33. Dealing first with income tax, Judge Clark accepted (and indeed it was common ground) that in order to determine whether regulation 72 of the PAYE Regulations applied, there were three issues to be considered. Only if HMRC could succeed in their arguments on all three would Mr West be liable to the income tax charge. The three issues were:

> (a) On making the relevant payment, did Astral deduct the amount of tax which it should have deducted?
>
> (b) If not, was Astral's failure to deduct wilful?
>
> (c) If so, did Mr West receive the relevant payment knowing that Astral had wilfully failed to deduct?

34. Judge Clark decided, in relation to the first issue, that Astral had deducted tax in accordance with the PAYE Regulations. Accordingly, he did not need to reach any conclusion on the second and third issues.

35. On the question whether Astral had deducted tax, Judge Clark had regard, in particular, to the draft management accounts for the relevant period which had been approved and signed by Mr West. Those accounts showed, first, in the detailed trading and profit and loss account for the period, the gross amount of the director's remuneration (£202,976) and the employer's NICs, and secondly, under the heading "Creditors", an entry for "Tax and NIC" for the 2011 period (£99,886). Judge Clark found, at [69], that Mr West's approval of those accounts and his subsequent use of them as the basis for the instructions to the liquidators, amounted to confirmation of the voting of the gross amount of director's remuneration as shown.

36. Judge Clark found support for the payment of remuneration and the acknowledgement of the consequent indebtedness to HMRC from the signed form

P35 for 2011-12, and the evidence given regarding the submission of a supplementary form P35 for 2010-11 showing a liability for PAYE and employer's NICs. He was satisfied that the indebtedness acknowledged in this way resulted from the deduction of tax from the grossed-up amount of remuneration for the relevant period (FTT at [70]). On that basis, Judge Clark held, at [71], that tax had been deducted from the remuneration provided by Astral to Mr West. The judge distinguished *R v Inland Revenue Commissioners, ex parte McVeigh* [1996] STC 91 ("*McVeigh*"), on which HMRC had relied. As he had held that the first pre-condition to the operation of regulation 72 was not satisfied, Judge Clark held at [72] that there was no basis for transferring Astral's liability to account for income tax under PAYE to Mr West.

37. As regards NICs, Judge Clark noted that the question to be considered in relation to regulation 86 of the NIC Regulations was different from that raised in relation to PAYE. The question did not concern wilful failure to deduct, but whether there was a wilful failure on the part of Astral to pay the primary Class 1 contributions, and if so whether Mr West knew that Astral had wilfully failed to pay those contributions.

38. It was clear that there had been no such payment. However, Judge Clark found, at [91], that Astral's failure to pay was not wilful, since at the time the liability arose Astral was not in a position to pay the resulting NICs to HMRC. Accordingly, the relevant condition in regulation 86 had not been fulfilled, and Astral's liability to pay the NICs could not be transferred to Mr West.

39. Ms O'Neill, dissenting, contrasted the position of Astral with that of a struggling and ongoing company where there was a reasonable belief that the company would be able to meet its liability to HMRC when due. She concluded, at [97], that in Astral's case the bookkeeping entries in relation to the deduction of PAYE and NICs on the gross remuneration of £202,976 were entirely notional, and that they had no substance in reality. Ms O'Neill went on to conclude that, by creating an obligation to deduct tax (and pay NICs) which Mr West (and thus Astral itself) knew could not be paid to HMRC, Astral had wilfully failed to discharge those obligations, and it had done so in the knowledge of, and indeed at the instigation of, Mr West.

Discussion

40. We take the same approach as the FTT to the income tax questions. We will, therefore, address first whether Astral deducted tax on making the relevant payment, and then go on to consider whether any failure to deduct was wilful on Astral's part and, if it was, whether Mr West knew that to be the case when he received the relevant payment. Before addressing those questions, however, we should deal in a little more detail with the important decision in *McVeigh*.

McVeigh

41. *McVeigh* was the case relied upon by HMRC, both before the FTT and before us, in relation to the question whether, for PAYE purposes, Astral had made a deduction of the relevant amount of tax. That judgment, as we have described, was distinguished by Judge Clark, who did not adopt its reasoning.

42. *McVeigh* came before May J in the High Court on a judicial review of the decision of HMRC to make a direction under what was then regulation 42 of the Income Tax (Employment) Regulations 1993 ("the 1993 Regulations") that the employee pay personally the tax which his employer had failed to deduct. *McVeigh* was dealt with in that way because, at that time, there was no right of appeal to a tribunal against such a direction.

43. *McVeigh* concerned certain bonuses which had been voted by a company in favour of one of its directors, Mr McVeigh. In each case an amount, described as a "net bonus", and representing the gross bonus less tax and NICs, was credited to Mr McVeigh's director's loan account. Amounts of PAYE and NICs referable to the bonuses were recorded in a ledger headed "Director's bonus account (PAYE/NIC)". The accounts were signed by the directors. The company did not account to the Inland Revenue for the PAYE tax or the NICs, and Mr McVeigh did not declare the bonuses in his personal tax returns. The Inland Revenue made a determination obliging the company to pay the tax, but the company, which was then in liquidation, did not do so. The Revenue then made a direction under regulation 42 of the 1993 Regulations, directing Mr McVeigh to pay the tax. Mr McVeigh sought judicial review of that direction.

44. The relevant conditions under regulation 42 of the 1993 Regulations were in substance the same as those at issue in this appeal as regards PAYE, namely whether the employer had failed to deduct the amount of tax which he was liable to deduct under the 1993 Regulations, whether he had failed to do so wilfully, and whether the employee had received the emoluments knowing of the wilful failure to deduct.

45. On the question whether there had been a failure to deduct, and having first concluded that deduction of tax is not the same as payment of tax, May J referred, at pages 98f – 99a, to what he described as the "usual circumstances":

> "It is clear that the usual circumstances where these provisions may apply will be where an employee has received a payment gross and there will have been no deduction of tax because the payment was made gross. If, on the other hand, the employee is paid net, he or she will normally receive a document required by employment legislation, but not by tax legislation, indicating how the net amount is calculated. In the modern world the fact of payment in an amount net of tax will normally constitute deduction, whether or not the employer also effects any money movement of the sum which is deducted, for example by transferring it to a tax reserve. There will be a pre-existing entitlement to gross pay and a deduction from this is effected by paying the net amount due after subtracting the tax. This accords with reg 14, where

> the employer has to ascertain, among other things, the tax and to deduct it 'on making the payment in question'.
>
> Regulations 49(5) and 42(3) would normally operate where the employer had wilfully paid an employee gross and the employee knew this. Although the employer has to prepare a deductions working sheet under reg 38, the preparation of that sheet does not, in these normal circumstances, constitute or contribute to the making of the deduction. It is, as the regulation makes clear, the making of a record and one of the things that has to be recorded is 'the amount of tax, (if any), deducted or repaid on making the payment' (see reg 38(3)(c), which is one of a number of instances where the point of deduction appears to be on making the payment). Again, although the employer is required to give a P60 certificate to the employee and to provide the Revenue with forms P14 and P35, the giving and providing of those documents does not constitute the deduction of tax. The documents record among other things the deduction of tax."

46. May J then drew a distinction between the normal case and the position in *McVeigh*. He described those circumstances as having the following features: (a) there was no actual payment of money; there was at most, at the relevant time, bookkeeping and accounting, (b) there was no pre-existing entitlement to a gross sum from which calculated tax was deducted upon payment to reach the net sum paid; instead there was a grossing-up calculation to produce, after deduction of tax and NICs, an amount approximately equal to the debit balance on the loan account, and (c) the grossed-up amount was then declared as a bonus and the bookkeeping entries were made.

47. At that point, May J described the "crucial question" as follows:

> "In my judgment in this case the crucial question whether the employer deducted the amount of tax which he was liable to deduct under the 1993 regulations cannot be determined by what I have described as 'normal considerations', for the simple reason that on the date when payment is to be treated as having been made no actual payment was in fact made. There was, accordingly, no deduction in the normal sense of a deduction constituted by the payment of a net sum against a pre-existing entitlement to gross pay".

48. May J then recorded that Mr McVeigh had argued that the inclusion of the tax liability within the creditors in the accounts, the entering of the amounts net of deductions in the loan account ledger and the entering of the deductions in the other ledger constituted the crediting of Mr McVeigh with amounts net of tax and the setting aside (in the sense of accounting for) the tax. Taken together, it was submitted, these actions constituted deduction.

49. That argument was rejected by May J in these terms at page 99g-j:

> "Those matters would no doubt contribute to a deduction of tax if, additionally, the tax was accounted for and paid. But in this case the employer, to Mr McVeigh's knowledge, has neither accounted for nor paid the tax and these failures were wilful, or so the Revenue have concluded upon a basis which was, in my judgment, not perverse. In

> these circumstances I consider that it would be a misuse of language to say that the bookkeeping and accounting alone, without actual payment, and without any of the procedures which the 1993 regulations require, constituted a deduction of tax from the gross payment. There was, on the contrary, a wilful failure to do anything relating to tax obligations, beyond making some internal paper entries which the company proceeded to ignore for tax accounting purposes and which Mr McVeigh also ignored when he submitted his own tax returns. That, in substance, is what, according to Mr Shortland's affidavit, the Revenue decided in making their direction. In my judgment there was no deduction of tax by the company, and the direction of 12 September 1994, which is challenged, was a sustainable direction in law and in fact."

May J held as a matter of law that there was, in those factual circumstances, no deduction of tax by the company.

Mr West's arguments on income tax

50. Mr Slater sought to uphold Judge Clark's approach to *McVeigh*. Judge Clark said this at [82] – [83] of the FTT decision:

> "[82] In *McVeigh*, May J stressed the abnormality of the circumstances under consideration. His comments must therefore be read in that context. It is apparent from the report of the case in Simon's Tax Cases that one of the cases mentioned in the skeleton argument for Mr McVeigh was [*Garforth (Inspector of Taxes) v Newsmith Stainless Ltd* [1979] STC 129]. That case confirmed that putting money unreservedly at the disposal of a director amounted to payment. Thus May J was aware of that principle (subsequently confirmed by s 686 ITEPA 2003, as set out above). He found that on the relevant date, no actual payment was in fact made. It followed from that finding that there was no deduction.
>
> [83] I am satisfied that, contrary to the position in *McVeigh*, there was a payment when the remuneration was allocated to Mr West and set off against the amount outstanding on the director's loan account. I am further satisfied that deduction of tax was made in Astral's case as part of the process of producing the draft Management Accounts, with the result that those accounts contained an acknowledgment of the indebtedness to HMRC in respect of the amounts due under PAYE. I do not consider that the principles in *McVeigh* relating to circumstances described as other than normal apply in Mr West's case."

51. Mr Slater sought also, as Judge Clark had done, to distinguish the facts in *McVeigh* from the facts of this case. He pointed out that, whereas in *McVeigh* the company's accountants had informed HMRC that the bonuses had not been "processed under PAYE", in this case all the PAYE procedures had been followed, as Judge Clark had found at [81]. In *McVeigh*, the accountants did not provide a calculation showing the specific tax and NICs that had been deducted; in this case such a calculation was made. In this case, unlike in *McVeigh*, annual end of year

returns (forms P35) were prepared, signed by Mr West as director, and filed with HMRC. Also, in this case, the gross remuneration and tax deducted were entered in Mr West's personal tax return, which was signed by him, and Mr West gave evidence of his belief that PAYE had been deducted.

Did Astral deduct income tax?

52. By way of introduction, we should make two points.

53. First, we should make clear that we are not bound by *McVeigh*, which was a judgment of the High Court (see *Secretary of State for Justice v B* [2010] UKUT 454 (AAC) and *Revenue and Customs Commissioners v Noor* [2013] STC 998). We should not, however, depart from such a decision except in circumstances where another High Court judge could properly do so. Essentially, we should do so only if we are convinced or satisfied that the decision of the High Court was wrong (see *Gilchrist v Revenue and Customs Commissioners* [2014] UKUT 169 (TCC); [2015] Ch. 183, at [84]).

54. Secondly, in considering *McVeigh*, it seems to us that Mr Slater was wrong to submit that it was a decision on its own facts, and that May J's view on whether tax had been deducted was not a decision on a point of law. In our judgment, even though *McVeigh* was a judicial review and followed a different procedural route to that adopted in this case, May J was deciding, as a matter of law, that there was there a failure to deduct tax. May J's observations were not, therefore, *obiter dicta*.

55. With those points in mind, there are essentially three reasons why we have concluded that the *ratio* of *McVeigh* is applicable in this case, that we should follow *McVeigh*, and that Judge Clark was wrong not to do so.

56. Our first reason is that we do not regard the distinctions between the facts of this case and those in *McVeigh* as of particular significance. There are a number of more important similarities between the cases. Both cases involved the voting of a gross amount of remuneration to which the director had no pre-existing entitlement. The amount of that remuneration in each case was set so that, after deduction of tax and NICs, it would equal, or approximately equal, the amount outstanding and due to the company on a director's loan account. Both involved the crediting of that amount to the loan account. Both involved the making of appropriate ledger entries, both as to the loan account and tax, in the company's accounts. Crucially, in neither case was tax actually paid to HMRC.

57. The additional calculations and documents prepared in this case, to which Mr Slater has directed our attention, were simply more of the same as compared with what happened in *McVeigh*. They were, as May J described them in *McVeigh*, just "bookkeeping and accounting". This applies as much to the PAYE procedures, the accountants' calculation showing the specific tax and NICs that had been deducted, and the end of year returns in form P35, as it does to the entry of the gross remuneration and tax deducted in Mr West's personal tax return.

58. Our second reason is that the *ratio* of *McVeigh* was not about the detail of the accounting or record-keeping procedures undertaken by the company or the individual director, but about the essential nature of the transaction that was being undertaken. May J said that the crucial question of whether the employer deducted the tax could not be determined by what he described as "normal considerations", because "on the date when payment [was] to be treated as having been made no actual payment was in fact made" so that "there was … no deduction in the normal sense of a deduction constituted by the payment of a net sum against a pre-existing entitlement to gross pay". May J went on to explain that "it would be a misuse of language to say that the bookkeeping and accounting alone, without actual payment, and without any of the procedures which the 1993 regulations require, constituted a deduction of tax from the gross payment". Of course, he understood that the concept of "deduction" was different from the concept of "payment"; he had said so at page 98f of his judgment. But his point was that where there was a "wilful failure to do anything relating to tax obligations, beyond making some internal paper entries", it could not properly be held that a deduction of tax had been made. It is true also that May J referred specifically to "internal paper entries" and "the procedures which the … regulations require", but in our view, for the reasons we have already partly given, the fact that some "external paper entries" may be made or some regulatory procedures complied with, as they were here, cannot change the position. In both *McVeigh* and in this case, the crucial stark realities were that: (a) when the gross remuneration was voted, the employee had no pre-existing entitlement to it, (b) the remuneration was set so as to eliminate the director's loan account, and (c) most importantly, there was never from start to finish any possibility of the tax actually being paid. In such circumstances, as it seems to us, as a matter of law, no amount of "bookkeeping and accounting" or other "making of a record" can amount to a true deduction of tax.

59. Our third reason for our conclusion on this point is that we think that Judge Clark misunderstood *McVeigh*, and distinguished it on a false premise at [83] of the FTT's decision. Judge Clark seems to have thought that May J found that there had been no actual payment of the net remuneration to Mr McVeigh. In fact, however, there is no proper distinction between this case and *McVeigh* as regards payment in respect either of the remuneration itself or the tax. In each case the crediting of the remuneration to the director's loan account is properly to be regarded as payment, and in each case there were book entries regarding the liability of the company to tax (and NICs), but no actual payment of that tax to HMRC.

60. For these reasons, we have concluded that, on the making of the relevant payment, Astral did not deduct the amount of tax which should have been deducted.

Was Astral's failure to deduct tax wilful, and, if so, did Mr West know that it was?

61. It is convenient to deal with these two questions together. As Mr West was the sole director of Astral, it is his actions, intentions and awareness that fall to be ascribed to the company. We can accordingly consider both questions effectively from the perspective of Mr West alone.

62. Mr Slater argued that Astral could not have deliberately failed to deduct PAYE, and Mr West could not have known that the company had deliberately failed to deduct the tax, because Mr West himself believed that the company had deducted tax. Mr West's belief, Mr Slater submitted, and we accept, is a purely subjective question. As May J put it in *McVeigh*, at page 96d, referring to *R v IRC, ex p Chisholm* [1981] STC 253, "… 'knowing' means knowing, not 'ought to have known' and 'wilfully means 'intentionally or deliberately'."

63. What Mr Slater is essentially arguing is that because Mr West believed that, as a matter of law, what Astral had done amounted to a deduction of tax, neither Astral could be said to have deliberately failed to deduct the tax nor could it be said that Mr West himself knew of such a wilful failure.

64. That, in our judgment, is not the correct approach to questions of this nature. For a person wilfully to effect a particular legal outcome, it is not necessary for that person to be cognisant of the legal consequences of his or her actions. It is necessary only for that person intentionally or deliberately to put in train the various actions (or knowingly to fail to do so in the case of omissions) that in the event have the material consequences in law.

65. Mr Slater placed some reliance on Mr West having relied on professional advice in order, as he put it, to "do the right thing". That did not, however, affect Mr West's knowledge as to (a) the mechanics of the creation of the remuneration in his favour, (b) its calculation as a gross amount which, after deduction of tax and NICs, would equal the amount he owed to the company on his Loan Account, (c) the crediting of the relevant amounts in the company's accounts to both his Loan Account and to a creditor's account in respect of tax and NICs, and (d) the making of the various corporate and personal tax returns. Crucially, it did not affect the accepted fact that Mr West knew all along that, notwithstanding the acknowledgement of the indebtedness of the company to HMRC in respect of the tax and NICs purportedly deducted, no actual payment of tax could or would ever be made.

66. Our conclusion is unaffected by the evidence that, at the material time, Mr West had been under the impression that, in any event, he would have to pay the outstanding tax and NICs. We accept that Mr West did not deliberately set out to avoid a tax liability on the salary voted in his favour. We accept that he was at the relevant time unaware of the fact that his own liability to tax would depend on the application of regulation 72 of the PAYE Regulations, and that he could not be regarded as manipulating events so as to avoid the application of that regulation. But such intentions are not conditions that need to be met. What matters is whether Mr West (as the guiding mind of Astral) intentionally failed to deduct tax, and whether he knew that that had happened. His knowledge of the factual matters we have mentioned above must be sufficient to satisfy both those conditions. The fact that Mr West may not, or even probably did not, know that those facts meant that, as a matter of law, a deduction had not been made is not a relevant matter. He is to be taken to intend the legal consequences of his deliberate actions.

NICs

67. As we have explained above, regulation 86 of the NIC Regulations can apply only if there has been no deduction of the primary contributions from the relevant earnings, as such a deduction would operate as a recovery of those contributions from the employee. That requires the same analysis as we have carried out in relation to the income tax issue, and the question of deduction of PAYE. The same analysis gives rise to the same conclusion. For the reasons we have given, we conclude that as a matter of law Astral made no deduction of primary contributions in relation to the relevant earnings of Mr West.

68. It is common ground that Astral did not pay the NICs to HMRC. The only questions for the purpose of regulation 86 are whether the failure to pay was wilful on the part of Astral and whether Mr West knew that. Again, for the reasons we have given above in relation to the PAYE question, we are satisfied that, by paying an amount to Mr West (through credit against Mr West's liability to the company on his Loan Account), Astral deliberately created a debt to HMRC, knowing that it would be unable to pay that debt. In those circumstances, Astral's failure to pay the NICs was wilful. Mr West, as the directing mind of Astral, knew that.

69. In our judgment, Judge Clark was wrong to decide at [91] that Astral's failure to make payment of the NICs was not wilful, on the basis that at the time the liability arose Astral was not in a position to pay. Mr West, and therefore, Astral, knew all the material facts that we have mentioned at paragraph 65 above.

70. We conclude, therefore, that the conditions of regulation 86(1)(a) of the NIC Regulations have been met, and that accordingly paragraph 3(1) of Schedule 1 to the SSCBA does not apply. The consequence is that Mr West is liable for the NICs.

Determination

71. In those circumstances, HMRC's appeal must be allowed, and the decision of the FTT (arrived at by the casting vote of Judge Clark) must be set aside.

Should the amounts of income tax and NICs due in respect of 2011-12 be increased to reflect Mr West's gross earnings of £202,976?

72. Ordinarily, on the setting aside of the FTT's decision on an appeal by HMRC, the consequence would simply be that the assessment and the amendment made by HMRC to Mr West's self-assessment for the relevant years and the decisions in relation to NICs would be confirmed. There are, however, in this case two further issues to consider.

73. The first is that, on any basis, the tax assessment and amendment and the NICs decisions do not reflect the true position. The original tax assessment and amendment and the original NICs decisions were made on the basis that Mr West's drawings from his Loan Account were earnings from which no PAYE or NICs had been deducted. That was not correct. As the FTT recorded at [38], HMRC accept that those drawings were loans and not payments on account of remuneration. Relevant earnings arose

only in the period 2011-12, when the actions taken by Astral and Mr West described in this decision took place. It is, accordingly, only the period 2011-12 with which we are concerned. That requires a variation in any event to the tax assessment and amendment and to the NICs decisions.

74. The second issue is more fundamental. As part of their case on this appeal, HMRC have submitted that the amounts of income tax and NICs due in respect of 2011-12 should be increased to reflect Mr West's gross earnings of £202,976, by virtue of the FTT's powers in regulation 72C of the PAYE Regulations, section 50(7) of TMA, and regulation 10 of the NIC Decisions and Appeals Regulations. In re-making the decision of the FTT, we have those same powers by virtue of section 12(4)(a) of the Tribunals, Courts and Enforcement Act 2007.

75. In seeking to determine the correct amount of tax in this case, we raised with the parties during the hearing the question of the effect (if any) of any part of the voting of the remuneration in favour of Mr West being *ultra vires* the company. Our concern was whether, in the circumstances of this case, the ascertainment of an amount of remuneration by the company on a gross basis in order, after deduction of tax and NICs, to arrive at a net figure equal to a liability of a director to the company, could be a genuine exercise of the company's power to award remuneration, or was instead a disguised gift of capital, according to the principles explained in *Re Halt Garage (1964) Ltd* [1982] 3 All ER 1016 ("*Halt Garage*"). We invited the parties to make written submissions on that question, which they duly produced.

76. As a general matter, tax on earnings is chargeable on a receipts basis. As we described above, in the case of a UK resident employee, the full amount of any general earnings which are received in a tax year is an amount of taxable earnings from the employment in that year (section 15(2) ITEPA). Section 18 ITEPA provides, in a manner similar to section 686 ITEPA in relation to the meaning of "payment" for the purpose of the PAYE Regulations, for when general earnings are treated as received:

> "(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—
>
> *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.
>
> *Rule 3*
>
> If the employee is a director of a company and the earnings are from employment with the company (whether or not as director), whichever is the earliest of—

(a) the time when 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;

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

(2) Rule 3 applies if the employee is a director of the company at any time in the tax year in which the time mentioned falls.

(3) In this section "director" means—

(a) in relation to a company whose affairs are managed by a board of directors or similar body, a member of that body,

(b) in relation to a company whose affairs are managed by a single director or similar person, that director or person, and

(c) in relation to a company whose affairs are managed by the members themselves, a member of the company,

and includes any person in accordance with whose directions or instructions the directors of the company (as defined above) are accustomed to act.

(4) For the purposes of subsection (3) a person is not to be regarded as a person in accordance with whose directions or instructions the directors of the company are accustomed to act merely because the directors act on advice given by that person in a professional capacity.

(5) Where this section applies—

(a) to a payment on account of general earnings, or

(b) to sums on account of general earnings,

it so applies for the purpose of determining the time when an amount of general earnings corresponding to the amount of that payment or those sums is to be treated as received for the purposes of this Chapter."

77. *Halt Garage* concerned payments of remuneration which were authorised by the shareholders unanimously. The shareholders, Mr and Mrs Charlesworth, were husband and wife, and they were also the only directors of the company. A claim was made by the company's liquidator for a declaration under section 333 of the Companies Act 1948 that the former directors were guilty of misfeasance and breach of trust in relation to the company misapplying money and assets of the company by paying excessive remuneration to the directors. The sums in question were weekly amounts paid from 1967 until the company was sold in March 1971. During the period in question, the company was making losses and the accounts in 1968-69 showed that the company was insolvent.

78. Having carried out an extensive review of the authorities, Oliver J concluded that the amount of remuneration is a matter for the management of the company to determine, and the court would not normally interfere. He said, at page 1039b-c:

> "… assuming that the sum is bona fide voted to be paid as remuneration, it seems to me that the amount, whether it be mean or generous, must be a matter of management for the company to determine in accordance with its constitution which expressly authorises payment for directors' services. Shareholders are required to be honest but … there is no requirement that they must be wise and it is not for the court to manage the company."

79. Having acknowledged that the label "remuneration" may not always be determinative, Oliver J went on to say, at page 1039f-g:

> "The real test must, I think, be whether the transaction in question was a genuine exercise of the power. The motive is more important than the label. Those who deal with a limited company do so on the basis that its affairs will be conducted in accordance with its constitution, one of the express incidents of which is that the directors may be paid remuneration. Subject to that, they are entitled to have the capital kept intact. They have to accept the shareholders' assessment of the scale of that remuneration, but they are entitled to assume that, whether liberal or illiberal, what is paid is genuinely remuneration and that the power is not used as a cloak for making payments out of capital to the shareholders as such."

80. Applying those tests, Oliver J concluded that the payments to Mr Charlesworth were a genuine exercise of the company's power to pay remuneration, and were not patently excessive or unreasonable. However, in the case of Mrs Charlesworth, having regard to her inactivity during the period in question, it could not be said that the amounts drawn by her were genuine awards of remuneration to her for holding the office of director. The part of her drawings in excess of what would have been a reasonable award was *ultra vires* the company and repayable to the liquidator.

81. In *Progress Property Co Ltd v Moorgath Group Ltd* [2010] UKSC 55 ("*Progress Property*"), at [19], Lord Walker summarised the effect of *Halt Garage* as follows:

> "… the case does show that if the label of remuneration does not square with the facts, the facts will prevail and the result may be an unlawful distribution, even if the directors in question intended no impropriety. Later in his judgment Oliver J recognized that, observing (at 1044) 'In the absence of any evidence of actual motive, the court must, I think, look at the matter objectively and apply the standard of reasonableness.' "

As in *Halt Garage,* an unlawful transaction of this kind is *ultra vires* (see also *Aveling Barford Ltd v Perion Ltd* [1989] BCLC 626 per Hoffmann J at page 631, and *Progress Property* per Lord Walker at [15]).

82. There is a distinction between a transaction which may be considered to be *ultra vires* in the narrow sense, and thus wholly void, and one which is *ultra vires* in the wider sense, which is capable of conferring rights on innocent third parties. The distinction was summarised by Browne-Wilkinson LJ in *Rolled Steel Products (Holdings) Ltd v British Steel Corporation* [1986] Ch 246 at page 302:

> "The judge drew a distinction between two meanings of *ultra vires* which he called the "narrow sense" and the "wider sense." As I understand his judgment, he treated *ultra vires* in the narrow sense as covering any transaction outside the express or implied powers of a company stated in its memorandum of association and *ultra vires* in the wider sense as covering a transaction which, although within such powers, is entered into in furtherance of 'some purpose which is not an authorised purpose': [1982] 1 Ch. 478, 497. Although it is not entirely clear, he appears to have treated transactions which are *ultra vires* in his narrow sense as being wholly void as opposed to those which are *ultra vires* in the wider sense, which are capable of conferring rights on third parties who have no notice of the invalidity: see p. 499. He then apparently held that the guarantee by the plaintiff was *ultra vires* in the wider sense and, since British Steel Corporation had notice of that fact, it was unenforceable by British Steel Corporation."

At page 304, Browne-Wilkinson LJ went further in suggesting that the term *ultra vires* was really only apt in cases where the acts in question were in excess of the capacity of the company, and that it should not include acts which were within the company's capacity but were wrongful, in the sense of being in excess or abuse of powers. But the practical distinction between the two, namely that only in the latter case may an innocent third party obtain rights, is the same. In *Progress Property*, at [15], Lord Walker described an unlawful return of capital as *ultra vires* in the "wider and looser sense of the term".

83. Ms Laura Poots, counsel for HMRC, submitted that, on the analysis in *Halt Garage*, the evidence indicated that the remuneration declared in favour of Mr West (the gross sum of £202,976) was not a genuine exercise of the company's power to pay remuneration and was therefore unlawful and incapable of being ratified by Mr West, the sole shareholder. The amount declared was significantly in excess of the salary amounts paid in prior years, and it was also significantly in excess of the dividends paid in earlier years. It does not, Ms Poots submits, appear to bear any relation to the value contributed by Mr West. Furthermore, as Ms Poots points out, it is clear that the amount of remuneration was calculated in order to clear Mr West's Loan Account, rather than to reward Mr West in line with the services that he had provided to the company. Finally, the remuneration was declared at a time when Astral was known by Mr West to be insolvent.

84. HMRC nonetheless submit that, absent a conclusion of this tribunal (or the FTT) that the voting of the remuneration was unlawful, the voting of the remuneration was a determination for the purposes of section 18 ITEPA (see section 18, Rules 3(b) and (c)), so that Mr West received earnings in the sum of £202,976.

85. Where HMRC wishes to assert that an assessment (including an amendment to a self-assessment) is to be increased by virtue of section 50(7) TMA, the burden is on them to show that the original assessment or amendment undercharges the taxpayer (see *Revenue and Customs Commissioners v C M Utilities Limited* [2017] UKUT 0305 (TCC), at [42]). In order to discharge that burden, it is accordingly for HMRC to show that the determination by Astral of the gross remuneration was a lawful determination, such that under Rule 3(b) or (c) of section 18 ITEPA it is the gross remuneration that should be treated as having been received by Mr West, and not, as the original assessment and amendment provided, the net amount actually received by Mr West.

86. Given Ms Poots' submissions regarding the lawfulness or unlawfulness of the declaration of gross remuneration in favour of Mr West, it is in our judgment not possible for HMRC to discharge that burden. We do not consider that, on the evidence available to the FTT and this tribunal, it is possible for it to be definitively concluded, in HMRC's favour, that there was a lawful determination of the gross amount of the remuneration, such that it is that gross amount of earnings that Mr West should be regarded as having received.

87. That leaves the question whether the net amount of the remuneration has been properly assessed, subject only to the whole amount being part of the amended self-assessment for 2011-12. HMRC's position on this is that, even if the voting of the remuneration were unlawful, it remains the case that Astral did make a payment of earnings to Mr West and credited a sum on account of those earnings in the company's books and records. That payment has not been avoided or otherwise set aside, and therefore Mr West received a payment of earnings in the net sum of £129,150.

88. Mr Slater submits, on the other hand, that the net remuneration is merely part of the gross; the three elements, namely the gross remuneration, the deduction and the resulting net amount, are wholly interconnected. The credits of the net remuneration to Mr West's account and the tax and NICs to a PAYE and NIC account are all elements of the gross remuneration. The net remuneration does not have an independent life of its own. It exists only because the gross remuneration exists. If that is void, so too is the net.

89. In contrast to the position where HMRC are seeking to increase an assessment or self-assessment under section 50(7) TMA, where the burden is on HMRC, in any case where the taxpayer is arguing for a reduction, the burden of proof is normally on the taxpayer. That is the effect of section 50(6) TMA which provides that, absent reduction on account of an assessment or self-assessment overcharging tax, "the assessment … shall stand good". The same applies to an appeal in respect of NICs; see regulation 10 of the NIC Decisions and Appeals Regulations.

90. In the same way that we have concluded that we cannot, on the evidence available, definitively conclude that there was a lawful determination by Astral of the gross amount of the remuneration, nor can we conclude in Mr West's favour that such

a determination was unlawful and void. In those circumstances, the tax assessments and NICs decisions must stand good.

91. However, we should add that, even if we had been in a position to conclude that there had been no lawful determination by Astral of the gross amount of the remuneration, we would nonetheless have concluded that the net amount of £129,150 did represent taxable earnings of Mr West, both for tax and NICs purposes.

92. As regards tax, having regard to the rules in section 18 ITEPA, it is clear to us that the crediting of the net sum to Mr West's Loan Account in discharge of his liability to Astral was a "payment of or on account of earnings" within Rule 1, or a sum on account of such earnings which was "credited in the company's accounts and records" within Rule 3(a). That is the case notwithstanding that there may have to be a repayment if invalidity were established. Such a contingency does not affect the deemed receipt by Mr West. If there were to be a repayment, that may give rise to questions of "negative earnings" (see *Martin v Revenue and Customs Commissioners* [2015] STC 478), but as Mr West has not repaid anything, and there has been no claim by the liquidator, such questions do not arise in this case.

93. As regards NICs, there is no equivalent to section 18 ITEPA. But we would in any event have concluded that there was a payment of earnings when Mr West's liability to Astral on his Loan Account was discharged by the credit for the net amount of £129,150, and that the amount of the earnings was that net sum. No movement of cash is required for there to be a payment (see *Garforth (Inspector of Taxes) v Newsmith Stainless Ltd* [1979] STC 129).

Decision

94. We allow HMRC's appeal and set aside the decision of the FTT.

95. We re-make that decision by determining that for the tax year 2011-12, the taxable earnings of Mr West for the purposes of income tax and NICs were £129,150. The assessment and decision for 2010-11 are reduced to nil, and the earnings subject to tax and NICs for the purpose of the self-assessment and the NICs decision for 2011-12 are increased to £129,150.

96. We understand that the parties will seek to agree on that basis the final figures for tax and NICs. In case of dispute in that respect, the parties have liberty to apply not later than one month after the date of release of this decision.

SIR GEOFFREY VOS, CHANCELLOR OF THE HIGH COURT
UPPER TRIBUNAL JUDGE ROGER BERNER

RELEASE DATE: 29 March 2018