

Personal Liability Notices for Directors (Lecture B1340 – 22.24 minutes)

The Social Security Administration Act 1992 was amended in 1998 to introduce a concept of personal liability for directors of companies which failed to pay NIC due.

HMRC may issue a “personal liability notice” (PLN) on any director (or other officer) of a company when the company has failed to pay contributions within the time allowed (not necessarily under circumstances of insolvency) where that failure to pay appears to be due to the fraud or neglect of individuals who were at the time of the failure to pay, officers of the company. In such a case the officer is referred to as a “culpable officer” (SSAA1992 s121C).

HMRC will issue the notice, taking into account the extent of the officer’s culpability in the company’s failure to pay, and may share the liability between more than one individual. If the company subsequently makes payment, then the liabilities shown on the notices are correspondingly reduced. Interest may be added to the contributions due by the company (which will include both primary and secondary contributions, and Classes 1A and 1B if appropriate) and will be included in the PLN.

The notice is issued following the company’s failure to pay by the due date, and not necessarily its inability to pay. However it is unlikely that HMRC would use this power if they had the option of pursuing the company for the funds.

Although the legislation provides for an “officer” to be personally liable for unpaid NIC’s, it is unlikely that a company secretary rather than a director would have the degree of control over the company’s affairs to be held responsible for the failure to pay

What are the indicators of neglect?

A review of appeal cases against PLN’s under s 121C indicates that HMRC generally pursues directors where there has been no attempt to make payment of PAYE and NIC and in particular where the individuals involved have been associated with companies which have previously gone insolvent owing HMRC substantial amounts of money.

It is worth noting that the number of appeal cases recorded recently has dropped to a very low level, probably indicating that the introduction of Real Time Information (RTI) for payroll allows HMRC to intervene much earlier when NIC is unpaid and thus the serious cases for which PLN’s have been issued in the past are not much in evidence.

Appeal case study : TC01130 Stephen Roberts and Alan Martin v HMRC

This appeal case concerned the Personal Liability Notices issued against the appellants which totalled £90,959 (each individual being issued with a notice for half of that amount) being the estimated unpaid NIC due by Innova Limited.

The company was incorporated in June 2007 and carried on business as a staff agency, providing staff to banks and other financial organisations, both as a recruitment consultant and the provider of staff (both employees of the company and sub-contractors).

Innova was a successor (phoenix) company to Synergi Global Solutions Limited, a company of which both the appellants were directors, and which operated the same business as Innova. Synergi went

into liquidation in July 2007 with PAYE, NIC and VAT debts of about £165,305 of which £103,733.07 was attributable to outstanding PAYE tax and NIC.

Innova kept payroll records showing that PAYE tax and National Insurance contributions (NIC) had been regularly deducted from the wages of its employees. The records showed that between 31 July 2007 and 31 March 2008, PAYE tax and National Insurance of £220,708.36 were due and payable to HMRC. No sums in respect of PAYE or National Insurances were ever remitted by Innova to HMRC although throughout that period, the Appellants paid themselves substantial salaries and expenses. Mr Martin's salary was £75,000 per year and Mr Roberts' was £125,000 per annum.

Innova had an accountant who prepared monthly payroll sheets showing payments due to employees and the total PAYE Tax/National Insurance Contributions. Monthly payroll sheets were produced showing payments due to employees and total PAYE tax and National Insurance Contribution (NIC). The Appellants were aware that Innova had a statutory obligation to pay PAYE tax and NIC to HMRC each month. Innova's accountant was responsible for sending PAYE tax and NIC to HMRC on the instructions of a director. The Appellants were the sole signatories on Innova's bank account.

No such instructions were ever given, as no NIC or PAYE tax was ever remitted by Innova to HMRC. Each month, from the outset of Innova's trading, the Appellants conducted a financial review and each month they took the decision to refrain from making any payments of PAYE tax or NIC.

At no stage, while Innova was trading, did the Appellants contact HMRC to discuss Innova's failure to pay PAYE tax or NIC. Instead, they resolved to pay creditors on a business critical basis. This basis involved continuing to pay their own salaries and creditors with whom they might do business with any successor company to Innova.

Shortly before Innova went into liquidation, certain contractors were paid to ensure that their services could be used by a planned successor company (Cornerstone Resources Ltd). In particular, between March and April 2008, trade creditors were reduced from £104,025.21 as at 17 March 2008 to £24,119.51 as at 2 April 2008. However, no payments were made to HMRC. Innova ceased trading on or about 18 April 2008.

Cornerstone began trading in about May 2008 when a PAYE scheme was set up. It had the same registered office as Innova. The Appellants were the directors of Cornerstone and they awarded themselves the same salaries they had received from Innova. HMRC officers visited Cornerstone's accountant on 27 February 2009 to examine Cornerstone's payroll records in order to quantify the debt owed to HMRC. No payments of PAYE tax or NIC were made by Cornerstone until 26 November 2009 when £5,000 was paid. Cornerstone's PAYE tax and NIC liability for the tax year 2008/09 has been assessed at £126,677.86 of which £121,677.86 was still outstanding as at 6 September 2010.

On 28 June 2010, the Appellants were each disqualified from holding the office of director for a period of four years.

The Appellants sought to displace the PLN's on the basis that they were not neglectful, but the Tribunal gave their appeal short shrift. The decision records:

"We have, however, no difficulty in holding on the balance of probabilities, that Innova's failure to pay the NIC specified in the PLNs was attributable to the neglect on the part of the Appellants. HMRC have discharged the onus of proof which rested on them. It was plain that the Appellants were fully aware of the statutory obligations in

relation to payment of NIC. They received information each month about the financial health of Innova including the amount of NIC due and payable by the 19th of the month. They were personally responsible for ensuring the payment of NIC and PAYE tax. They were responsible for the decision each month, while Innova traded, not to pay NIC and PAYE tax and chose instead to pay other creditors and their own salaries; they thus propped up for as long as possible an ailing business with funds which should have been remitted to HMRC. No attempt was made to discuss matters with HMRC. They made no reasonable provision for the payment of NIC or PAYE tax; even although they must have been aware that the liability to HMRC was increasing each month.

Having traded in the consultancy business for a number of years through the medium of Synergi, the Appellants were well aware of a company's statutory obligations in relation to the payment of PAYE tax and NIC. From the outset Innova was probably underfunded. If it was not, then one must ask why no PAYE tax or NIC was ever paid. It is no defence to say that HMRC were not chasing for payment. Innova had a statutory obligation to pay whether or not HMRC demanded payment sooner or later.

No reasonable and prudent businessman would have behaved in this way or conducted business in this manner. No reasonable and prudent businessman would have neglected to pay the NIC as it fell due. Any reasonable and prudent businessman, having control of the operations of Innova, would probably have ceased trading within a few months of start-up at the latest or attempted to make arrangements with HMRC about deferring payment."

The test of 'neglect' - Appeal case: O'Rorke v HMRC TC01675

This case is an appeal about a subsidiary aspect of the power in section 121C; it concerns whether medical evidence submitted at an earlier hearing should be allowed, and the key issue tested was whether the test of "neglect" in the legislation is an objective test or a subjective one. If the test is subjective, then evidence as to the defendant's state of mind at the time of the offence would be relevant to an appeal; if objective then the medical evidence would not be admissible.

Mr O'Rorke was the finance director of L Wear & Co; he resigned as a director on 22 February 2007. On 5 March 2007 the company went into liquidation owing £321,306.60 of unpaid NICs. On 3 September 2009 HMRC issued Mr O'Rorke with a PLN for £290,307.60, and on 25 June 2010 this was reduced to £218,593.77.

Mr O'Rorke appealed against the PLN on the basis that he suffered from an addiction which affected his behaviour, and this ought to be taken into account when assessing whether he was negligent in carrying out his duties.

HMRC argued that the test of negligence in s 121C was an objective test and thus the state of mind or mental capacity of the officer was irrelevant in determining his culpability for the failure of the company to pay. This therefore excluded the submission of medical evidence by Mr O'Rorke to support his claim that he was not culpable due to his state of mind brought about by his addiction. HMRC's view is based on the normal understanding of neglect in other areas of legislation. They claimed that there was no basis on which a different, subjective, interpretation could be based, and that the court was therefore obliged to follow the normal interpretation of neglect – this being an objective test. Had Parliament intended a different meaning to apply, then the law would have made this clear.

HMRC cited a number of cases to support their view, and most particularly Peter Inzani v R & C Commrs [2006] STC SCD 279, in which an earlier court definition of neglect set out in Blyth v Birmingham Waterworks Co (1856) 11 Exch 781:

‘Negligence is the omission to do something which a reasonable man, guided upon those considerations which ordinarily regulate the conduct of human affairs would do, or doing something which a prudent and reasonable man would not so. The defendants might be liable for negligence if, unintentionally, they omitted to do that which a reasonable person would have done, or did that which a person taking reasonable precautions would not have done.’

Other cases were cited which also referred to Blyth. The Inzani case was a similar appeal against a PLN under s 121C, and another case cited was a 2011 appeal against a PLN – Stephen Roberts & Alan Martin v R & C Commrs [2011] UKFTT 268 (TC).

The Tribunal considered the matter in some depth and came to the conclusion that as s121C is a penal provision, the tribunal should be careful in how the legislation is construed. HMRC’s view is that as the legislation is clear, the intention of Parliament expressed in Hansard is not relevant (Pepper v Hart). However in J E Chilcott & Others v R & C Commissioners [2009] STC 453, subsequently upheld by Lord Neuberger with the following:

‘The fact that some might regard the operation of s144A, according to its terms as penal, merely emphasises that the court should construe it with care and if there is a narrower construction less beneficial to the Revenue, more beneficial to the taxpayer, available then the court should at least seriously consider it, and if appropriate, adopt it.’

The Tribunal decided to follow some of the matter quoted in Hansard, and found the test to be a subjective test, which must take into account the state of mind of the officers concerned.

Upper Tribunal appeal: HMRC v O’Rourke [2013] UKUT 0499

The Upper Tribunal overturned the decision of the First Tier Tribunal in the above case. The Tribunal Judge, Mr Justice Hildyard, found the concept a difficult one, but on balance could not find sufficient in the context of the legislation to support the displace the standard view of neglect as being an objective test.

Appeal case: Michael Denmark v HMRC TC0696

This is a routine appeal against a personal liability notice, but suggests that the powers in FA 2020 are well placed to deal with issues raised by this appeal.

Mr Denmark was the sole director of Worldwide Support Services Limited (WSSL). The company was incorporated in July 2012. It operated until it was voluntarily liquidated in December 2013. During this time, the company operated as a payroll services company, but made no payments to HMRC either of PAYE or of National Insurance Contributions. Payroll started in November 2012 but no 2012-13 P35 was filed; the company did file under RTI in 2013-14 for the time it was active. During the appeal it emerged that Mr Denmark was also a director of two other companies in liquidation owing money to HMRC. The total arrears of PAYE and NIC for the two tax years (but only just over 12 months of operation) were £1,359,870. A successor company WSS London Ltd went into liquidation in July 2014 owing HMRC £543,590 in PAYE and NIC – once again no payments having been made at all.

The appeal was dismissed. Mr Denmark was disqualified as a director for his conduct while a director of Worldwide Support Services Ltd through an undertaking given on 5 October 2015. He was further disqualified by court order on 2 March 2018 for conduct while a director of two further companies.

Appeal case: Vinod Parmar & Bhwana Parmar v HMRC TC04927

This case applied both the PAYE and NIC rules together to recover substantial sums from two company directors. The company records were poor to non-existent, and the directors took much of the company takings in cash for themselves, paying for personal expenditure and credit card bills. The amounts were not recorded as income of the company. The company was subsequently liquidated, and HMRC raised assessments on the two directors for PAYE on the amounts calculated as removed over a period of years, and issued personal liability notices for the related NIC.

The directors sought to argue that the amounts so taken should be regarded as dividends, as that was always their intention – to draw a modest salary (below the NI limit) and the balance by way of dividends. However, given that the amounts had not been included in the company accounts (nor was corporation tax paid on them) and there had been no director or shareholder meetings, this was an impossible claim.

The Personal Liability Notices were upheld.

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