



TC03081

Appeal number: TC/2012/05944

VAT default surcharge - late payment - difficult personal and family circumstances causing oversight - whether reasonable excuse - yes - Appeal allowed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

CPA BESPOKE JOINERY LIMITED

Appellant

- and -

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

**TRIBUNAL: JUDGE MICHAEL S CONNELL
TIM RATCLIFFE**

Sitting in public at Alexandra House, The Parsonage, Manchester on 1 July 2013

Mr Craig Ashton for the Appellant

Mr A J O'Grady Officer of HM Revenue and Customs, for the Respondents

DECISION

The Appeal

1. CPA Bespoke Joinery Limited (“the Appellant”) appeals against a default surcharge of £5,631.44, for its failure to submit, in respect of its VAT period ended 30 November 2011, by the due date, payment of the VAT due. The surcharge was calculated at 15% of the VAT due of £37,542.95.

2. The point at issue is whether or not the Appellant has a reasonable excuse for making late payment.

10 Background

3. The Appellant’s business activity is of bespoke joinery manufacturing and installations.

4. The Appellant had previously defaulted on VAT payments in period 05/10 when a VAT surcharge liability notice was issued and again in respect of periods 08/10, 11/10 and 05/11. Surcharges were applied of 2%, 5% and 10% respectively.

5. The Appellant paid VAT on a quarterly basis. Section 59 of the VAT Act 1994 requires a VAT return and payment of VAT due, on or before the end of the month following the relevant calendar quarter. [Reg. 25(1) and Reg. 40(1) VAT Regulations 1995]. The Appellant’s return was received by HMRC on 1 January 2011. Payment was made by two FPS instalments of £20,000 and £19,659.58, which reached HMRC on 12 January 2012 and 13 January 2012 respectively.

6. HMRC have discretion to allow extra time for both filing and payment when these are carried out by electronic means. [VAT Regulations 1995 SI 1995/2518 regs. 25A (20), 40(2)]. Under that discretion, HMRC allow a further seven days for filing and payment. The due date for the 11/11 period was 7 January 2012.

7. Section 59 Value Added Tax Act 1994 (“VATA”) sets out the provisions in relation to the default surcharge regime. Under s 59(1) a taxable person is regarded as being in default if he fails to make his return for a VAT quarterly period by the due date, or if he makes his return by that due date but does not pay by that due date the amount of VAT shown on the return. The Commissioners may then serve a surcharge liability notice on the defaulting taxable person, which brings him within the default surcharge regime, so that any subsequent defaults within a specified period result in assessment to default surcharges at the prescribed percentage rates. The specified percentage rates are determined by reference to the number of periods in respect of which the taxable person is in default during the surcharge liability period. In relation to the first default the specified percentage is 2%. The percentage ascends to 5%, 10% and 15% for the second, third and fourth default.

8. A taxable person who is otherwise liable to a default surcharge may nevertheless escape that liability if he can establish that he has a reasonable excuse for

the late payment which gave rise to the default surcharge(s). Section 59 (7) VATA 1994 sets out the relevant provisions : -

5 ‘(7) If a person who apart from this sub-section would be liable to a surcharge under sub-section (4) above satisfies the Commissioners or, on appeal, a Tribunal that in the case of a default which is material to the surcharge –

 (b) there is a reasonable excuse for the return of VAT not having been so despatched then
- he shall not be liable to the surcharge and for the purposes of the preceding provisions of this section he shall be treated as not having been in default in respect of the prescribed accounting period in question ..’

9. It is s 59(7)(b) on which the Appellant seeks to rely. The burden falls on the Appellant to establish that it has a reasonable excuse for the late payment in question.

15 10. Section 59(7) must be applied subject to the limitation contained in s 71(1) VATA 1994 which provides as follows : -

 ‘(1) For the purposes of any provision of section 59 which refers to a reasonable excuse for any conduct –
 (a) any insufficiency of funds to pay any VAT is not reasonable excuse.’

11. Although an insufficiency of funds to pay any VAT due is not a reasonable excuse, precedent case law has established the principle that the underlying cause of any insufficiency of funds may constitute a reasonable excuse.

12. The onus of proof rests with HMRC to show that the surcharges were correctly imposed. If so established, the onus then rests with the Appellant to demonstrate that there was reasonable excuse for late payment of the tax. The standard of proof is the ordinary civil standard of a balance of probabilities.

13. The Appellant’s appeal against the surcharge for period 09/11 was received by the Tribunal on 21 May 2012.

30 Appellant’s Case

14. The Appellant does not dispute that its VAT payment for the period 11/11 was due on 31 December 2011 or that the Appellant was late making payment. It is agreed that the payment if made electronically was due on 7 January 2011 but that the final balance due did not reach HMRC until 13 January 2012.

35 15. In correspondence with HMRC, Mr Craig Ashton one of the directors of the Appellant company, said that because of the economic climate many of the company’s customers were paying late which caused a cash flow problem. The company was also in the process of setting up an online banking payment system and was waiting to receive a card reader which was necessary to set up the account.

16. Mr Ashton said that the penalty was also unfair and disproportionate given that the company's PAYE payments were only made a few days late.

17. A further reason for the delay in payment was that the company had a £20,000 per day limit and had to remit the amount due to HMRC by way of two payments. Mr Ashton said that he thought the FPS payments would reach HMRC the same day as they were sent, unaware that HMRC did not subscribe to the scheme.

18. Mr Ashton said that the period around Christmas is always a difficult time for the company because the construction industry shuts down for a two-week period. He had left instructions with the company accountant to file the PAYE return and this had been done on time. He returned from the Christmas break on 9th January and realised that the PAYE was overdue and late. He immediately attended to payment.

19. Mr Ashton said in correspondence with HMRC that one of the reasons he had overlooked the PAYE liability was because of other factors of a personal nature relating to his family life that he did not want to disclose. He said that the company had an excellent VAT compliance record but that at the due date personal domestic difficulties had badly affected him. He had been going through a difficult divorce and was in the process of buying another house which was in a very poor state of repair, which meant that his business records and papers were kept his parents' house where he had been staying temporarily. The month of December 2011 had been particularly bad, mainly because of problems encountered with his 16-year-old son.

20. On Christmas Day 2011 his son had gone missing. Social services had become involved and discovered that this son had been using illicit class A substances. Mr Ashton said that it was a very traumatic time for him and the combination of the strain of his divorce and his son going missing for two weeks meant that his mind was not on VAT and his business.

HMRC's Case

21. The Period 11/11 had a due date of 7 January 2012 for electronic VAT Payments and Returns. The VAT Return was received electronically on time by HMRC on 1 January 2012. The amount due on the tax return was £37,542.95. The company paid the VAT by way of FPS, but payment was made by instalments, each made after the due date late and the final balance was not received by HMRC until 12 January 2012.

22. The Christmas and New Year closure of businesses in the construction industry is an annual event and the Appellant would therefore have known well in advance that the date for payment of VAT would fall due during the closure period. Given that this was a foreseeable event the Appellant would have been expected to make arrangements for payment prior to the closure period, or if the exact amount was not known, to make a payment on account. In any event there was nothing to prevent the company making payment whether or not the construction industry had closed down.

23. The potential financial consequences attached to the risk of further default would have been known to the Appellant after issue of the Surcharge Liability Notice

in December 2009, given the information contained in the Notice. Included within the notes on the reverse of the Surcharge Liability Notice, is the following, standard, paragraph:

5 ‘Please remember: Your VAT returns and any tax due must reach HMRC by the due date. If you expect to have any difficulties contact either your local VAT office, listed under HM Revenue & Customs in the phone book as soon as possible, or the National Advice Service on 0845 010 9000.’

24. The requirements for submitting timely electronic payments can also be found -

- 10 • In notice 700 "the VAT guide" paragraph 21.3.1 which is issued to every trader upon registration.
- On the actual website www.hmrc.gov.uk
- On the E-VAT return acknowledgement.

15 25. Also the reverse of each default notice details how surcharges are calculated and the percentages used in determining any financial surcharge in accordance with the VAT Act 1994 s 59(5).

26. Therefore HMRC say that the surcharge has been correctly issued in accordance with the VAT Act 1994 s 59(4).

20 27. With regard to the Appellant’s grounds of appeal, Notice 700/50 (December 2011) s 6.3 (the notice represents HMRC's policy and understanding of the relevant legislation) states that HMRC consider that genuine mistakes, honesty and acting in good faith are not acceptable as reasonable excuses for surcharge purposes.

28. It is specifically stated in s 71(1) VATA 1994 that any insufficiency of funds to pay any VAT is not reasonable excuse.

25 29. Insofar as the Appellant argues that the surcharge is entirely excessive or disproportionate to the modest delay which occurred, the case of *Total Technology (Engineering) Limited v HMRC* heard in the Upper Tribunal held that:

- (1) There is nothing in the architecture of the Default Surcharge system which makes it fatally flawed.
- 30 (2) In order to determine whether or not a penalty is disproportionate, the Upper Tier Tribunal addressed the following factors:
- (a) The number of days of the default
- (b) The absolute amount of the penalty
- (c) The ‘inexact correlation of turnover and penalty’
- 35 (d) The ‘absence of any power to mitigate’

and decided that none of these leads to the conclusion that the Default Surcharge regime infringes the principle of proportionality.

5 30. Mr O'Grady for HMRC said that, whilst accepting that there may have been some family difficulties which impacted on Mr Ashton, HMRC had not been given any further information until Mr Ashton provided details of this in his evidence to the Tribunal at the hearing.

Conclusion

31. The Appellant was clearly aware of the due date for payments of its VAT and the potential consequences of late payment.

10 32. One of the Appellant's grounds of appeal is that it suffered cash flow shortage caused by late paying customers.

15 33. In *Customs & Excise Commissioners –v- Steptoe [1992] STC 757* the tax-payer argued that although the proximate cause of his default was insufficiency of funds, the underlying cause of that insufficiency, namely the unexpected failure by a major customer to pay him on time, amounted to a reasonable excuse. The Court determined on a majority that the statutory exclusion of insufficiency of funds as an excuse did not preclude consideration of the underlying cause of insufficiency, and that a trader might have a reasonable excuse if it were caused by an unforeseeable or inescapable event or when, despite the exercise of reasonable forethought and due diligence, it could not have been avoided. The Court nevertheless made it clear that the test had to be applied strictly.

25 34. To decide whether a reasonable excuse exists where insufficiency of funds causes the failure the Tribunal must take for comparison a person in a similar situation to that of the actual tax-payer who is relying on the reasonable excuse defence. The Tribunal should then ask itself, with that comparable person in mind, whether notwithstanding that person's exercise of reasonable foresight, due diligence and a proper regard for the fact that the tax would become payable on the particular dates, those factors would not have avoided the insufficiency of funds which led to the failures.

30 35. Having considered the Appellant Company's financial circumstances and the background facts, the Tribunal takes the view that a prudent tax person in circumstances similar to that of the Appellant would have avoided the insufficiency of funds by having appropriate precautionary measures put in place. There was in any event no evidence that the company was actually suffering serious cash flow problems.

35 36. Having heard oral evidence from Mr Ashton the Tribunal is however satisfied that he was going through a particularly difficult period at and around the time when the Appellant company's VAT fell due for payment; and given his personal circumstances it is understandable that he overlooked making prior arrangements to ensure the VAT was paid on time. Immediately upon his return following the Christmas 'shut down', he made arrangements to pay the VAT. That was on 9 January

2012. He immediately arranged for two FPS payments which reached HMRC on 12 and 13 January 2012.

37. In all the circumstances in the Tribunal's view, the Appellant has shown a reasonable excuse for the late payments.

5 38. The appeal is accordingly allowed and the surcharge discharged.

39. 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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MICHAEL S CONNELL

TRIBUNAL JUDGE

RELEASE DATE: 26 November 2013

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