[2018] UKFTT 255 (TC)

TC06485

Appeal number: TC/2017/08584

VAT – penalties – appeal against default surcharge – whether reasonable excuse – sections 59(7) and 71(1)(b) VAT Act 1994 – reasonable excuse for first late payment – surcharge reduced

FIRST-TIER TRIBUNAL
TAX CHAMBER

ASTON SERVICES GROUP LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE ALASTAIR J RANKIN
MR NOEL BARRETT

Sitting in public at Tribunals Service, Alexandra House, 14-22 The Parsonage, Manchester, M3 2JA on Tuesday 10 April 2018 at 10:00 AM

Mr Ian Gilston, Chairman for the Appellant

Mr Richard Kelly, Presenting Officer, HM Revenue and Customs, for the Respondents

DECISION

1. This is an appeal by Aston Services Group Ltd (the Group) against a VAT default surcharge of £10,094.71 for the period 06/17.

Background

2. The Company registered for VAT with effect from 1 April 1973 and carries on the business of contract cleaning. The Company submits its VAT returns electronically on a quarterly basis and first entered the default surcharge regime for the period 12/16. It has defaulted on two occasions.

3. For the 12/16 quarter the due date for electronic payments was 7 February 2017. The Company paid in three separate instalments with the balancing payment received by HMRC on 21 April 2017, over two months late.

4. According to HMRC's Statement of Case on 9 February 2017 Mr Gilston, the Chairman of the Company, telephoned to HMRC to advise that there was an issue with their VAT payment for the 01/17 period. Mr Gilston explained that there was a delay in customers paying them and therefore the Company could not make full payment. A payment plan was agreed and HMRC maintain that Mr Gilston was advised that their direct debit would be cancelled. This cancellation was confirmed by letter from HMRC to the Company dated 14 February 2017 which letter advised the Company that if it wished to pay by direct debit in future it would need to set up a new direct debit.

5. For the period 06/17 the due date for electronic payments was 7 August 2017. The total VAT liability was £504,735.68. Payment was received in four separate instalments via both CHAPS and the Faster Payments Service (FPS). The first payment of £304,735.68 was received by CHAPS on 10 August 2017 followed by four FPS payments of £20,000.00 on 8 September 2017, £50,000.00 on 11 December 2017, £10,000.00 on 17 January 2018 and the final payment of £120,000.00 on 7 February 2018.

6. Mr Gilston telephoned to HMRC on 8 August 2017, after the due date to request a time-to-pay agreement which was refused as HMRC considered the request was made after the due date.

7. HMRC issued a default surcharge notice on 11 August 2017 for £10,094.71 being 2% of the unpaid VAT liability. By letter dated 1 September 2017 the Company appealed the surcharge notice penalty on the following basis:

> "The amount of 10% is only applicable to the amount outstanding after the due payment date being 10th August 2017."

8. By letter dated 20 October 2017 HMRC upheld the default surcharge as follows:

> "I can confirm that payment of £304735.68 was received on 10 August 2017. Your VAT return shows a liability of £504735.68. The due date for payment in full (other than payments collected by direct debit) was 7 August 2017. The due date is shown on your online VAT Return and you must ensure that cleared funds reach HMRC's bank account by this date."

9. By email dated 6 November 2017 Mr Gilston advised HMRC that he believed the Company did merit cancellation of the surcharge. His reason being:

> "The fact that Pride Shop fitters (sic) Ltd of Glasgow one of our clients owed us £188,000 and only made us aware after a considerable amount of dialogue and promises to pay that they would not be able to pay us on time on the 8th August 2017 and have now subsequently gone into administration.
>
> Only then could we have foreseen a cash flow issue and then spoken to yourselves and adjusted the DD payment to reflect the position they now left us, ASG, in.
>
> All these reasons meant only on the 8/9th of August could we have envisaged an issue with making the full payment on time on the 10th via the set up DD.
>
> We phoned on the 9th August explaining our issue to the VAT helpline accordingly."

10. By letter dated 9 November 2017 HMRC's Review and Litigation advised Mr Gilston that the Company was allowed only one review.

11. The Company lodged a Notice of appeal to this Tribunal dated 20 November 2017 and received by the Tribunal on 21 November 2017. The grounds of appeal were basically those set out in the letter dated 1 September 2017 quoted in paragraph 7 above. At the start of the hearing Mr Kelly advised the Tribunal that HMRC had no objection to the appeal being allowed to proceed. Accordingly the Tribunal granted the Company permission for the appeal to proceed.

The Company's evidence

12. Mr Gilston in his oral evidence to the Tribunal claimed that he believed the Company had a reasonable excuse for not paying the VAT liability by the due date as there was a reasonable excuse. If the Tribunal determined that the reasonable excuse did not apply to the entire VAT liability then his second ground was that the default penalty should be assessed only on the £200,000.00 not paid by the due date.

13. Mr Gilston informed us that the Company's standard terms of business allowed customers 60 days to pay an invoice. After an invoice was outstanding for 30 days someone from the Company would telephone the customer and after 60 days a firm of solicitors sent a polite letter. If an invoice was outstanding for 90 days the Company instructed a firm of debt collectors. Mr Gilston's fellow director had kept in constant touch with Pride Shopfitters Ltd (Pride) and was always advised that payment would be forthcoming. A statement dated 10 May 2017 was produced showing three

invoices dated 28 February 2017, 24 March 2017 and 4 April 2017 totalling £175,028.12 due by Pride. Mr Gilston also produced a further invoice also dated 4 April 2017 for £3,893.70. A conference telephone call promised payment on either 6 or 7 August 2017. Mr Gilston tried to telephone Pride on 6 August and again on 7 August but on neither date was the telephone answered. Pride subsequently went into administration.

14. Mr Gilston informed us that the Company usually collected in excess of £1M each month but was always owed about £2M. It was not unusual for a customer to owe the Company £100K .

15. Turning to the contacts with HMRC around the due date Mr Gilston informed us that he had been told by HMRC in the past that they could not help until the Company had defaulted. During his telephone conversation with HMRC on 8 August 2017 he stated that he thought the due date was 10 August and that a direct debit was in place. As HMRC advised him that there was no direct debit in place and a default surcharge notice would issue, Mr Gilston made arrangements to pay £304,753.68 by CHAPS which arrived with HMRC as cleared funds on 10 August 2017.

16. Mr Gilston maintained that neither he nor his book-keeper were aware that no direct debit was in place. The Company's book-keeper had been with the Company for many years and was surprised to be told that no direct debit was in place. Mr Gilston was unable to say whether or not the Company had received HMRC's letter dated 14 February 2017.

HMRC's contentions

17. Section 59(1) of the Value Added Tax Act 1994 (the 1994 Act) states:

> 59 The default surcharge.
> (1) Subject to subsction (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—
> (a) the Commissioners have not received that return, or
> (b) the Commissioners have received that return but have not 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.

18. Section 59(4) of the 1994 Act states:

> (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 notice, and
> (b) has outstanding VAT for that prescribed accounting period,

> 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.

19. Mr Kelly informed the Tribunal that as the Company's final balancing payment for the 06/17 period was not received until 7 February 2018, six months after the due date, HMRC maintain the surcharge was validly raised. As the Company had defaulted in the 12/16 period the potential financial consequences of any further default would have been known to it. As this was a second default the surcharge had been correctly calculated at 2% of the VAT liability.

20. HMRC maintain that the Company's default was due to turnover problems. It had faced issues with late payment by customers for a number of VAT periods prior to the appealed period. Accordingly the Company should have addressed its turnover issues before the 06/17 period.

21. Mr Kelly pointed out that section 71(1)(a) of the 1994 Act specifically states that "an insufficiency of funds to pay any VAT due is not a reasonable excuse". The Company should have contacted HMRC before the due date to arrange a time-to-pay agreement. As the Company had entered into such agreements before it should have known that they must be made before the due date in order to avoid a default surcharge.

22. Section 108(2) of the Finance Act 2009 states:

> (2) P is not liable to a penalty for failing to pay the amount mentioned in subsection (1) if—
> (a) the penalty falls within the Table, and
> (b) P would (apart from this subsection) become liable to it between the date on which P makes the request and the end of the deferral period.

23. HMRC maintain that the Company did not submit a new direct debit until 2 November 2017 which was well after the due date.

24. Mr Kelly maintained that the Company did not have a reasonable excuse for the default for the period 06/17 and the appeal should accordingly be dismissed.

Discussion

25. When considering whether the Company has a reasonable excuse in this context, we consider the reasonable excuse exception to be an objective test applied to the individual facts and circumstances of the appellant in question.

26. In *Bancroft and another v Crutchfield (HMIT)* [2002] STC (SCD) 347 in relation to Section 59C(9)(a) the learned Special Commissioner (Dr John Avery Jones CBE) stated:

> "A reasonable excuse implies that a reasonable taxpayer would have behaved in the same way."

27. The concept of "reasonable excuse" appears throughout VAT and direct tax legislation. There is much case law in this tribunal as well as its predecessors (the VAT and Duties Tribunal and the Special and General Commissioners). It is not possible to do justice to all these decisions but there is helpful guidance in the decision of the VAT Tribunal in *The Clean Car Company Limited v C & E Commissioners* [1991] VATTR 239 where HH Judge Medd OBE QC) said:

> "So I may allow the appeal if I am satisfied that there is a reasonable excuse for the Company's conduct. Now the ordinary meaning of the word 'excuse' is, in my view, "that which a person puts forward as a reason why he should be excused".

28. Mr Kelly in his speaking notes which he made available to the Tribunal put it another way:

> "Was what the taxpayer did a reasonable thing for a responsible trader conscious of and intending to comply with his obligations regarding tax." (The underlining was made by Mr Kelly.)

29. During the course of the hearing Mr Kelly produced copies of "Online Direct Debit instructions for VAT Declaration Service". One copy referred to a direct debit with an effective date of 13 February 2017 for a bank account in the name of Cleanall Services Ltd. The other direct debit was for a bank account in the name of Aston Services Group Ltd with an effective date of 9 September 2017. Mr Gilston explained that the Company had changed its name from Cleanall Services Ltd to Aston Services Group Ltd on 1 January 2017. Neither Mr Gilston nor Mr Kelly were able to explain how a direct debit with an effective date of 13 February 2017 could be in old name of the company after the date on which it had changed its name though Mr Gilston was able to confirm the bank account details on this direct debit were those of the Company's current bank account.

30. As the direct debit with an effective date of 13 February 2017 was created on 6 February 2017 neither Mr Gilston nor Mr Kelly were able to explain why this direct debit was created. Mr Gilston was unable to confirm that the Company had received HMRC's letter date 14 February 2017 which advised that a new direct debit would need to be created.

31. The Tribunal finds there was sufficient confusion around the issue of direct debits for Mr Gilston and the Company's book-keeper to have no reason to believe that no direct debit was in place until Mr Gilston was informed of this situation during his telephone conversation with HMRC on 8 August 2017.

32. Mr Kelly informed the Tribunal that only where payments were made by direct debit would the due date have been 10 August 2017 in order to avoid a default surcharge.

33. In paragraph 4 we refer to HMRC's Statement of Case and a telephone call made by Mr Gilston to HMRC on 9 February 2017. No notes of this telephone call were included in the papers before the Tribunal. The history of telephone calls in the

bundle of documents shows a gap between 5 January 2017 and 20 February 2017 when a time-to-pay arrangement was agreed. It is not clear which VAT quarter this arrangement was for but it seems probable that it related to the 12/16 quarter as exact amounts are mentioned for each agreed payment. The Company would not have known the exact amount of its VAT liability for the 03/17 quarter until the end of the quarter. In any event, whether the time-to-pay arrangement was requested on 9 February 2017 as stated by HMRC or later that month, the request was made after the claimed due date of 7 February 2017.

34. The Tribunal was shown HMRC's notes of a telephone conversation between the Company and HMRC on 8 May 2017 when the Company requested a time-to-pay agreement in respect of the 03/17 quarter. This request appears to have been agreed to by HMRC during the telephone conversation though subsequent entries on 15 May 2017 indicate the agreement was only agreed on 15 May 2017.

35. HMRC's records show a note was entered on 15 May 2017 that no further time-to-pay arrangements would be agreed but this information does not appear to have been passed to the Company.

36. During the hearing both parties referred briefly to the Upper Tribunal decision in *ETB (2014) Ltd and The Commissioners for Her Majesty's Revenue and Customs* [2016] UKUT 0424 (TCC). Judges Sinfield and Clark gave a helpful summary of the leading case on reasonable excuse – *Customs and Excise v Steptoe* [1992] STC 757 – at paragraph 15:

> "In summary, the question to be asked when considering whether someone has a reasonable excuse for failing to pay an amount of tax on time because of a cash flow problem is whether the insufficiency of funds was reasonably avoidable. A cash flow problem would usually be regarded as reasonably avoidable if the person, having a proper regard for the fact that the tax was due on a particular date, could have avoided the insufficiency of funds by the exercise of reasonable foresight and due diligence."

Decision

37. Mr Gilston has not persuaded the Tribunal that he had a reasonable excuse due to the failure of Pride to pay the Company around £185K before the due date. We were not shown any bank statements. Even if Pride had paid on time, the amount which they owed the Company was over three hundred thousand pounds less than the total VAT due. The VAT element owed by Pride would have been around £30K. The Company must have used the VAT paid by other customers to fund its ongoing operations. Traders who borrow VAT in order to fund their business do so at their peril. The final instalment of the VAT due for the 06/17 quarter was not paid until 7 February 2018. Although we were not informed whether the tax due for the subsequent VAT quarters of 09/17 and 12/17 was paid on time no evidence was produced by Mr Gilston as to why it took over six months to discharge the liability for the 06/17 quarter.

38. However, the Tribunal notes that HMRC granted the Company time-to-pay agreements on 9 February 2017 in respect of the 12/16 quarter and on 8 May 2017 in respect of the 03/17 quarter, the due dates according to HMRC being 7 February 2017 and 7 May 2017. HMRC's records of the telephone conversation on 8 May 2017 do not show either that the Company was told that there was no direct debit in place nor that there would be no further time-to-pay arrangements allowed, nor was Mr Gilston told that he was wrong in his belief that telephoning to HMRC on the 8th or 9th day of the month was too late.

39. Applying the objective test referred to in *The Clean Car Company Limited* decision referred to in paragraph 25 above we consider Mr Gilston acted reasonably on 8 August 2017 conscious of and intending to comply with the Company's obligations. This was the third time that he had requested a time to pay arrangement after the due date but the first time that he had been told by HMRC that he should have made the request on or before the due date. It was also the first time that he was made aware of the fact that no direct debit was in place and so he had a reasonable excuse with regard to the initial payment of part of the 06/17 quarter.

40. Mr Gilston therefore reasonably believed that telephoning to HMRC on 8 August 2017 to ask for a time-to-pay arrangement was not too late. He was by then too late to set up a new direct debit but he did all that he could to have cleared funds in HMRC's bank account by 10 August. Although the payment of £304,735.68 was late the Tribunal believes the Company had a reasonable excuse for this late payment and therefore allows the appeal against £6,094.71 of the penalty but dismisses the appeal against the balance penalty of £4,000.00

41. At the conclusion of the hearing Mr Kelly asked the Tribunal whether we had power to reduce a surcharge. Although this had been clearly stated by Mr Gilston as his fall back position in the event of the Tribunal not allowing his appeal against the entire surcharge on the grounds of reasonable excuse Mr Kelly did not address us on this point.

42. Section 59(4)(b) of the VAT Act 1994 refers to "outstanding VAT for that prescribed accounting period". Section 59(7)(b) provides:

> "If a person who, apart from this section, 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 –
>
> (b) there is a reasonable excuse for the return or VAT not having been so despatched
>
> he shall not be liable to the surcharge …"

43. Section states

> "(1) Where any person is liable—
> (a) to a surcharge under section 59 **…**

the Commissioners may, subject to subsection (2) below, assess the amount due by way of penalty, interest or surcharge, as the case may be, and notify it to him accordingly; …"

44. Section 83 states:

"Subject to section 84, an appeal shall lie to a tribunal with respect to any of the following matters—
(q) the amount of any penalty, interest or surcharge specified in an assessment under section 76;"

45. Section 84(6) provides as follows:

"Without prejudice to section 70, nothing in section 83(q) shall be taken to confer on a tribunal any power to vary an amount assessed by way of penalty, interest or surcharge except in so far as it is necessary to reduce it to the amount which is appropriate under sections 59 to 70;

46. As soon as Mr Gilston learnt that no direct debit was in place he arranged for cleared funds to arrive in HMRC's bank account on 10 August 2017. HMRC were therefore in exactly the same position as they would have been if the amount had been paid by direct debit. As we have found that the Company had a reasonable excuse for paying £304,735.68 on 10 August 2017 we consider that only £200,000.00 was outstanding in accordance with section 59(4)(b) and accordingly a surcharge at 2% of this amount is the appropriate default surcharge to use the language of section 84(6). We consider that this is the correct position in view of the exception allowed in section 84(6).

47. Having reached the decision which we did in paragraph 40 it would be totally wrong to then proceed to allow the appeal in full or to dismiss the appeal entirely. Our decision falls within the requirements of section 59(4)(b) and section 59(7)(b).

48. 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.

ALASTAIR J RANKIN
TRIBUNAL JUDGE

RELEASE DATE: 3 MAY 2018