



SHERIFF APPEAL COURT

**[2018] SAC (Civ) 2
GLW-A1184-11**

Sheriff Principal M W Lewis
Appeal Sheriff N Ross
Sheriff Principal C A L Scott QC

OPINION OF THE COURT

delivered by SHERIFF PRINCIPAL M W LEWIS

in appeal by

MAN HEN LIU

Pursuer and Appellant

against

COLIN A F HASTINGS

Defender and Respondent

Appellant: Dewar QC; Bell; Cannons Law Practice LLP

Respondent: Moynihan QC; Anderson Strathern LLP

10 January 2018

Background

[1] Man Hen Liu (“the appellant”) was sequestered on 3 October 2005. The respondent is his permanent trustee. The general functions of a permanent trustee are set out within section 3(1) of the Bankruptcy (Scotland) Act 1985 (“the 1985 Act”).

[2] Following appointment, the respondent started to discharge his duty to recover, manage and realise the appellant’s estate and to distribute the funds realised among the

creditors. The clear thrust of the sheriff's findings is that the appellant failed to provide the respondent with adequate information for this purpose.

[3] One of the most blatant examples of such a failure arose in 2006. The appellant owned a number of businesses, and for several years prior to his sequestration these were operated by his son, Sandy Liu, under a power of attorney. In 2006 the respondent required the appellant to complete a statement of assets and liabilities form, and a supplementary questionnaire form. The appellant returned both on 4 October 2006, but provided no detailed information in response to the majority of questions. He stated that questions about any assets transferred by him in the previous five years did not apply to him. These two documents represented the full extent of the information supplied by him to the respondent.

[4] The pattern of limited co-operation by the appellant continued. The appellant resided mainly in China until June 2010. He did not comply with the respondent's request to provide an address in China. He was represented by solicitors and various firms of accountants in Scotland. The respondent supplied detailed information when requested to do so by the accountants acting for the appellant. Neither the appellant nor those representing him replied in any meaningful way to correspondence from the respondent.

[5] On 14 August 2006 the respondent received a claim in the sequestration from HMRC. This covered the trading of one of the appellant's businesses, the Stuart Hotel, for periods after 30 April 2003. Unknown to the respondent, the pursuer would subsequently allege he had transferred that business to his son, Sandy Liu, with effect from 30 April 2003, and would claim he therefore had no personal liability for PAYE or NIC payments after that date. By late 2006 the respondent held information that, amongst other things, the appellant had never notified HMRC that he had ceased to trade that business, that the liquor licence was in the appellant's name after 30 April 2003, that the appellant had granted a lease in

June 2004 over the business premises and that by missives dated September 2005 he had purported to sell the business premises “together with the business”, all of which tended to indicate that the appellant continued to trade there after April 2003. He saw no documents intimating to suppliers any change of business, or evidencing any transfer of employees. The respondent had a meeting with Sandy Liu who did not inform him that the business of the Stuart Hotel had been transferred by the appellant to him. The respondent duly concluded that the appellant was liable for PAYE and other taxes in respect of the Stuart Hotel business for, amongst other things, periods after 30 April 2003.

[6] On 25 July 2007 and 6 February 2008 the respondent sent to the company creditors, the appellant and his son, circulars which set out his adjudications of the HMRC claim. He also advised that appeals were available, and the relevant deadlines. Neither the appellant nor his son appealed those adjudications. The respondent duly settled the HMRC claim.

[7] The respondent also settled an HMRC claim under section 73(1) of the Value Added Tax Act 1994 (“VATA”) for under-declared VAT in the sum of £260,000 or thereby.

[8] In 2011, the appellant brought a damages action alleging that the respondent had breached the duty of care owed to the appellant. In that action the appellant challenged, amongst other claims, the basis of the respondent’s adjudication of PAYE/NIC which included claims for a period after the date upon which the appellant claimed that he had ceased to trade. The appellant also challenged the basis upon which the respondent had settled the VAT claim due to the fact that the claim had been made more than three years after the end of a VAT accounting period and was not exigible, therefore.

[9] Following a proof before answer, the sheriff assoilzied the respondent from the craves of the Initial Writ. He found in fact and in law that in his adjudications of the HMRC

claims, the respondent had acted reasonably and did not breach his duty of care to the appellant.

[10] Although this appeal originally raised a number of issues, only the issues relating to PAYE/NIC adjudication and the treatment of VAT were argued at appeal.

Preliminary Observations

Role of an Appellate Court

[11] At paragraph 1.3 in the respondent's Note of Argument, reference was made to the, by now, well-known authorities of *McGraddie, Henderson & RBS v Carlyle*. The general position adopted on behalf of the respondent was that the appeal had to fail because the sheriff had set out an ample rationale for the conclusions reached by him. Senior counsel for the appellant "in broad terms" accepted what was stated within said paragraph 1.3. He acknowledged the difficulty which the authorities presented. However, he sought to maintain that the sheriff's conclusions were not "reasonably based" and were thus vulnerable to attack. The sheriff's findings could be shown to be plainly wrong and there was also a demonstrable failure on the part of the sheriff to consider relevant evidence.

The Duty of Care

[12] Mr Dewar accepted the sheriff's formulation that the trustee's duty of care in adjudicating claims is to deal with claims timeously in a summary fashion upon the available information and, as to whether to accept or reject claims, to arrive at decisions which are reasonably capable of justification. It was the scope, rather than the nature, of this duty which informed the present appeal. He submitted that the sheriff had been obliged to arrive at rational conclusions. He submitted that the respondent had failed to proceed with

reasonable care and had therefore not complied with the duty or duties incumbent upon him.

[13] The sheriff's formulation of the duty of care on the respondent was not disputed, and we agree with it. We also agree with the sheriff's statement that "It would appear that the circumstances of the case are everything to answering the question – what is reasonable and therefore what is the scope of the insolvency practitioner's duty?"

The Grounds of Appeal

Appellant's Submissions

[14] Before dealing with each of the grounds of appeal, senior counsel, somewhat surprisingly, urged us not to be distracted by the sheriff's adverse findings in respect of the credibility and reliability of the appellant and his son, Sandy Liu, and that because the sheriff did not, at any point in his decision, state in terms that he did not believe them. We consider that this proposition is without merit. The sheriff could not have been more clear that he found the evidence of both the appellant and Sandy Liu to be incredible and unreliable (see paragraphs [4] – [8] and [32] within the sheriff's Note).

PAYE/NIC

[15] HMRC lodged claims in the sequestration for the sum of £657,229.33. The respondent adjudicated upon the claims and settled them in full. (See findings in fact 2, 3 and 6.) The adjudications are set out in two memos dated 23 July 2007. Much time during the hearing was spent examining those memos (see pages 552 - 640 of the appendix.)

[16] This ground of appeal was largely informed by a core factual proposition, namely that there had been a transfer of the appellant's business (the Stuart Hotel) to his son,

Sandy Liu, on 30 April 2003. On that factual hypothesis, it had been argued before the sheriff that the respondent's decision to adjudicate in favour of the HMRC claim was in breach of the duty of care owed to the appellant. However, on the first morning of the appeal hearing, that factual matrix was significantly altered in the course of senior counsel's submissions. He intimated that he no longer founded upon any argument based upon a 30 April 2003 business transfer. Instead, he purported to utilise 14 June 2004 as the relevant date for the purposes of his argument.

[17] He submitted instead that there had been evidence demonstrating that the hotel had been leased to "the Stuart Hotel Limited" (a company controlled by Sandy Liu) with effect from 14 June 2004. In this novel approach to the appeal, senior counsel argued that the existence of such a lease was wholly inconsistent with the continuation of trade by the appellant from the hotel premises beyond the 14 June date and that the sheriff, therefore, had been plainly wrong in his failure to acknowledge that important inconsistency.

VAT

[18] It was argued (a) that the respondent had breached his duty of care to the appellant by agreeing to meet a claim (by HMRC) which was not legally exigible; and (b) that the respondent's duty of care had also been breached by his persuading HMRC to issue an assessment for the "non-voluntary" payment of VAT.

[19] In support of his argument, senior counsel relied upon the combined effect of sections 73(1) and 77 of VATA which was to confer power on the VAT Commissioners to make assessments in relation to under-declared VAT within three years of the end of the accounting period in question. Whilst a 20 year time extension applied where there was dishonesty or fraud (see sections 60 and 77 of VATA) it was for HMRC (and no one else) to

determine whether, on the facts of the case, the conduct involved amounted to dishonesty or fraud and to proceed accordingly.

[20] It was maintained, on behalf of the appellant, that as at 24 January 2007, when HMRC wrote to the respondent inviting a voluntary payment, HMRC had, by then, concluded that any other basis for an assessment (i.e. dishonesty or fraud) was out of the question. The manner in which the respondent had replied to HMRC was tantamount to active encouragement that HMRC should issue an assessment for the “non-voluntary” payment of VAT.

[21] Senior counsel also contended that the respondent was at fault because he had agreed to meet a claim which was not legally exigible. It was submitted that whatever the effect or purpose of the HMRC letter dated 12 February 2007, the exercise of the powers available under sections 60 and 77 of VATA was not involved.

Respondent’s Submissions

PAYE/NIC

[22] In addressing the question of whether there had been a cessation of trading by the appellant prior to his sequestration, senior counsel for the respondent rounded on the *change of position* involved in the appellant’s reliance upon an entirely new cessation date, namely 14 June 2004. He stressed that the court was not dealing with what might be described as a *continuum*.

[23] He highlighted the fact that both the appellant and his son had claimed that the business of the Stuart Hotel had been transferred in April 2003. The lease which gave rise to the new cessation date had supposedly been executed in June 2004. That, senior counsel

observed, threw up a difficult question; just *who* was the transferor of the business in June 2004?

[24] He referred to the report by the witness Gordon Christie, a chartered accountant with a background in insolvency and to paragraph 4.9 therein, in particular. He submitted that the sheriff had carefully considered Mr Christie's list of factors for and against the date of cessation founded upon at proof. Reference was made to findings in fact 24 to 29. The sheriff had accepted the existence of a lease but there were other indicators which had served to undermine the appellant's position on cessation.

[25] Those indicators included a fraudulent application for a loan; the preparation of accounts down to December 2003 being accounts of which the appellant knew nothing; the reference in the questionnaire completed by the appellant to the final accounting period down to April 2004; and a singular absence in the forms completed to show when the appellant ceased to trade. On top of those factors lay the sheriff's damning conclusions regarding the credibility and reliability of the appellant and his son. Against that background, senior counsel submitted that there had been no error on the part of the respondent in concluding that he simply could not be satisfied regarding the alleged cessation of business by the appellant.

[26] In placing on record the respondent's objection to this aspect of the appeal being presented upon a materially different factual basis to that presented before the sheriff, senior counsel for the respondent, in any event, contended that nothing had been said on behalf of the appellant which might, in any way, justify this court in taking a completely different approach from that taken by the sheriff. Moreover, senior counsel maintained that any suggestion that the respondent had not doubted the genuine nature of the June 2004 lease was incorrect. With reference to passages within the transcript of the evidence, he argued that

there had been evidence from the respondent asserting that the lease was a sham. In any event, the appellant's case had been perilled upon an alleged cessation of business in April 2003.

[27] The appellant's revised Note of Argument lodged on 27 July 2017 proposed the deletion of finding in fact 14 but with a substituted finding in fact to the effect that the appellant had ceased trading with effect from 30 April 2003 when his business was transferred to his son, Sandy Liu. However, in the course of the appeal hearing and to suit the altered chronology upon which the appellant now relied, the aforementioned substitution had been departed from and the deletion of finding in fact 14 *simpliciter* was now proposed.

[28] Senior counsel submitted that the deletion of finding in fact 14 would be wholly inappropriate. In an entirely artificial manner, this court was now being invited to focus only upon the later period of events in 2004. In contrast, and quite correctly, maintained senior counsel, the sheriff had looked at the totality of the evidence concerning the period from April 2003 to December 2005. He had concluded (in response to parties' competing factual contentions) that there was no satisfactory evidence from which it could be inferred that the appellant had ceased trading in April 2003.

[29] He repeated his criticism of the attempt to introduce consideration of a new, later cessation date. It involved an unwarranted fragmentation of the factual matrix presented to the sheriff. It avoided difficult questions such as "why did the appellant fail to mention the business transfer in the questionnaire completed?" It was an attempt to bypass a time frame and those issues related thereto which had resulted in an adverse outcome for the appellant.

VAT

[30] Senior counsel noted that inherent in the appellant's approach to this aspect of the appeal was the proposed introduction of a new finding in fact [31] to the effect that:

"No ordinarily prudent person conducting his own affairs (*et separatim* any ordinarily competent trustee in sequestration) would have agreed to meet a claim for VAT which was not legally exigible."

[31] He reminded the court that the terms of paragraph [28] in the sheriff's Note were not the subject of challenge in this appeal. Therefore, the proposed new finding in fact, together with the appellant's argument on VAT, had been "skewed" to coincide with the appellant's characterisation of the duty of care said to have been incumbent upon the respondent. In senior counsel for the respondent's submission, aside from all else, this was an illegitimate attack upon paragraph [28] using "backdoor" methods.

[32] Senior counsel also reminded the court that section 60 of VATA had a dual purpose. Its primary or direct purpose concerned charging provisions which authorise the imposition of a penalty. Its indirect purpose (via section 70(7)) involved section 60 being used as one of the criteria in a situation where the VAT assessment may be made after three years have elapsed following the final VAT period. He submitted that where that indirect purpose was at play, there was no need to mention, specifically, section 60 in the letter/notice issued by HMRC. Therefore, that aspect of the appellant's argument was entirely fallacious.

[33] Paragraph [40] in the sheriff's Note went a long way towards demonstrating why the appellant's arguments, both at first instance and on appeal, were entirely ill-conceived. The appellant's attempt to present this part of the appeal under reference to isolated pieces of correspondence was also ill-conceived. There was no doubt that the respondent had considered all salient factors. He concluded that there had been dishonesty having regard to a

discernible pattern of under-declaration (of VAT). In turn, the sheriff was satisfied on the material presented to him that there was such a basis to infer dishonesty.

[34] Senior counsel submitted that, in considering the duty of care, the question was whether the respondent's decision was reasonably capable of justification. His justification had been set out within his second adjudication of 23 July 2007 (see pages 609 - 612 of the appendix.) He maintained that such justification had been eminently reasonable. Had the appellant taken the view that the acceptance of the claim was erroneous he could have appealed the adjudication but he did not.

[35] Insofar as the appellant sought to found upon some procedural impropriety in regard to HMRC's alleged failure to provide specification of the basis for the VAT assessment, senior counsel invited the court to reject such an argument. The appellant had a right of appeal. The sheriff had found (rejecting the appellant's evidence) that the appellant had received the circular setting out the respondent's assessment of his liabilities, and was therefore aware of these. If the appellant had an innocent explanation for the non-payment of VAT then he could have lodged an appeal to challenge the assessment. The appellant's engagement with accountants was amply demonstrated within findings in fact 11 and 12. An appeal, even at the stage of the second adjudication, could have served to achieve recovery of all and any monies handed over as a consequence of an incorrect or ill-informed assessment. It was counsel's contention that no procedural impropriety existed.

Causation

[36] On causation, the respondent relied on the appellant's failure to exercise his rights of appeal against the adjudication. The respondent also relied on the sheriff's determination that it had not been proved that the tax outcome would have been any different if the respondent

had acted differently. The proposition that negligence on the part of the respondent had, in fact, caused the appellant to be landed with an excessive tax bill had not been established in evidence.

[37] On the absence of an appeal by the appellant, senior counsel argued that there could and should have been an appeal after the first adjudication (i.e. on the hypothesis that the appellant was minded to challenge the assessment). He also demonstrated that an appeal taken after the second adjudication could have had the same effect (see section 73(9) of VATA). Accordingly, the operative cause of any loss suffered by the appellant in the VAT context was the failure of the appellant to exercise his right or rights of appeal.

[38] Insofar as any explanation for the failure to appeal existed, it appeared to amount to nothing more than “ignorance” and non-receipt of the relevant circular (which evidence the sheriff did not accept). That an individual such as the appellant should find encouragement to seek monetary compensation in these circumstances was simply “an affront to justice”, as counsel put it. Where the appellant considered that the VAT assessment was excessive it was incumbent upon him to challenge HMRC on that issue.

[39] Senior counsel for the appellant was unable to offer a principled rebuttal of these submissions. He maintained that the appellant’s tax liability would have been much lower had the respondent not acceded to the HMRC assessments and that the respondent’s actions caused the appellant’s losses. He also argued that the onus of proof lay with the respondent when it came to proving that the “loss” was unavoidable.

Conclusions

[40] We consider that the appellant’s attempt to alter the business cessation date relied upon (i.e. from 30 April 2003 to 14 June 2004) must fall foul of the principles articulated in the

authorities referred to within paragraph [11] above. The sheriff was, of course, the fact-finder at first instance. At proof, he was specifically invited by the appellant's counsel to accept as a matter of fact that 30 April 2003 was the cessation date for trading. From what we have seen and heard in this appeal, there is nothing to suggest that the sheriff's approach to the evidence was in any way irrational, perverse or plainly wrong. He has explained the reasoning which underpins the findings in fact. Aside from all else, the sheriff formed an adverse view of the appellant and his son when it came to the issues of credibility and reliability.

[41] Accordingly, the appeal, in our opinion, fails in relation to the challenges directed at the sheriff's findings in fact. Further, insofar as the PAYE/NIC grounds of appeal rely upon the shift in date to 14 June 2004, we condemn such reliance as illegitimate in the context of this appeal. An appellant cannot be permitted to seek to cure failure at first instance by the introduction, on appeal, of a novel factual matrix particularly where his principal witnesses at proof have been found to be incredible and unreliable.

[42] In regard to all of the issues pertaining to PAYE/NIC, we conclude that the submissions advanced on behalf of the respondent are to be preferred. Even where, for the sake of argument, we had been persuaded to countenance the aforementioned shift in date to 14 June 2004, the criticisms articulated by senior counsel for the respondent served to expose the folly involved in trying to re-write history in the circumstances of this case. For example, as the respondent's counsel pointed out, there had been evidence before the sheriff to the effect that the lease which the appellant purported to found upon had been a sham.

[43] Given the sheriff's findings on credibility and reliability together with his detailed consideration of the fundamental inconsistencies in the appellant's position (see paragraph [6] of his Note) it is, in our view, reasonable to infer scepticism over the lease. We also accept the force in the respondent's senior counsel's question; who *would* have been the *transferor* in the

context of a lease granted in June 2004? That question and the appellant's failure to answer it in the course of the appeal, shows fundamental issues of credibility in the appellant's position. The sheriff in our view correctly (at paragraph [19] in his Note) determined that "It was not necessary for the court to resolve the factual dispute about when it was the pursuer ceased to trade at the Stuart Hotel. The issue for the court is whether the defender acted reasonably in concluding that the pursuer continued to trade after 30 April 2003."

[44] Moreover, in relation to the duty of care said to have been incumbent upon the respondent, the sheriff's articulation of that duty was not the subject of challenge in the appeal. That being so, we found it difficult to comprehend the argument presented by senior counsel for the appellant when it came to the sheriff's treatment of the duty of care. Insofar as it was maintained that the sheriff erred in his application of the duty of care to the facts of this case, we reject that proposition. Of course, for the purposes of the appellant's PAYE/NIC case, the allegation of fault on the part of the respondent was predicated upon the factual proposition that the appellant had ceased to trade as at 30 April 2003 (see Article 5 – pages 35 - 37 of the Appeal Print.) As we have already mentioned, the entirely different factual hypothesis involving 14 June 2004 as the material date has been rejected by this court.

[45] In relation to VAT, having regard to the various arguments inherent in the respondent's submissions, we have also concluded that the appeal is without merit. On the facts found established by the sheriff, his treatment of the competing arguments was entirely sound, in our view. The sheriff considered that the actions of the respondent in dealing with HMRC were eminently justified. Nothing said on appeal has caused us to regard the sheriff's approach to this aspect of the case as being unsound in any way. In the final analysis, it was the appellant's failure to mount a direct challenge with HMRC which gave rise to any "loss".

The sheriff determined that there was no breach of duty on the part of the respondent and we can find no basis for interfering with that determination.

[46] The absence of an appeal (to HMRC) by the appellant was, of course, the subject of submissions concerning the issue of causation. While it is probably unnecessary for us to decide upon that issue, we have reached the view that the respondent's submissions are to be preferred. Put shortly, we agree with senior counsel's contention that the operative cause of any loss said to have been suffered by the appellant in the context of VAT was the appellant's failure to exercise his right or rights of appeal. Therefore, it is, indeed, arguable that his claim for damages under this head was misconceived from the outset.

Decision

[47] In all the circumstances, we are left in no doubt that the appeal is without merit. We have, accordingly, refused the appeal and adhered to the sheriff's interlocutor of 14 March 2017. We award the expenses of the appeal in favour of the respondent and find the cause suitable for the employment of senior counsel.