



TC05578

Appeal number: TC/2016/05129

*VAT – Late payment - Default surcharge – Reasonable Excuse –
Proportionality – appeal dismissed*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

FRANCIS ANTHONY WHITE

Appellant

- and -

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

Respondents

TRIBUNAL: JUDGE RUPERT JONES

The Tribunal determined the appeal on 23 December 2016 without a hearing under the provisions of Rule 26 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (default paper cases) having first read the Notice of Appeal dated 27 September 2016 (with enclosures) and HMRC's Statement of Case dated 27 October 2016 acknowledged by the Tribunal on 7 November 2016.

DECISION

1. The appellant appeals against a default surcharge imposed upon him in respect
5 of VAT period 07/16 in the sum of £445.18.

Facts

2. The appellant was registered for VAT and was assigned Registration No: 757
0707 19.

3. The tax assessed on the appellant's VAT return, received on 06 March 2016, for
10 his quarterly VAT period 01/16 (01/11/15-31/01/16) was £21,175.91. The appellant
failed to make full payments of VAT due to HMRC by the deadline of 7 March 2016.
He made Faster Payment System (FPS) payments on 03, 06 and 07 March 2016
totalling £20,175.91. However, he made a final payment of £1,000 by FPS on 24
15 March 2016, some seventeen days late. In accordance with the scheme he was not
was made subject to any default surcharge but further defaults within a twelve-month
period rendered him liable to such a surcharge.

4. The tax assessed on the appellant's VAT return, received on 07 September
2016, for his quarterly VAT period 07/16 (01/05/16-31/07/16) was £32,259.09. The
20 appellant failed to make full payments of VAT due to HMRC by the deadline of 7
September 2016. He made a FPS payment on 07 September 2016 in the sum of
£10,000. However, he made a final payment of £22,259.09 by CHAPS on 08
September 2016, one day late. On 16 September 2016, the appellant was issued with
a default surcharge of £445.18, at 2% of the VAT outstanding as at the due date.

5. On 27 September 2016 the appellant appealed against the default surcharge on
25 the ground set out below.

The Law

6. The onus of proof rests upon HMRC to demonstrate that a penalty is due. Once
so established, the onus is the on the appellant to demonstrate there is a reasonable
excuse for late payment.

7. The default surcharge regime is described by Judge Bishopp in *Energys
30 Holdings* [2010] UKFTT 20 TC0335 ("Energys"):

"The first default gives rise to no penalty, but brings the trader within the regime; he
is sent a surcharge liability notice which informs him that he has defaulted and warns
him that a further default will lead to the imposition of a penalty. A second default
35 within a year of the first leads to the imposition of a penalty of 2% of the net tax due.
A further default within the following year 15 results in a 5% penalty; the next, again
if it occurs within the following year, to a 10% penalty, and any further default within
a year of the last to a 15% penalty. A trader who does not default for a full year

escapes the regime; if he defaults again after a year has gone by the process starts again. The fact that he has defaulted before is of no consequence."

8. The legislation for the default surcharge regime is found primarily in Section 59 Value Added Taxes Act 1994 ("VATA") those parts relevant in this appeal are set out below:

59 – The default surcharge

59(1) Subject to subsection (1A) below if, by the last day on which a taxable person is required in accordance with regulations under this Act to furnish a return for a prescribed accounting period

10 – (a) the Commissioners have not received that return; or

(b) the Commissioners have received that return but have not 10 received the amount of VAT shown on the return as payable by him in respect of that period, then that person shall be regarded for the purposes of this section as being in default in respect of that period.

59(1A) [not relevant]

15 59(2) Subject to subsections (9) and (10) below, subsection (4) below applies in any case where –

(a) a taxable person is in default in respect of a prescribed accounting period; and

20 (b) the Commissioners serve notice on the taxable person (a "surcharge liability notice") specifying as a surcharge period for the purposes of this section a period ending on the first anniversary of the last day of the period referred to in paragraph (a) above and beginning, subject to subsection (3) below, on the date of the notice.

25 59(3) If a surcharge liability notice is served by reason of a default in 25 respect of a prescribed account period and that period ends at or before the expiry of an existing surcharge period already notified to the taxable person concerned, the surcharge period specified in that notice shall be expressed as a continuation of the existing surcharge period and, accordingly, for the purposes of this section, that existing period and its 30 extension shall be regarded as a single surcharge period.

30 59(4) Subject to subsections (7) to (10) below, if a taxable person on whom a surcharge liability notice has been served- (a) is in default in respect of a prescribed accounting period ending within the surcharge period specified in (or extended by) that 35 notice, and (b) has outstanding VAT for that prescribed accounting period, 5 he shall be liable to a surcharge equal to whichever is the greater of the following, namely, the specified percentage of his outstanding VAT for that prescribed accounting period and £30.

35 59(5) Subject to subsections (7) to (10) below, the specified percentage 5 referred to in subsection (4) above shall be determined in relation to a prescribed accounting period by reference to the number of such periods in respect of which the taxable person is in default during the surcharge period and for which he has outstanding VAT, so that- (a) in relation to the first such prescribed accounting period, the 10 specified percentage is 2 per cent; (b) in relation to the second such period, the specified percentage is 5 per cent; (c) in relation to the

third such period, the specified percentage is 10 per cent; and 15 (d) in relation to each such period after the third, the specified percentage is 15 per cent.

5 59(6) For the purposes of subsections (4) and (5) above a person has outstanding VAT for a prescribed accounting period if some or all of the VAT for which he is liable in respect of that period has not been paid by 20 the last day on which he is required (as mentioned in subsection (1) above) to make a return for that period; and the reference in subsection (4) above to a person's outstanding VAT for a prescribed accounting period is to so much of the VAT for which he is so liable as has not been paid by that day. 25

10 59(7) If a person who, apart from this subsection, would be liable to a surcharge under subsection (4) above satisfies the Commissioners or, on appeal, a tribunal that, in the case of a default which is material to the surcharge – (a) the return or, as the case may be, the VAT shown on the return 30 was despatched at such a time and in such a manner that it was reasonable to expect that it would be received by the Commissioners within the appropriate time limit, or (b) there is a reasonable excuse for the return or VAT not having been so
15 despatched, 35 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 (and, accordingly, any surcharge liability notice the service of which depended upon that default shall be deemed not to have been served).

20 59(8) For the purposes of subsection (7) above, a default is material to a surcharge if – (a) it is the default which, by virtue of subsection (4) above, gives rise to the surcharge; or 5 (b) it is a default which was taken into account in the service of the surcharge liability notice upon which the surcharge depends and the person concerned has not previously been liable to a surcharge in respect of a prescribed accounting period ending within the surcharge period specified in or extended by that notice. ...

25 9. Section 71(1) VATA provides:

“For the purposes of any provision of section 59 ... which refers to a reasonable excuse for any conduct: (a) an insufficiency of funds to pay any VAT due is not a reasonable excuse; and (b) where reliance is placed on any other person to perform a task, neither the fact of that
30 reliance nor any deleteriousness or inaccuracy on the part of the person relied upon is a reasonable excuse.”

10. There is significant case law on reasonable excuse.

11. From this case law it is clear that the Tribunal must consider all of the relevant facts and determine whether the taxpayer acted as a reasonably conscientious business person would have done.

35 12. As Judge Medd articulated in *The Clean Car Company Ltd v CEC* [1991] VTTR 234:

“the test of whether there is a reasonable excuse is an objective one. In my judgment it is an objective test in this sense. One must ask oneself: was what the taxpayer did a
40 reasonable thing for a responsible trader conscious of and intending to comply with his obligations regarding tax, but having the experience and other relevant attributes of the taxpayer and placed in the situation that the taxpayer found himself in at the relevant time, a reasonable thing to do?”

13. There are cases which have come before the tribunal in connection with reasonable excuse concerning exceptional transactions and errors made in connection with them (see *Appropriate Technology Ltd v CEC* [1991] VATTR 226). However, the Tribunal does not consider them relevant in the context of the present case. The Appellant did not make an error in his return as a consequence of having failed to understand his VAT requirements. His return when rendered was accurate.

14. Similarly, the line of cases including and following *Jo Ann Neal* [1988] STC 131 make it clear that basic ignorance of the law does not represent a reasonable excuse.

15. The question of the proportionality of the system of default surcharges vexed the tribunal for a number of years. However, the case law is now, in the Tribunal's view, reasonably settled.

16. The judgment of the recently decided matter of *Kingsdale Group Ltd and another v HMRC* [2016] UKFTT 236 undertook a thorough review of the case law on proportionality in the context of the default surcharge regime.

17. This Tribunal adopts that tribunal's review:

“42. The doctrine of proportionality is central to our discussions later in this decision. In relation to it and its application to the issues in this case, we have reviewed the following cases (all of which, save *Enersys*, are binding on us): *Dyrektor Izby Skarbowej w Biaymstoku v Profaktor Kulesza, Frankowski, Jowiak, Orowski* (Case C-188/09) [2010] ECR I-7639 ("Profaktor") *Paraskevas Louloudakis v Elliniko Dimosio* (Case C-262/99) [2001] ECR I- 5547 ("Louloudakis") *The Commissioners for HMRC v Total Technology (Engineering) Ltd* [2012] UKUT 418 (TCC), [2013] STC 681 ("Total Technology") *The Commissioners for HMRC v Trinity Mirror plc* [2015] UKUT 0421 (TCC) ("Trinity Mirror") *International Transport Roth GmbH v Secretary of State for the Home Dept* [2003] QB 728 ("Roth") *James v UK* (Application 8793/79) (1986) 8 EHRR 123 ("James") *Wilson v SoS for Trade and Industry* [2003] UKHL 40 [2004] 1AC816 ("Wilson") *Molenheide and others* [1997] ECR I-72181 ("Molenheide") 20 R(on the application of Lumsden and others) (Appellants) v Legal Services Board (Respondent) [2015] UKSC 41 ("Lumsden") *Enersys*

43. From them we have derived the following principles:

(1) Member States are obliged to take all legislative and administrative measures to ensure collection of VAT (*Profaktor* at [21]). This is required to ensure that the tax is collected accurately thus ensuring the normal functioning of the VAT system by, in turn, ensuring tax neutrality (*Profaktor* at [21]).

(2) The measures may not, however, go further than is necessary to achieve the objective of levying and collecting the correct amount of tax (*Profaktor* at [26]).

(3) In the absence of harmonisation of European Union Legislation relating to sanctions which may be applied for non-compliance with such legislative measures,

Member States are empowered to choose sanctions which seem to them to be appropriate (Profaktor at [29]).

(4) But they must exercise that power in accordance with the principle of proportionality (Profaktor at [29]).

5 (5) Proportionality is a general principle of EU law which is enshrined in article 5 (4) of the Treaty on European Union. Under the principle of proportionality, the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties (Lumsden at [24]).

10 (6) The principle of proportionality is therefore applicable to national measures which are adopted by a Member State in exercise of its powers relating to VAT (Molenheide at [48]).

(7) It is for the national court to determine whether such national measures are compatible with the principle of proportionality (Molenheide at [49]).

15 (8) In deciding whether the measures or their application is appropriate and not disproportionate, the court must exercise a value judgment by reference to the circumstances prevailing when the issue is to be decided. It is the current effect and impact of the legislation which matters, not the position when the legislation was enacted or came into force (Wilson at [62]).

20 (9) Proportionality as a general principle of EU law involves a consideration of two questions: first, whether the measure in question is suitable or appropriate to achieve the objective pursued; and secondly, whether the measure is necessary to achieve that objective, or whether it could be attained by a less onerous method (Lumsden at [33])
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25 (10) As is the case for other principles of public law, the way in which the principle of proportionality is applied in EU law depends to a significant extent upon the context (Lumsden at [23]).

30 (11) In the context of its application to penalties, the principle of proportionality is that: (A) penalties may not go beyond what is strictly necessary for the objective pursued; and (B) a penalty must not be so disproportionate to the gravity of the infringement that it becomes an obstacle to the freedoms enshrined in the Treaty (Louloudakis at [67]).

(12) In the field of VAT, the freedoms enshrined in the Treaty means the underlying aims of the EU Directives which govern VAT (the "Directive") (Trinity Mirror at [14]).

35 (13) The objective of the default surcharge penalty (the "penalty") in enforcing the collection of tax is itself a natural consequence of the essential aim of the Directive to ensure the neutrality of taxation of economic activities (Trinity Mirror at [56]).

- (14) The underlying aim of the Directive for this purpose is the fiscal neutrality which protects taxable persons since VAT is intended to tax only the final consumer (Trinity Mirror at [59]).
- 5 (15) And given that this is achieved by the collection and deduction at each stage of the supply chain, ensuring the timely payment at each stage is a necessary consequence of that aim (Trinity Mirror at [60]).
- (16) The correct approach, therefore, is to determine whether the penalty goes beyond what is strictly necessary for the objectives pursued by the default surcharge regime (Trinity Mirror at [63]).
- 10 (17) But a penalty must not become an obstacle to the underlying aims of the Directive (Total at [72]).
- (18) An excessive penalty will impose a disproportionate burden on a defaulting trader and distort the VAT system as it applies to him (Total at [72]).
- 15 (19) For example, the imposition of a flat rate penalty might be proportionate as far as a penalty regime is concerned; but disproportionate in respect of its application to a specific small trader. It might go beyond what is necessary in relation to such trader and would distort the VAT system as far as that trader is concerned. The burden would bear more heavily on him than on a larger trader (Total at [76]).
- 20 (20) The application of the doctrine of proportionality can be at a high level (is the penalty regime as a whole disproportionate?), or at an individual level (does the penalty regime that applies in a particular case, disproportionate?) (Total at [74]).
- 25 (21) The margin of appreciation given to law makers in implementing social and economic policy should be a wide one and the courts will respect the law makers judgment as to what is in the public interest unless that judgment is manifestly "without reasonable foundation" (James at [46]) or "not merely harsh but plainly unfair" (Roth at [26]).
- (22) The principles of "devoid of reasonable foundation" or "not merely harsh but plainly unfair" can be applied to a case relating to a particular taxpayer just as much as it can be applied to the regime as a whole (Total at [93], Trinity Mirror at [72]).
- 30 (23) A UK court should be cautious in the extreme in saying that national legislation has overstepped the mark in setting the level of penalty (Total at [73]).
- (24) But a national measure will not be proportionate if it is clear that the desired level of protection could be obtained equally well by measures which were less restrictive of a fundamental freedom (Lumsden at [66]).
- 35 (25) The default surcharge regime viewed as a whole is a rational scheme (Trinity Mirror at [65]).

(26) A penalty (if it is not a fixed rate penalty) must vary according to some objective criteria. The use of the amount unpaid as an objective criterion is an appropriate if not the most appropriate criterion (Trinity Mirror at [65]), (Total at [90]).

5 (27) But this is only so if the amount of the penalty for a failure to file or pay is itself proportionate to that failure (Total at [88]).

(28) Since the penalty is for failing to pay and file by the due date, and not for delay in paying after that date, the fact that a trader is only one day late in paying does not, per se, render an otherwise proportionate penalty, disproportionate (Total at [88]).

10 (29) The absence of any financial limit does not render the regime disproportionate; but may, in a wholly exceptional case, (dependent on its own circumstances), render its application to a particular case, disproportionate (Trinity Mirror at [66]).”

The Appellant’s appeal grounds

18. The appellant notified his appeal to the Tribunal on 27 September 2016. His grounds of appeal were as follows:

15 Dear Sir/Madam,

I am asking you to please reconsider the penalty for late payment of my VAT for the following reasons.

20 While I understand that the payment arrived with HMRC on the morning of 8 September, when it was due the day before, the reason I was not able to send it beforehand was the people that I needed to gain information from (with respect to what monies received were from overseas and which ones had VAT attached) had been away for all of August until 4 September, and the then the sixth and seventh of September were a weekend, when it was not possible for me to contact my bank in order to send the payment to HMRC.

25 I made the payment as soon as I was able, and feel that a penalty of £450 under these circumstances is really a lot of money. The September deadline is difficult to make every year, on account of gathering together the information needed, while many people are still on their holidays.

30 I would be very grateful if you could please take this into account and consider cancelling this penalty.

Yours gratefully,

Francis White.

HMRC’s Submissions

35 19. HMRC submitted that the appellant had acknowledged that payment for period 07/16 was rendered late and as a result, a default had occurred.

20. They contended that the reasons put forward by the appellant for the delay in payment are at odds with the demonstrable facts. The appellant's preferred method of payment has consistently been via the Faster Payment System (FPS). The part payment for the amount due for the period 07/16 was received by HMRC on 7
5 September 2016, the due date which was a Wednesday and not a Sunday as stated by the appellant with the return being submitted on the same day.

21. The late payment was made on 8 September 2016, a Thursday.

22. The appellant had provided no explanation as to why the payment was made in two parts. If it transpired that this was due the daily transaction limits imposed by the
10 bank then HMRC would content that this would not provide a reasonable excuse as it would indicate that the Appellant was aware of those limits.

23. If, as stated, the appellant had experienced difficulty in obtaining all the information required to complete the 07/16 return by the due date for the reasons cited in the appeal he could have applied for a change of stagger to alleviate that issue.
15 HMRC Notice 700 s.20.5.1 advised that this option is available and how to apply.

24. As the appellant operates the cash accounting scheme he accounts for the VAT on a 'monies received' basis therefore he would be aware from his bank statements the amounts received. If he was unsure of the VAT liability this could have been corrected on the next VAT return.

20 25. HMRC contended that, based on the forgoing the Appellant had not put forward any arguments which could be considered to constitute a reasonable excuse for the late payment of the balance of the VAT due for the 07/16 period which would allow for the removal of the surcharge.

26. The rates of surcharge are laid down in law and neither HMRC nor the Tribunal
25 have the power to reduce the amount because of mitigating circumstances. Section 70 of VATA does not apply to surcharges issued under section 59 of the Act.

Discussion and Decision

27. On 7 November 2016 the Tribunal wrote to the appellant informing him of his
30 right to reply to HMRC's statement of case of 27 October 2016 within 30 days. He did not do so. Therefore the Tribunal has only received the brief information contained in his grounds of appeal.

28. The Tribunal is satisfied that the penalty is due and that HMRC has discharged its burden in proving so.

29. The Tribunal is not satisfied that the appellant has a reasonable excuse for non
35 payment of VAT by the deadline. This is for the reasons submitted by HMRC as set out above.

30. The Appellant should have been aware of the requirement to render and pay his returns on time.

31. The appellant has not satisfied the tribunal as to why there would be any difficulty calculating his VAT liability under his return. Indeed, he was able to calculate the liability and submit his return on time. Therefore there cannot have been any difficulty obtaining information from his client on time. Even, if there had been,
5 he should have been able to calculate his liability based upon monies he had received without reference to his client.

32. Equally the Tribunal is not satisfied that there was a reasonable excuse for failing to make the requisite payment on time. The appellant uses the FPS to make payments. The deadline for payment was 7 September 2016. This did not fall upon
10 the weekend as suggested by the appellant. Indeed, the appellant filed his return and made part payment on 7 September 2016. If there had been any difficulty receiving information or a payment from a client who returned on 4 September 2016 the appellant had sufficient time on Monday and Tuesday 5-6 September 2016 to resolve this. He was able to make part payment in time. The appellant has not given any
15 explanation as to why he was unable to make the balance of the payment on time. He was clearly able to contact his bank in order to make payment.

33. The Tribunal is also satisfied that the application of the default surcharge in the sum of £445.18 at 2% of the tax liability outstanding at the deadline for payment is not disproportionate. Even though the part payment was made only one day late, this
20 in itself could not render the penalty disproportionate. The appellant has not provided any other information in support of any argument that the penalty is disproportionate. The Tribunal notes that, exclusive of VAT, the appellant's sales in the period 01/06 were £216,910 with purchases of £85,224. In 07/06, exclusive of VAT, sales were £236,876 with purchases of £85,681. The size of the penalty could not be said to be
25 disproportionate to the size of the appellant's business.

34. Therefore the appeal must be dismissed.

35. 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
30 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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TRIBUNAL JUDGE
JUDGE JONES
RELEASE DATE: 30 DECEMBER 2016

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