[2013] UKFTT 223 (TC)

TC02637

Appeal number: TC/2011/08224

Penalty - late payment of PAYE and NICs - FA 2009, Schedule 56 - whether an insufficiency of funds was a reasonable excuse for late payment - no - whether lack of specific warning a reasonable excuse - no - whether any special circumstances existed to justify a reduction in the penalty amount - no - whether the penalty was disproportionate - no appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

ANDREW WOMACK t/a DACTYL PUBLISHING **Appellant**

- and -

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

TRIBUNAL : JUDGE MICHAEL S CONNELL
BEVERLEY TANNER

Sitting in public at Byron House Maid Marion Way Nottingham on 23 October 2012

Mr. Andrew Womack, for the Appellant Company

Mr. Philip Oborne, Officer of HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal against a penalty assessment (as amended) of £2,832.34 imposed under Schedule 56 of the Finance Act 2009 ("Schedule 56") in respect of the late payment by the Appellant of monthly payments of PAYE and National Insurance contributions ("NICs") in months of the year ending 5 April 2011.

2. The dates and amounts of the PAYE payments due and made were not in dispute. The appeal was based on whether the Appellant had a "reasonable excuse". The Appellant argued that the one of the reasons for late payments was insufficiency of funds and that the insufficiency was attributable to events outside its control. However the Appellant's main argument that it was unaware of the new penalty regime and that it was unfair for HMRC not to have taken necessary measures to ensure the Appellant was aware of the new penalty regime. The Appellant argued that the penalties should have been imposed when the defaults occurred and HMRC's decision to impose penalties was disproportionate unfair and arbitrary.

Background

3. The Appellant is a publishing company and designs and supplies student planners, staff planners, yearbooks, prospectuses and newsletters. The company started trading in 1994 and is based in Retford Nottinghamshire.

4. From 6 April 2010, a new penalty regime was introduced by HMRC for late payment of monthly PAYE and NIC by employers. Previously, there was a mandatory electronic payment surcharge on large employers (those with over 250 employees). The surcharge ranged from 0% to 0.83% of the amount paid late and depended on the number of defaults in any one year. It was therefore possible for many employers to delay payments to HMRC without incurring any material costs. Under Schedule 56 Finance Act 2009, however, this possibility was removed. Schedule 56 imposes penalties for late payment of PAYE. The legislation in relevant part is set out in below.

5. The penalties under Schedule 56 are based on a sliding scale as shown in the table below. The penalty varies as provided by paragraph 6, subparagraphs (4) to (7). The first default in any year is disregarded altogether. The remaining defaults trigger a penalty of 1%, 2%, 3% or 4% depending on their number. A 4% penalty is payable if there are ten or more defaults during the tax year.

No of failures	Penalty
1	no penalty providing the payment is less than six months late
2-3	1%
4-6	2%
7-9	3%
10 or more	4%

The penalty will not be levied if a) a time to pay agreement has been agreed in advance of the due date(s), b) if there are "special circumstances in terms of paragraph 9 Schedule 56 or c) if the Appellant can establish that there was a reasonable excuse for each or any default, and that each

payment was made as soon as the reason excuse ended. Reason excuse is not defined by legislation, but it can be considered to be an event or events beyond the taxpayer's control which prevented the payments being made by the due date.

6. The Appellant was late in paying its monthly PAYE and NICs to HMRC eleven months in the 2010 -11 tax year. The first default month is disregarded in accordance with the regulations and following the decision in *Agar* any default in month twelve does not crystallise in the default year 2010 – 11, but instead falls in the year 2011-12. Therefore there were nine defaults. HMRC produced for the hearing, a table showing the amounts of PAYE and NIC due for each of the relevant months, the penalty trigger date for each month, the date that payment was made for each of the months, and number of days that the payment was late in each of the 8 months in which payment was said by HMRC to have been late. The amounts, the due dates, the actual payment dates and the penalty amounts charged are set out in the table below.

PAYE and NIC Due and paid late	Due Date	Days Late	Penalty @ 4%
£9005.41	19.05.2010	17	disregarded
£8236.97	19.06.2010	20	£329.48
£7893.44	19.07.2010	25	£315.74
£10,787.59	19.08.2010	20	£431.50
£11,295.57	19.09.2010	14	£451.82
£13,526.17	19.10.2010	17	£541.05
£0	19.11.2010	0	£0
£11,516.64	19.12.2010	16	£460.67
£11,707.47	19.01.2011	17	£351.22
£10,414.89	19.02.2011	15	£312.44
£9032.71	19.03.2011	6	£270.98
£0	19.04.2011	N/A	£0
£94,411.45		TOTALS	£2832.34

7**.** HMRC assessed a penalty at 3% of the total amount of defaults and notified it to the Appellant in a letter dated 5 July 2011. The Appellant asked HMRC for an independent review. By letter dated 6 September 2011 HMRC confirmed the decision. The Appellant appealed to the Tribunal on 12 October 2011.

8. The arguments in the Appellant's notice of appeal and letters to HMRC as summarized by HMRC were that:

1. Lack of notice. The way that the penalty charges had been raised without specific warning was very harsh. The Appellant said that HMRC were at fault in failing to raise a penalty on the first and subsequent defaults. The first penalty should have been raised on 20 June 2010 and at a rate of 1% , which would have been £82.36. To have submitted a penalty notice at that stage would have not only acted as a deterrent, but have ensured that attention was given to payments being made on time in future months. It was unreasonable for HMRC to delay issue and notification of the penalty, and allow the total penalties to mushroom to £4,193.76 by the time the penalty notice was finally issued on

23 June 2011. This allowed the misdemeanour to continue without the Appellant being aware that it was incurring penalties.

2. The average number of days PAYE was paid late was 18. The penalties and equivalent of an interest charge of 75% , which is totally disproportionate to the offence. Indeed, it is much higher than penalties for far more serious tax offences. The situation is not dissimilar to a motorist passing the same speeding camera once each month for 30 months before been notified by the police of the offences and receiving appropriate penalties for each offence, the penalty rate incrementally increasing with each offence. The Appellant believes this would not be acceptable to the courts and would be regarded as morally and ethically reprehensible. The Appellant accepted that he had been warned about the penalties but had no idea of the severity of the penalties or the changes in the PAYE penalty regime. The Appellant assumed that penalties would be in line with a fair rate of interest on outstanding amounts over the period for which they were outstanding.

3. The company had been struggling with cash flow in the default year because it had rescued a bookbinding factory, which had gone into liquidation. This depleted the Appellants capital resources but as a result of the factory rescue, more than 10 people who would otherwise have been made redundant, were still full in full-time employment with the Appellant

The legislation

9. The relevant legislation is contained in Finance Act 2009, Schedule 56.

Paragraph 1 of Schedule 56 states as follows:

> ‘(1) A penalty is payable by a person ("P") where P fails to pay an amount of tax specified in column 3 of the Table below on or before the date specified in column 4.
>
> (2) Paragraphs 3 to 8 set out—
>
> (a) the circumstances in which a penalty is payable, and
>
> (b) subject to paragraph 9, the amount of the penalty.
>
> (3) If P's failure falls within more than one provision of this Schedule, P is liable to a penalty under each of those provisions.
>
> (4) In the following provisions of this Schedule, the "penalty date", in relation to an amount of tax, means the date on which a penalty is first payable for failing to pay the amount (that is to say, the day after the date specified in or for the purposes of column 4 of the Table)’.

10. The table lists numerous various categories of taxes of which those referred to in items 1 and 2 (as shown in the extract from the Table below) are relevant to this appeal.

	Tax to which payment relates	*Amount of tax payable*	*Date after which penalty is incurred*
PRINCIPAL AMOUNTS			
1	Income tax or capital gains tax	Amount payable under section 59B(3) or (4) of TMA 1970	The date falling 30 days after the date specified in section 59B(3) or (4) of TMA 1970 as the date by which the amount must be paid
2	Income tax	Amount payable under PAYE regulations ...	The date determined by or under PAYE regulations as the date by which the amount must be paid
3	Income tax	Amount shown in return under section 254(1) of FA 2004	The date falling 30 days after the date specified in section 254(5) of FA 2004 as the date by which the amount must be paid

11. Regulations 67A and 67B of the Social Security Contributions Regulations (SI 2001/1004 as amended) provide that Schedule 56 applies also to Class 1 National Insurance contributions as if they were an amount of tax falling within item 2 of the above Table, and to Class 1A and Class 1B National Insurance contributions as if they were an amount of tax falling within item 3 of the above Table.

12. Paragraph 5 of Schedule 56 states that paragraphs 6 to 8 of Schedule 56 apply in the case of a payment of tax falling within item 2 or 4 in the Table.

13. Paragraph 6 of Schedule 56 states as follows:

(1) P is liable to a penalty, in relation to each tax, of an amount determined by reference to--

(a) the number of defaults that P has made during the tax year (see sub-paragraphs (2) and (3)), and

(b) the amount of that tax comprised in the total of those defaults (see sub-paragraphs (4) to (7)).

(2) For the purposes of this paragraph, P makes a default when P fails to make one of the following payments (or to pay an amount comprising two or more of those payments) in full on or before the date on which it becomes due and payable--

(a) a payment under PAYE regulations;

(b) a payment of earnings-related contributions within the meaning of the Social Security (Contributions) Regulations 2001 (SI 2001/1004);

(3) But the first failure during a tax year to make one of those payments (or to pay an amount comprising two or more of those payments) does not count as a default for that tax year.

(4) If P makes 1, 2 or 3 defaults during the tax year, the amount of the penalty is 1% of the amount of the tax comprised in the total of those defaults.

(5) If P makes 4, 5 or 6 defaults during the tax year, the amount of the penalty is 2% of the amount of the tax comprised in the total of those defaults.

(6) If P makes 7, 8 or 9 defaults during the tax year, the amount of the penalty is 3% of the amount of the tax comprised in the total of those defaults.

(7) If P makes 10 or more defaults during the tax year, the amount of the penalty is 4% of the amount of the tax comprised in the total of those defaults.

(8) For the purposes of this paragraph--

(a) the amount of a tax comprised in a default is the amount of that tax comprised in the payment which P fails to make;

(b) a default counts for the purposes of sub-paragraphs (4) to (7) even if it is remedied before the end of the tax year.

(9) The Treasury may by order made by statutory instrument make such amendments to sub-paragraph (2) as they think fit in consequence of any amendment, revocation or re-enactment of the regulations mentioned in that sub-paragraph.

14. Paragraph 9 of Schedule 56 allows HMRC to reduce a penalty if special circumstances exist.

Paragraph 9 states as follows:

(1) If HMRC think it right because of special circumstances, they may reduce a penalty under any paragraph of this Schedule.

(2) In sub-paragraph (1) "special circumstances" does not include--

(a) ability to pay, or

(b) the fact that a potential loss of revenue from one taxpayer is balanced by a potential over-payment by another.

(3) In sub-paragraph (1) the reference to reducing a penalty includes a reference to--

(a) staying a penalty, and

(b) agreeing a compromise in relation to proceedings for a penalty.

15. Paragraph 10 of Schedule 56 states as follows:

(1) This paragraph applies if--

(a) P fails to pay an amount of tax when it becomes due and payable,

(b) P makes a request to HMRC that payment of the amount of tax be deferred, and

(c) HMRC agrees that payment of that amount may be deferred for a period ("the deferral period").

(2) If P would (apart from this sub-paragraph) become liable, between the date on which P makes the request and the end of the deferral period, to a penalty under any paragraph of this Schedule for failing to pay that amount, P is not liable to that penalty.

(3) But if--

(a) P breaks the agreement (see sub-paragraph (4)), and

(b) HMRC serves on P a notice specifying any penalty to which P would become liable apart from sub-paragraph (2),

P becomes liable, at the date of the notice, to that penalty.

(4) P breaks an agreement if--

(a) P fails to pay the amount of tax in question when the deferral period ends, or

(b) the deferral is subject to P complying with a condition (including a condition that part of the amount be paid during the deferral period) and P fails to comply with it.

(5) If the agreement mentioned in sub-paragraph (1) (c) is varied at any time by a further agreement between P and HMRC, this paragraph applies from that time to the agreement as varied.

16. Paragraph 11 states in mandatory terms that HMRC must levy a penalty where P is liable:

11(1) Where P is liable for a penalty under any paragraph of this Schedule HMRC must--

(a) assess the penalty,

(b) notify P, and

(c) state in the notice the period in respect of which the penalty is assessed.

17. Paragraphs 13-15 of Schedule 56 provide for appeals to the Tribunal against a decision of HMRC that a penalty is payable, or against a decision by HMRC as to the amount of the penalty that is payable. The Tribunal's powers are laid down in paragraph 15:

15(1) On an appeal under paragraph 13(1) that is notified to the Tribunal, the Tribunal may affirm or cancel HMRC's decision.

(2) On an appeal under paragraph 13(2) that is notified to the Tribunal, the Tribunal may--

(a) affirm HMRC's decision, or

(b) substitute for HMRC's decision another decision that HMRC had power to make.

(3) If the Tribunal substitutes its decision for HMRC's, the Tribunal may rely on paragraph 9--

(a) to the same extent as HMRC (which may mean applying the same percentage reduction as HMRC to a different starting point), or

(b) to a different extent, but only if the Tribunal thinks that HMRC's decision in respect of the application of paragraph 9 was flawed.

(4) In sub-paragraph (3) (b) "flawed" means flawed when considered in the light of the principles applicable in proceedings for judicial review.

(5) In this paragraph "Tribunal" means the First-tier Tribunal or Upper Tribunal (as appropriate by virtue of paragraph 14(1)).

18. As observed in *Dina Foods Limited*, [TC01546] under paragraph 15 the Tribunal is given power:

> 'to confirm or cancel the penalty, or substitute for HMRC's decision another decision, but only one that HMRC had the power to make. The Tribunal can only rely upon the "special circumstances" provision in paragraph 9 to a different extent than that applied by HMRC if it thinks that HMRC's decision in that respect was flawed. Applying judicial review principles, the Tribunal must consider whether HMRC acted in a way that no reasonable body of commissioners could have acted, or whether they took into account some irrelevant matter or disregarded something to which they should have given weight. The Tribunal should also consider whether HMRC have erred on a point of law.'

19. Under paragraph 16 of Schedule 56, the Appellant may escape liability for a penalty if the Tribunal is satisfied that there was a reasonable excuse. Paragraph 16 was amended by Schedule 11 of the Finance (No 3) Act 2010 (c, 33). As originally drafted, paragraph 16 provided that liability to a penalty did not arise in relation to any failure for which there was a reasonable excuse. In the amended version, the paragraph also went on to say: "the failure does not count as a default for the purposes of paragraph 6..." The effect of this change is therefore that under the amended legislation, it is clear that defaults for which there is a reasonable excuse are not to be counted when fixing the appropriate rate of penalty to be charged.

Paragraph 16 of Schedule 56 states as follows:

(1) If P satisfies HMRC or (on appeal) the First-tier Tribunal or Upper Tribunal that there is a reasonable excuse for a failure to make a payment-

(a) liability to a penalty under any paragraph of this Schedule does not arise in relation to that failure, and

(b) the failure does not count as a default for the purposes of paragraph 6...

(2) For the purposes of sub-paragraph (1)--

(a) an insufficiency of funds is not a reasonable excuse unless attributable to events outside P's control,

(b) where P relies on any other person to do anything, that is not a reasonable excuse unless P took reasonable care to avoid the failure, and

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

20. In considering a reasonable excuse the Tribunal examines the actions of the Appellant from the perspective of a prudent tax payer exercising reasonable foresight and due diligence and having proper regard for its responsibilities under the Taxes Acts.

21. The operation of Schedule 56 was considered in *Dina Foods*. It was observed that:

> '(1) the legislation became operative with a commencement date of 6 April 2010, so that the first time penalties could be raised under these rules was after the end of the 2010/11 tax year, given the way that the penalties talk in terms of the number of defaults during the year in question (at [11]);
>
> (2) except in the case of special circumstances, the scheme laid down by the statute gives no discretion: the rate of penalty is simply driven by the number of PAYE late payments in the tax year by the employer (at [31]);
>
> (3) the scheme of the PAYE legislation requires taxpayers to pay over PAYE on time; the legislation does not require HMRC to issue warnings to individual employers, though it would be expected that a responsible tax authority would issue general material about the new system (at [33]);
>
> (4) lack of awareness of the penalty regime is not capable of constituting a special circumstance; in any event, no reasonable employer, aware generally of its responsibilities to make timely payments of PAYE and NICs amounts due, could fail to have seen and taken note of at least some of the information published and provided by HMRC (at [37]);
>
> (5) any failure on the part of HMRC to issue warnings to defaulting taxpayers, whether in respect of the imposition of penalties or the fact of late payment, is not of itself capable of amounting either to a reasonable excuse or special circumstances (given that there is no separate penalty for each individual default, and the penalty can only be assessed once the aggregate of the late paid tax comprised in the total of the defaults for a particular tax year has been ascertained) (at [38]-[39]);
>
> ……

Evidence and submissions

22. HMRC's bundle of documents included copies of correspondence, computerized records of telephone attendance notes and HMRC notices, together with the materials by which the new penalty system had been publicised.

23**.** It was not in dispute that the Appellant was required throughout the relevant year to make monthly payments of PAYE and NICs by the 19th day of each month. Nor was there any dispute between the parties as to the amount of PAYE and NIC to be paid by the Appellant in each of the months in question. It was accepted by the Appellant that each of the payments in respect of which a penalty has been imposed was indeed late. There was also no dispute as to the calculation of the penalties apart from the potential application of paragraphs 9 and 16 of Schedule 56

24. HMRC produced for the hearing a revised penalty notice dated 12 April 2012. This revised penalty notice revised the amount of the penalty previously imposed to take account of the decision in *Agar Ltd v Revenue & Customs* [2011] UKFTT 773 (TC). The revised penalty was calculated on the basis that the effect of *Agar* is that the 12th penalty should not have been included in the penalty notice, as the Appellant did not become liable to it until after the end of the tax year in question. Consequently the original penalty total of £4,193.76 was reduced to £2,832.34

The Appellants submissions

25. Mr. Womack reiterated and expanded upon the grounds of appeal stated in his Notice of Appeal to the Tribunal. He said that the penalties should not be confirmed because he had a reasonable excuse for the defaults, summarised as follows:

1. The Appellant was suffering from a shortage of funds during the relevant period. This was attributable to a number of reasons, but mainly circumstances and events outside his control. The Appellant had taken over another company, which had gone into administration. This severely depleted the Appellant's working capital and cash flow resources.

2. The Appellant may have been a late paying PAYE but had never missed a payment. Payments were usually between 15 to 20 days late. The penalties were unfair and totally disproportionate to the delays that had occurred.

3. HMRC failed to notify the Appellant that it might be liable for penalties if its PAYE was paid late. Mr. Womack could not recollect receiving any prior information relating to the new penalty scheme. He was also particularly concerned that none of HMRC's letters made any reference to substantial penalties. He said that it was not unreasonable, given the extensive changes in the penalty regime, to have expected the letters, which followed the initial warning letter, to have included reference to the virtual certainty of penalties in the event of any further defaults. However none of the letters from HMRC following the second breach mentioned that penalties had already been incurred. Mr. Womack said that the new penalty regime does not act as a deterrent if HMRC do not alert employers to its existence. The fact that penalties are not raised until several months after the year-end seems to encourage delays in payment. There was no incentive for taxpayers to pay PAYE on time and it was tantamount to entrapment. Employers would like to be diligent in making their monthly PAYE payments, even if they are few days late. The Appellant said that he felt cheated. This was the first time the penalty regime had changed in 18 years and as soon as he became aware of the new penalty system he changed his firm's procedures. HMRC have operated the system to generate revenue

4. In phone calls, HMRC only ever mentioned that they had the right to impose penalties. The Appellant was never told that penalties *would* be imposed. The first time the Appellant was informed that a penalty had been incurred was in the notification of 5 July 2011. HMRC should have notified the Appellant preferably after the first late payment that counted as a default as and certainly no later than the second default that it had already incurred penalties. Mr. Womack argued that even if HMRC could not have known the final amount of a penalty until the end of the year in question, they would have known, at the time of the first late payment which counted as a default, that there would be a penalty and the minimum amount of the penalty. HMRC should at that time

have informed the Appellant or raised a penalty so that the Appellant could have put in place measures to avoid further defaults. In previous years, there had never been any difficulty when payments were just a few days late.

HMRC's submissions

26. MR. Oborne for HMRC said that the Respondents accepted that the onus is on them to show default, but as the Appellant had accepted the payments were late it was for them to show why the penalty should not be charged and that the standard of proof is on the balance of probabilities.

27. Mr. Oborne submitted that the Appellant had no reasonable excuse for the late payment of the PAYE. He submitted that under paragraphs 11 of Schedule 56, HMRC had no discretion as to the imposition of the penalty. He submitted that the amount of the penalty was set down in paragraph 6 of Schedule 56 and if the tax payer paid late, HMRC were obliged to impose the penalty. He said that in the first year of the penalty regime HMRC had targeted taxpayers who were the most persistent defaulters on a risk-assessed basis.

28. Mr. Oborne submitted that lack of awareness of the penalty regime was not a special circumstance. He said that HMRC publicised the late payment penalties for PAYE and NICs extensively both before and after they came into effect. An employer pack including a CD-ROM was mailed to all employers in February 2010; flyers were mailed to employers and factsheets were distributed at face to face events (such as "Employer Talk" and published on the HMRC website). Late payment penalties also featured in issues of Employer Bulletin, on the PAYE pages of the website (and on a podcast); on Businesslink and in published guidance and employer help books. He said that this should have acted as an early warning to the Appellant that the penalty regime was about to change. HMRC made every effort to educate employers on the changes. There was also communication with accountants and other tax agents, and publication in local and national media. HMRC's Employer Bulletins refer employers to HMRC's website. The website makes the deadlines for payment quite clear:

> 'PAYE/Class 1 NICs electronic payment deadline
>
> Your cleared payment must reach HMRC's bank account no later than the 22nd of the month following the end of the tax month or quarter to which it relates.
>
> PAYE/Class 1 NICs postal payment deadlines
>
> .....please ensure your cheque reaches HMRC no later than the 19th of the month following the end of the tax month or quarter to which it relates.'

29. Mr. Oborne said that the Appellant was sent a warning letter on 28 May 2010 advising that the payment had been late, that any further late payments might incur a penalty, and giving an Internet address at which further information about the penalty regime could be found. HMRC were not able to produce a copy of the original letter as it was a computer-generated letter, which had not been copied. However he was able to produce a copy of the format of the letter, which warned that, continued late payment could result in a penalty being charged. As referred to above the letter gave links to various web pages were more information could be obtained. The letter also included an offer to sign up to receive e-mail alerts as due dates approach, and informs the addressee to contact the business payment support service in the event of the employer being unable to pay PAYE on time.

30. Mr. Oborne said that HMRC had achieved well over hundred pieces of media coverage in national trade, regional and online press. The Appellant gave the general economic climate as a reason for its insufficiency of funds and as a reasonable excuse for late payments. However, this date back at least two years prior to the start of the default year and HMRC submit that it is reasonable to expect the Appellant by April 2010 to have put measures in place to ensure that PAYE was paid on time. The Appellant appeared to have made no effort to acquaint itself of its obligations under the new penalty system. The Appellant had spoken to HMRC officers during the default year and was warned of penalties. The Appellant did not ask for any further information in connection with the new penalty regime. There is no evidence of any conversations with HMRC where the Appellant discussed future PAYE payments, only arrears. HMRC can withhold enforcement of the any overdue liability if the circumstances warrant it, but it is necessary for the taxpayer to request deferment before any liability to tax falls due, and no such request was made by the Appellant

31. Mr. Oborne said that difficult trading conditions are normal part of business suffered by most companies. The company had not demonstrated that the taking over of the other company, which had gone into administration, could not have been achieved for example by increasing the firm's overdraft loan facilities. As a result this could not be regarded as a reasonable excuse...

Conclusion

32. At the end of the hearing the Tribunal reserved its decision which now follows.

33. We accept that the Appellant's late payments may have been due to cash flow pressures on the business. However as clearly stated in paragraph 6(2)(a) of Schedule 56, an insufficiency of funds does not qualify as a reasonable excuse. An inability to pay does not represent *special circumstances*, which might justify a reduction in a penalty. An exceptional or unforeseen event, which caused the insufficiency of funds, may to amount to a reasonable excuse but on the facts of this appeal there was no such event. Something specific and related to the particular taxpayer is required. A shortage of funds that is not unusual is something, which it is reasonable to expect an employer to be able to manage perhaps by arranging short-term finance. In this case there were no unusual circumstances, which might have caused an insufficiency of funds. In any event, the Appellants PAYE payments were consistently between 15 and 20 days late, which does not reflect a serious shortage of capital or cash flow problem.

34. HMRC were not under any statutory duty to seek to warn the Appellant of change and potential penalties. The legislation does not require HMRC to issue warnings to individual employers. It is settled law that that any failure by HMRC to give warning of the penalty regime, cannot provide a reasonable excuse. The obligation is to make payment by the due date – see *Rodney Warren & Co* [2012] UKFTT 57 (TC) and *Dina Foods Limited* above.

35. The Tribunal is satisfied that there was an extensive campaign of advance publicity and that there was no reason why Appellant should not have been sufficiently alerted. The Appellant's apparent lack of awareness of the new penalty regime is not capable of constituting a special circumstance or reasonable excuse.

36. The Appellant received an initial Penalty Default Warning letter in May 2010 (which explained about time to pay arrangements) and numerous enforcement warning letters. The first default would have attracted no penalty if there had been no further defaults for the remainder of the tax year. There was a considerable amount of contact with HMRC throughout the year about

late payments of PAYE. There were several telephone conversations with representatives of the company. A reasonably prudent employer, aware of its responsibilities to make timely payments of PAYE and NICs amounts, would have been prompted to make enquiries of HMRC to ascertain the cause of the problem and obtain information about the penalty regime.

37. On the evidence, we find that in telephone conversations which followed the initial warning letter, the Appellant was not told in unequivocal terms that he had already incurred penalties and would incur additional and increasing penalties if there were any further late payments after the first disregarded month. As Mr. Womack said, if HMRC had informed him that a penalty had already been incurred following the first late payment that counted as a default, steps possibly could have taken to prevent further defaults. Nonetheless this does not absolve the Appellant of its obligations or liability to penalties. HMRC's use of terminology such as 'may' unfortunately conveys the impression that liability to a penalty is not certain, which if there has been more than one default, and no reasonable excuse exists is not the case. As HMRC say, the penalty is set down in paragraph 6 of Schedule 56 and if the taxpayer pays late, HMRC are obliged to impose the penalty. However the word 'may' does not lack clarity and is not inconsistent with the provisions of Schedule 56. It is only when the end of the tax year has elapsed that HMRC can consider whether a penalty (or penalties) has been triggered and only then can they consider, whether special circumstances exist or whether there is a reasonable excuse for late payment.

38. In *Dina Foods*, at [40]-[42], the Tribunal considered whether the penalty was disproportionate, and said as follows:

> '40. In its initial appeal letter and in its formal notice of appeal, the company referred to the penalty being excessive. It is clearly not excessive on the terms of Schedule 56 itself because the system laid down prescribes the penalties. Nonetheless, whilst no specific argument was addressed to us on proportionality, we have considered whether, in the circumstances of this case, the 4% penalty that was levied on the total of the relevant defaults in the tax year can be said to be disproportionate.
>
> 41. The issue of proportionality in this context is one of human rights, and whether, in accordance with the European Convention on Human Rights, Dina Foods Ltd could demonstrate that the imposition of the penalty is an unjustified interference with a possession. According to the settled law, in matters of taxation the State enjoys a wide margin of appreciation and the European Court of Human Rights will respect the legislature's assessment in such matters unless it is devoid of reasonable foundation. Nevertheless, it has been recognised that not merely must the impairment of the individual's rights be no more than is necessary for the attainment of the public policy objective sought, but it must also not impose an excessive burden on the individual concerned. The test is whether the scheme is not merely harsh but plainly unfair so that, however effectively that unfairness may assist in achieving the social objective, it simply cannot be permitted.
>
> 42. Applying this test, whilst any penalty may be perceived as harsh, we do not consider that the levying of the penalty in this case was plainly unfair. It is in our view clear that the scheme of the legislation as a whole, which seeks to provide both an incentive for taxpayers to comply with their payment obligations, and the consequence of penalties should they fail to do so, cannot be described as wholly devoid of reasonable foundation. We have described earlier the graduated level of penalties depending on the number of defaults in a tax year, the fact that the first late payment is not counted as a default, the availability of a reasonable excuse defence and the ability to reduce a penalty in special circumstances. The taxpayer also has the right of an appeal to the Tribunal. Although the size of penalty that has rapidly accrued in the current case may seem harsh, the scheme of the legislation is in our

> view within the margin of appreciation afforded to the State in this respect. Accordingly we find that no Convention right has been infringed and the appeal cannot succeed on that basis'.

We agree with the observations made in *Dina Foods* as set out above. The principles were endorsed by the recent Upper Tribunal decision in *Total Technology (Engineering)*. We do not consider the penalties to be disproportionate to the defaults involved.

39. As stated in *Dina Foods,* the penalty regime may be harsh in order to act as a deterrent, but it is not "unfair". The penalty scheme as laid down by the statute provides no discretion (except where "special circumstances" apply, which was not suggested here). The penalty rate rises in accordance with the incidence of default and is a fixed percentage. The penalty cannot be excessive where it was correctly assessed and calculated. We therefore follow *Dina Foods Limited*, at [40] to [42], and *Agar* at [46] and find that the penalties raised were not disproportionate.

40. The Tribunal's jurisdiction on appeal against fixed penalties was considered by the Upper Tribunal in *Hok Ltd*, where it was confirmed that the Tribunal's power is limited to correcting mistakes. It may decide that HMRC were wrong in deciding that a penalty was due and discharge it; or it may decide that HMRC imposed a penalty of the wrong amount, and replace it with the correct amount. However, the Tribunal does not have a power to substitute an amount other than the correct amount, whether on the basis of fairness or otherwise. Thus if HMRC have imposed a penalty in circumstances where one is due, and the penalty imposed is of the correct amount, there is nothing the Tribunal is permitted to do. No such power is granted by statute and none arises under the general or common law. Similarly with regard to the possible existence of 'special circumstances' although s9 states that HMRC 'may' reduce a penalty, thus affording the Commissioners some discretion, there is no mechanism by which the Tribunal may review the exercise of that discretion. The discretion to mitigate a penalty is conferred on HMRC, but not on the Tribunal, and the legislation does not provide any mechanism by which the refusal of HMRC to exercise that discretion under s 9 may be challenged before the First-tier Tribunal.

41. For the above reasons the Tribunal finds that the Appellant has not established either a reasonable excuse for any of the late payments, or shown special circumstances justifying a mitigation of the penalty. The penalty was not disproportionate and the administration of the penalty regime was not unfair to the Appellant. It therefore follows that the appeal must be dismissed and the penalties confirmed.

42**.** 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.

MICHAEL S CONNELL

TRIBUNAL JUDGE

RELEASE DATE: 21 February 2013