



TC03114

Appeal number: TC/2013/02761

VAT default surcharge - whether Appellant in surcharge liability extension period at date of default - yes - insufficiency of funds - whether reasonable excuse - no - whether penalty disproportionate - no - Appeal dismissed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

QUARMBY GARAGE LIMITED

Appellant

- and -

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

**TRIBUNAL: JUDGE MICHAEL S CONNELL
ANN CHRISTIAN**

Sitting in public at City Exchange Leeds on 22 July 2013

Mr Philip Robinson Managing Director of the Appellant company and Mr Neil Sharman Chartered Accountant

Mrs N Newham, Officer of HM Revenue and Customs, for the Respondents

DECISION

The Appeal

1. Quarmby Garage Limited (“the Appellant”) appeals against a default surcharge of £1,168.31, for its failure to submit, in respect of its VAT period ended 31 December 2012, by the due date, payment of the VAT due. The surcharge was calculated at 10% of the VAT due of £11,683.13.

2. The point at issue is whether the Appellant has a reasonable excuse for making late payment.

10 Background.

3. The Appellant had previously defaulted on VAT payments in period 09/10, when a VAT surcharge liability notice was issued and again on 09/11, and 09/12.

4. 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 7 February 2013 and the payment was made by six FPS instalments between 11 February 2013 and 26 February 2013.

5. 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 12/12 period was 7 February 2013.

6. 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.

7. 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 : -

‘(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 –

5 (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 ..’
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8. 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.

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

15 ‘(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.’

10. Although an insufficiency of funds to pay any VAT due is not a reasonable excuse, the underlying cause of any insufficiency of funds if entirely unforeseen and outside the control of the taxpayer, may constitute a reasonable excuse.
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11. The onus of proof rests with HMRC to show that the surcharge was 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.
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Appellant’s Case

12. It is agreed that the VAT payment for the period 12/12 if made electronically was due no later than 7 February 2013. The Appellant does not dispute that its VAT payment was late. The final balance due did not reach HMRC until 26 February 2013.

30 13. The Appellant submits that the default for period 12/12 was outside the surcharge liability extension notice period, which was issued on the 09/11 default. There had been a number of late payments in the interim period and surcharges issued, but each of these had been removed. The Appellant therefore says that the 12/12 default was a first default which should have attracted no penalty.

35 14. The Appellant’s second ground of appeal is insufficiency of funds and that Mr Robinson had attempted to contact HMRC in order to request a time to pay arrangement. Mr Robinson, the managing director of the company, had attempted to speak to HMRC on 11 February 2013 without success. HMRC had allowed time to pay arrangements previously, which had always been adhered to. Mr Robinson said
40 he found it difficult to speak to anyone at HMRC who could make a decision. He

managed to speak to someone who gave him a telephone number, but this was only an automated line advising where he could find information on the Internet. He says it was impossible to discuss the situation with anybody.

5 15. The VAT was paid late because of cash flow difficulties. The Appellant had been struggling financially since 2009 when one of its major customers went into liquidation, which occasioned considerable losses to the Appellant. The Appellant's first priority was to keep on its employees and pay its suppliers in order to remain in business. They had been able to arrange an additional month's credit with their suppliers without which they would have not been able to trade, but this only
10 marginally improved their cash flow. Staff had not been given a pay rise for five years and the directors had been forced to put capital into the business in order to keep trading.

16. The Appellant also says that the penalty is excessive and disproportionate.

HMRC's Case

15 17. Mrs Newham for HMRC said that 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 for the period 09/10, given the information contained in the Notice. Included within the notes on the reverse of the Surcharge Liability Notice, is the following, standard, paragraph:

20 '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.'

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

- 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.

30 19. 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).

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

35 21. HMRC's 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.

22. It is also specifically stated in s 71(1) VATA 1994 that any insufficiency of funds to pay any VAT is not reasonable excuse. HMRC acknowledges that one of the Appellant's major customers had gone into liquidation causing significant losses for the Appellant, but that was in 2009 and correspondence with the Appellant since then had indicated that it had been able to trade out of that particular problem.

23. Mrs Newham said that the Appellant did not contact HMRC to agree a time to pay arrangement prior to the due date of 7 February 2013. Any request for a time to pay arrangement must be made prior to the date the VAT falls due for payment.

24. The Appellant's default for the period 09/10 was treated as a first default as previous default surcharges had been cancelled. The default for the period 09/11 attracted a 2% penalty. However, because the surcharge was below £400, by concession, an assessment was not raised. Nonetheless, the surcharge period was extended to 30 September 2012. It is possible that the Appellant thought that because no penalty had been raised no default had occurred. The default for period. 09/12 was therefore a third default and attracted a penalty of 5%. The default period of 9/12 fell within the surcharge period and extended the surcharge liability period to 09/13. The default under appeal was therefore within the surcharge liability period and a surcharge was applicable in accordance with s 59 (5) (c) VATA 1994

Conclusion

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

26. The Appellant's first ground of appeal is that it suffered cash flow shortage caused by a defaulting major customer.

27. 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.

28. 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. The Appellant had been late in making its VAT payments in periods

before the default period under appeal. There was a pattern of the Appellant failing to adhere to its VAT payment obligations.

29. Having considered the background facts and circumstances leading up to the default, the Tribunal finds that the underlying and primary cause of the default was not an unforeseen event outside the control of the Appellant. A prudent tax payer in circumstances similar to that of the Appellant would have avoided the default by having appropriate precautionary measures put in place. The Appellant could have applied for a time to pay arrangement before the due date but did not do so. The Appellant may have attempted to contact HMRC to agree a time to pay arrangement, but having been unsuccessful should have made a formal request in writing, or at least made further efforts to contact HMRC. The Appellant would have been aware that at the date of default a time to pay arrangement had not been agreed.

30. Insofar as the Appellant argues that the surcharge is excessive or disproportionate to the modest delays 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.

(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’

(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.

31. The burden of proof is on the Appellant to show that the underlying cause of its failure to meet its VAT payment obligations was due to unforeseen circumstances or events beyond its control. In the Tribunal’s view, for the reasons given above, that burden has not been discharged and there was no reasonable excuse for the Appellant’s late payment of VAT for the 12/12 period.

32. The appeal is accordingly dismissed and the surcharge upheld.

33. 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

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RELEASE DATE: 2 December 2013