



TC04357

Appeal number: TC/2014/00453

INCOME TAX – late payment of debt- can this be set off against income - taxpayer continued supplying services - debt gradually recovered - debt not bad nor estimated to be bad - appeal allowed in part as debt from one client was bad

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

MALCOLM MICHIELS

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE BARBARA KING
JOHN WOODMAN**

Sitting in public at North Shields on 19 March 2015

The Appellant, Malcolm Michiels, appeared in person

Rosalind Oliver of HM Revenue and Customs, for the Respondents

DECISION

The issue

- 5 1. The issue in this appeal concerned the sum of £6713 which the appellant, Malcolm Michiels, had entered in box 26 of his tax return for the year 2010-11. That box is headed 'Irrecoverable debts written off'.
2. Mr Michiels had submitted his electronic return on 28 October 2011 and the respondents "HMRC" had opened an enquiry into that return on 9 October 2012.
- 10 3. HMRC issued a closure notice on 23 June 2013 stating that additional tax in the sum of £2602.60 was due to be paid by Mr Michiels. HMRC did not accept that the sum of £6713 was a 'bad debt' or 'estimated to be a bad debt'. The tax calculation by HMRC also involved a recalculation in respect of depreciation and capital allowances which were not in dispute before this Tribunal.
- 15 4. During the hearing Mr Michiels pointed out that the sum of £6713 involved debts from two clients. HMRC agreed that the sum of £438.38, for client A was a bad debt and should not form part of the profits for Mr Michiels during 2010-11. This left a sum of £6275 on which the Tribunal was asked to make a ruling.

The Law

- 20 5. Section 35 of the Income Tax (Trading and Other Income) Act 2005 ("ITTOA") contains the following:-
- (1) In calculating the profits of a trade, no deduction is allowed for a debt owed to the carrying on the trade, except so far as –
- (a) The debt is bad,
- 25 (b) The debt is estimated to be bad
- (c) The debt is released wholly and exclusively for the purposes of the trade as part of a statutory insolvency arrangement
- (2) If the debtor is bankrupt or insolvent, the whole of the debt is estimated to be bad for the purposes of subsection (1)(b), except so far as any amount may
- 30 be reasonably be expected to be received on the debt.
6. Section 25 of ITTOA provides that profits must be calculated in accordance with generally accepted accounting practice subject to any adjustment required or authorised by law in calculating profits for income tax.

Background.

- 35 7. Mr Michiels gave oral evidence to the Tribunal. He has run a care agency business since approximately 2000. In 2010-11 he was providing carers for families

with dependent children, either because of age or where there is a need because of mental or physical disability.

8. During 2010-11 he had two clients who did not pay for the services they received during that year.

5 **Client A**

9. Client A did not pay a sum of £438.38 which was for one week's supply of services, involving the care of young children. Mr Michiels paid a visit and concluded that the parent of the children had very little money, very little in the way of assets and that steps to recover the outstanding debt were unlikely to be cost effective. Mr
10 Michiels produced a copy of the invoice sent to client A and gave oral evidence as why he thought the debt was bad. Mrs Oliver indicated that HMRC would accept that sufficient evidence had been produced to show that the sum of £438.38 was a 'bad debt'.

Client B

15 10. Client B involved the supply of care services for a dependent young adult.

11. The cost of the services provided to client B were approximately £1300 to £1500 per month. This involved the attendance of a carer for several hours most week days. Mr Michiels stated that he had sent out invoices out each month to client B and included the term that the invoice should be paid within 30 days.

20 12. We had a bundle of correspondence for the hearing. This contained copy letters from Mr Michiels to HMRC.

13. In a letter dated 16 October 2012 Mr Michiels stated that Client B owed £6731, which is the sum mentioned in his tax return and which is now accepted to include the debt owed by client A. This figure should therefore have been £6275.

25 14. In a letter dated 30 November (should be December) 2012 Mr Michiels stated that client B owed £6,631.50 in December 2010, but as at December 2012 client B owed £7444.50.

15. The Tribunal was not shown copy invoices for Client B, or a precise record of what was paid and when.

30 16. Mr Michiels told the Tribunal that he continued to provide carers for client B until January 2013. In a letter dated 24 January 2013 the debt was stated to be £7255.

35 17. Copy letters dated 3 April 2013 and 11 April 2013, written by Mr Michiels to client B, were shown to the Tribunal. These mention a debt of £5065.50 was outstanding as at April 2013. As at the date of the hearing Mr Michiels stated that the debt was approximately £1000 and he still hopes to recover the outstanding amount.

Findings

18. We find that the amount owing from client B built up over a period of time. Mr Michiels continued to provide services to client B because he thought that by doing so he was most likely to be repaid for the earlier services. He had an understanding of the circumstances of each of his clients and was able to assess who was likely to be able to pay and who could not. In the case of client B, he was correct in his assessment and it was the case that by continuing to provide services he continued to receive payments.

19. Under generally accepted accountancy practice we would have expected any payments made by client B after 5 April 2011 to have been allocated to the payment of the earliest invoices that were outstanding at any time. Mr Michiels produced no evidence to show that any payments made by client B could be allocated differently.

20. Without a detailed list of the amounts due and the payments made by Client B we could not make any findings as to when the debt, which accrued in 2010-11 was repaid, partially or in full. We find, on balance, that the sums which are now outstanding relate to a later period.

21. We find that Mr Michiels thought he had been told that he could enter sums in box 26 (headed 'irrecoverable debts written off') of his tax return where the debt was unpaid at the end of the tax year and he recalled that he had done this in previous years. HMRC have accepted that no penalty is appropriate in this case because Mr Michiels was attempting to follow what he thought he had been told. There was no evidence before the Tribunal about what Mr Michiels had considered to be bad debts in previous years.

22. The legislation refers to 'bad debts' or 'debt which are estimated to be bad'. We find that the sums outstanding from client B do not fit into either sub clause (a) or (b) of section 35(1). The sums outstanding from client B as at 5 April 2011 were paid late. Mr Michiels made no attempt to estimate a proportion of the debt which he thought would never be paid. He pursued the full amount from client B and was, in time, paid the full amount, albeit that further amounts are now outstanding.

Decision

23. The appeal is allowed in part as we agree that the sum of £438.38 as mentioned in paragraph 9 above is a bad debt.

24. We find that the sum of £6275 was not a bad debt nor was it estimated to be a bad debt as at 5 April 2011. This amount cannot therefore be set off by Mr Michiels against his profits in the tax year 2010-11. The appeal against that amount fails.

25. The question of any interest which may have accrued against the additional tax due from Mr Michiels is not a matter for the Tribunal.

26. 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.

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BARBARA KING
TRIBUNAL JUDGE
RELEASE DATE: 16 April 2015