[2021] UKFTT 0260 (TC)

TC08206

VAT – default surcharge – whether reasonable excuse – correspondence not received – no – whether disproportionate – high turnover/low margin business – no – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2018/06498

BETWEEN

ONE MOTION LOGISTICS LTD **Appellant**

-and-

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

TRIBUNAL: JUDGE ANNE FAIRPO

The hearing took place on 9 July 2020. With the consent of the parties, the hearing took place via the Tribunal video hearing platform. A face to face hearing was not held because of restrictions arising from the coronavirus pandemic. The documents to which I was referred are a bundle of documents of 219 pages, a joint authorities bundle of 115, the parties' skeleton arguments. After the hearing, both parties provided written submissions with regard to the proportionality point discussed below.

Mr Symonds, Counsel for the Appellant

Ms Parlour, litigator of HM Revenue and Customs' Solicitor's Office, for the Respondents

DECISION

Introduction

1. This is an appeal against VAT surcharge penalties for the 05/18 VAT period under s59A Value Added Tax Act 1994 ('VATA 1994'). The appellant originally also appealed against penalties for the 02/18 period, but withdrew this aspect of their appeal at the hearing.

Background

2. The appellant has been registered for VAT since 25 February 2014.

3. The appellant entered the surcharge regime in the 08/16 period as the payment for that period was ten days late. As this was the first default, no surcharge was payable but a surcharge liability notice was issued. The appellant defaulted again in the 02/17 period as the payment was three days late. A 2% surcharge liability notice was issued, extending the surcharge period.

4. On 22 November 2017 HMRC wrote to the appellant directing them to make payments on account in respect of VAT (under s28(2A) VATA 1994) because the appellant's total VAT liability in the qualifying period exceeded £2.3m. The letter set out the monthly payments to be made by the appellant for the 02/18 and 05/18 periods, including the amounts and due dates as follows:

   (1) For 02/18: £98,301 due on each of 31 January 2018 and 28 February 2018, with the balance due by 29 March 2018.

   (2) For 05/18: £98, 301 due on each of 30 April 2018 and 31 May 2018, with the balance due by 29 June 2018.

5. The letter confirmed that businesses within the Payments on Account (POA) regime are not entitled to the seven day extension to the due date for payments made electronically. The letter also confirmed that business within the POA regime are similarly not entitled to the associated seven day extension for filing their VAT return. The letter advised the appellant to cancel their direct debit for VAT as POA payments cannot be made by direct debit, and also advised that it normally takes three bank working days for payments to reach HMRC's bank account. The letter included a reminder that late payments are subject to default surcharge.

6. For the 02/18 period, the payment due on 31 January 2018 was received five days late on 5 February 2018. The 28 February 2018 payment was received on time. The Return was received seven days late on 7 April 2018 and the balancing payment was received nine days late on 9 April 2018.

7. For the 05/18 period, the payment due on 30 April 2018 was received two days late on 2 May 2018. The payment due on 31 May 2018 was received on time. The return and balancing payment were received eight days late on 7 July 2018.

8. There is no dispute as to when the returns and payments were made, nor as to the fact that they were made late. The question for this Tribunal is whether the appellant has a reasonable excuse for the defaults.

Appellant's evidence and submissions

Evidence

9. Mr Hershey, head of operations for the appellant, provided a witness statement and gave oral evidence at the hearing.

10. Mr Hershey confirmed that he had received the 22 November 2017 letter which directed the appellant to make payments on account, but had not paid close attention to it as he had sent it to the appellant's accountants and he relied on them to tell him when to pay VAT.

11. The accountants, Silver Levene, were engaged to review all financial information for the appellant's VAT returns and finalise those returns. Mr Hershey confirmed that he filed returns once they were approved by the accountants, and would be guided by the accountants as to the amount to pay in respect of VAT.

12. Mr Hershey stated that he only became aware that surcharges had arisen when he received a letter from HMRC dated 17 July 2019 which advised that the appellant was liable to a surcharge in respect of the 05/18 quarter for failing to make payments on time. He had not received the following correspondence from HMRC until after the surcharge notice for the 05/18 period was received:

(1) 26 February 2018 letter advising that a payment was late;

(2) 18 April 2018 letter advising of a surcharge for the 02/18 quarter for failing to make payments on time; and

(3) 20 April 2018 advising of the due dates for payments under the POA regime for the next three quarters.

13. Mr Hershey's evidence was that correspondence was received by the appellant's mailing department. Letters were scanned and a soft copy sent to the relevant employees. HMRC correspondence soft copies would be sent to Mr Hershey alone.

14. Mr Hershey noted that HMRC had been sending correspondence to a postal code ending "7HG", which does not exist. The appellant's address had a postal code ending "7HJ". The rest of the address used by HMRC, including the first part of the postal code, was correct.

15. Mr Hershey stated that he had always considered that VAT was payable on the seventh day of the second month following the end of the VAT quarter and had not been aware that the seven days extension of time for electronic payments was not available when entering the payment of account regime. As such, he had believed that he was paying the appellant's VAT liabilities on time when making payment on or before the seventh day of the second month following the end of the VAT period.

16. With regard to the late payment of the VAT balancing payment for the 02/18 period, Mr Hershey's evidence was that this had been paid on Saturday, 7 April 2018. It appeared that the bank must have processed the payment on the following working day, as it arrived with HMRC on Monday, 9 April 2018. Mr Hershey provided documents to show that the payment was actioned on 7 April 2019.

17. Mr Hershey confirmed that he had made payments on account on behalf of the appellant as follows:

(1) in respect of the 02/18 period:

(a) on 5 February 2018;

(b) on 27 February 2018;

(c) the balancing payment in April 2019 as above

(2) in respect of the 05/18 period:

(a) on 30 April 2018;

(b) on 30 May 2018 ;

(c) the balancing payment on 7 July 2018

18. Mr Hershey accepted that these payments showed that the company was aware that payments on account were required.

19. Ms Shah, an accountant at Silver Levene also provided a witness statement and gave oral evidence at the hearing. She had become the engagement manager for the appellant in March 2018 when the previous engagement manager left the firm. She became aware of the surcharges when advised by the appellant in July 2018 that they had received a surcharge letter from HMRC. The correspondence of 26 February 2018, 18 April 2018 and 20 April 2018 had not been received by Silver Levene. HMRC correspondence was sent to the appellant only, not to Silver Levene.

20. Ms Shah stated that she did not realised that the appellant was required to make payments on account of VAT: the information provided to the appellant as to payments to be made took into account information from the appellant's bank statement which showed that payments had been made to HMRC in respect of VAT.

21. The previous engagement manager had not explained that the appellant was making payments on account, nor had she explained the dates on which the appellant's VAT payments were required. HMRC's telephone conversations with 'Carly" had occurred before Ms Shah became the engagement manager. Carly was part of the corporate tax team for the appellant at Silver Levene: although it was possible that Carly had passed on the information to the previous adviser, Ms Shah had not been informed of the conversations. She accepted that the conversations between HMRC and Carly meant that Silver Levene were aware in February 2018 that a payment on account had not been made on time and that Silver Levene were aware that the appellant was within the POA regime.

22. Ms Shah had believed that the seven day extension for making payment electronically applied to businesses which had to pay VAT on account. She had advised the appellant to make VAT payment for the 02/18 period by 7 April 2018 and for the 05/18 period by 7 July 2018.

23. Mr Beale, parter at Silver Levene, gave evidence that no correspondence was received by Silver Levene directly from HMRC in respect of the appellant: all correspondence was forwarded by Mr Hershey or a member of his team. This was not challenged.

Submissions

Reasonable excuse

24. For the appellant, it was submitted that there was a reasonable excuse for the late payments for the 05/18 period because the reminder letter of February 2018, the surcharge liability notice for the 02/18 period, and the POA letter of 20 April 2018 had not been received by the appellant, and so they were not put on notice for the 05/18 period that the payments were late and that they were wrong to believe that the seven day extension period was available. HMRC had produced no evidence that the correspondence was posted to the appellant.

25. There had been an inadequate handover within Silver Levene, as there had been no explanation by the outgoing manager, which meant that the new engagement manager was unaware that the appellant was no longer entitled to the extension; this was also contended to be a reasonable excuse for the delays.

Proportionality

26. It was further submitted that the penalty was disproportionate as, given that the appellant had a high turnover/low margin business, the penalty was a substantial proportion (approximately 6-7%) of the profit and also a substantial proportion (88%) of the corporation tax liability for the relevant tax year of the appellant. This was an honest mistake, and the appellant had always intended to comply with their tax obligations.

27. The appellant contended that guiding principle, per *Trinity Mirror* [2015] UKUT 421 (TCC) §63 and other similar cases, regarding proportionality is to consider the gravity of the infringement and whether the level of the penalty is such that it is disproportionate to ensuring

fiscal neutrality. The requirement for proportionality is imported from the requirements of EU law, which also require that amount be taken of "good faith" on the part of the taxpayer in considering whether a penalty was disproportionate (*Louloudakis* C-262/99 at §77). The Upper Tribunal in *Total Technology* (§§52-72) concluded that penalties should not exceed what is "appropriate and necessary" to achieve a legitimate aim, being the efficient collection of VAT. In that case, the Upper Tribunal concluded that a penalty of £4,260 was proportionate for a second default that was one day late, but was swayed by the fact that the penalty was substantially less than that incurred in another case (*Enersys*). In *Enersys*, the Tribunal had considered that the penalty was disproportionate because it was so large. The CJEU in *Márton* (C-210/10) had considered that a fixed penalty rate of 100,000 Hungarian Fortuns (approximately €332 at the time) has been disproportionate because it did not take into account the circumstances of the individual case, and the fine was almost equivalent t the net monthly income of an employee in Hungary and was disproportionate to the infringement.

28. It was submitted that applying these principles to the appellant, the penalties were disproportionate because:

(1) it was large in amount (being larger than the penalty in Upper Tribunal which was acknowledged to be large in absolute terms) and disproportionate to the gravity of the infringement;

(2) the taxpayer had acted in good faith: the switch to the POA regime had caused some confusion for the appellant and its advisers and, if the surcharge notice for the 02/18 quarter had been received, the appellant would have been alerted to the fact that it was not making payments on time.

(3) the penalties are individually and cumulatively completely disproportionate for a high turnover/low margin business such as the appellant.

29. It was submitted that the appellant's case could be distinguished from *Trinity Mirror*, because neither the taxpayer nor the Tribunal had made any reference to what relation the penalty bore to profitability or the corporate tax liability, perhaps because neither factor assisted the taxpayer. The case can also be distinguished from *Total Technology* which involved a very low surcharge penalty.

30. It was submitted that this is a wholly exceptional case because the penalties individually constitute just under one month of the appellant's profit and around 40% of its corporate tax liability and cumulatively constitute around two months of profit and 87% of corporate tax liability for the relevant period. The infringements were relatively minor and were honest mistakes.

HMRC submissions

Reasonable excuse

31. HMRC submitted that the approach to be taken in respect of reasonable excuse was that set out in the case of *Perrin* [2018] UKUT 0156 (TCC), requiring the Tribunal to consider the particular circumstances in which the failure occurred as well as the particular circumstances and abilities of the person concerned who failed in this obligation. The Tribunal is then required to consider what a reasonable person, who wanted to comply with their tax obligations, would have done in the same circumstances and decide if the actions of the person met that standard.

32. HMRC contended that the appellant was, for the 02/18 and 05/18 periods, already in the surcharge regime: the surcharge for the 02/18 period was 5% of the relevant VAT and so had followed a default surcharge of 2% as well as the correspondence advising of the initial default. The surcharge for the 05/18 period was 10% as it was the third surcharge penalty arising.

33. HMRC submitted that the incorrect postcode did not mean that the disputed correspondence in February and May 2018 had not been properly served. The address had been set in 2016 and no correspondence since that date had been returned undelivered to HMRC in respect of the appellant. The appellant had confirmed that they had received the letters dated 22 November 2017 and the surcharge in May 2018. The same address had been used for all of the correspondence. HMRC submitted that the correspondence had been correctly served.

34. HMRC provided call logs which showed that HMRC had attempted to contact the appellant and their accountants when the first payment for the 02/18 period was made late. On 15 February 2018, a person named Carly at Silver Levene had taken details and stated that they would arrange for one of the VAT team to return the call. Carly had stated that the appellant was new to the POA regime. On 26 February 2018, a further call with Carly included confirmation from Carly that the late payment had now been made and a reminder from HMRC that a further payment was due on 28 February 2018.

35. HMRC submitted that the appellant's advisers had therefore been aware by 26 February 2018 that the first instalment of the POA regime was made late. The failure to communicate this internally by the accountants does not provide the appellant with a reasonable excuse for the late payment.

36. HMRC further submitted that, regardless of any arrangements made with the accountants, the appellant (via its directors) was ultimately liable for the timely submission of VAT returns and payments. Any reliance placed on a third party to undertake all or part of these obligations, and the failure of such third party, could not provide a reasonable excuse (s71(1)(b) VATA 1994).

37. HMRC contended that the obligations under the POA regime did not involve any complicated questions of law and the details were clearly set out in the letter of 22 November 2017, which the appellant and their accountants had confirmed had been received. That letter, and the letter of 20 April 2018 clearly states that the seven day extension for electronic payments is not available under the POA regime. HMRC submitted that a responsible trader would have taken note of the details and the effect on their tax responsibilities, including dates for payment and returns.

38. HMRC further contended that the appellant was aware of the instalment amounts and due dates because payments on account had been made on 5 and 27 February 2018, with further payments on account on 2 and 30 May 2018. It was unlikely that the appellant would have made payments on these dates unless they, or their agent, were aware that the appellant was required to make payments on account.

39. HMRC further contended that an insufficient handover between employees of the appellant's agent is not a reasonable excuse. HMRC would have expected the appellant or their agent to have exercised some due diligence and checked the requirements of the POA regime and noted the due dates accordingly.

40. HMRC considered that the oversight by the appellant and their agent in not noticing the information in the letter of 22 November 2017 is a genuine error, but a genuine error is not a reasonable excuse for the failure (per *Garnmoss Ltd* [2012] UKFFT315 (TC)). Following *Perrin*, the mistaken belief that the seven day extension was available does not amount to an objectively reasonable excuse for the defaults.

Proportionality

41. HMRC contended that the Upper Tribunal decision in *Trinity Mirror*, which is binding on this Tribunal, supports the position that the default surcharges charges are not disproportionate. Specifically, the Upper Tribunal concluded that (§65-67):

> "the default surcharge regime, viewed as a whole, is a rational scheme. The penalties are financial penalties, calculated by reference to the amount of tax unpaid at the due date … In common with the Upper Tribunal in *Total Technology,* we consider that the use of the amount unpaid as the objective factor by which the amount of the surcharge varies is not a flaw in the system; to the contrary, the achievement of the aim of fiscal neutrality depends on the timely payment of the amount due, and that criterion is therefore an appropriate, if not the most appropriate, factor. … the absence of any financial limit on the level of surcharge may result in an individual case in a penalty that might be considered disproportionate. … given the structure of the default surcharge regime … this is likely to occur only in a wholly exceptional case, dependent upon its own particular circumstances … we cannot ourselves readily identify common characteristics of a case where such a challenge to a default surcharge would be likely to succeed … whilst it might be tempting to seek to isolate, and thus confine, cases by reference to particular criteria, such cases, by reason of their exceptional nature, are likely to defy such characterisation."

42. HMRC submitted that this was not a wholly exceptional case. The appellant had failed to meet their tax obligations and had been issued with penalties in accordance with the legislation. The matter cannot be distinguished from *Trinity Mirror*. With regard to the amount of the penalty, the Upper Tribunal in *Trinity Mirror* had criticised the application of *Enersys* as, in assessing the gravity of the default, the amount of VAT unpaid is an essential element of the statutory regime. The appellant's reference to the Tribunal's comment in *Trinity Mirror* that a penalty of £70,000 was large in absolute terms needs to be considered in the wider context of that case, in which the Upper Tribunal noted that the size of the penalty was dictated by the substantial amount of VAT paid late and the surcharge percentage. The Upper Tribunal concluded that this was entirely consistent with the fiscal neutrality of the regime.

43. Further, the appellant's submissions that the penalty is disproportionate to their profitability are not relevant, as the penalty is not calculated by reference to profits. For similar reasons, the case of *Márton* is not applicable, as that referred to a flat rate fine which is wholly different to the escalating penalty regime in this case.

44. HMRC submitted that the appellant failed to consider information provided by HMRC in correspondence with the appellant acknowledged receiving. The appellant was aware of the payment schedule and made payments accordingly. HMRC submitted that it was in the wider social interest for consequences to be met for a failure by a taxpayer to meet tax obligations, in accordance with the underlying objective of the default surcharge system.

Relevant law

45. The default surcharges for the periods 02/18 and 05/18 were issued under s59A Value Added Tax Act (VATA) 1994. s59A (8)(ii) VATA 1994 provides that a surcharge does not arise if … on appeal, a Tribunal are satisfied that the person had a reasonable excuse for the failure for the payment not having been made on time.

Discussion

Reasonable excuse

46. The Upper Tribunal in *Perrin* held that "to be a reasonable excuse, the excuse must not only be genuine, but also objectively reasonable when the circumstances and attributes of the actual taxpayer are taken into account" (§75).

47. It is clear that the appellant and its advisers believed that the seven-day extension was available to them for the VAT payments due, and endeavoured to make payments accordingly. However, viewed objectively, I do not consider that this amounts to a reasonable excuse for

the default. The appellant agrees that they received HMRC's letter of 22 November 2017, which clearly states that the extension is not available.

48. The fact that the appellant did not pay much attention to this letter cannot provide them with a reasonable excuse: a reasonable taxpayer in the position of the appellant would, in my view, have made sure that they understood what the letter required of them in respect of their VAT obligations.

49. To the extent that the failures arose because of miscommunication within the appellant's accountants and the new engagement manager's failure to realise that the POA regime precluded the use of the seven-day extension, this also does not give rise to a reasonable excuse: reliance on a third party is not a reasonable excuse in this context. The November 2017 letter from HMRC had been provided to the accountants and they had advised the appellant to make the required payments on account and, even if they had previously been unaware that the extension does not apply within the POA regime, that letter provides that information (as noted above).

50. The appellant also argues that, as they did not receive correspondence from HMRC in February and April 2018, they have a reasonable excuse for not being aware that the payments were being made late.

51. s98 VATA 1994 makes provision for notices and other documents to be served by HMRC on taxpayers by post to the taxpayer's last or usual residence or place of business. s7 Interpretation Act 1978 provides that service by post is effected by properly addressing, pre-paying and posting a letter containing the document, and unless the contrary is proved, to have been effected at the time at which the letter would be delivered in the ordinary course of post.

52. The incorrect letter used by HMRC at the end of the appellant's postcode does not, in my view, mean that the above legislation does not apply. The appellant noted that the incorrect postcode is in fact non-existent and so it is not likely that the correspondence was diverted to a different place. All other correspondence from HMRC with that address has been received by the appellant. The appellant did not note that there had been any difficulty receiving any other correspondence during the period in question. Further, I consider that the evidence of Mr Hershey was that he personally had not received those letters. Given that the appellant's mail is received and scanned, it appears possible that the correspondence was in fact received and was misdirected within the appellant's systems. There was no evidence that any search had been made to establish whether the correspondence had been so misdirected.

53. As noted above, unless the contrary is proved, the surcharge liability notice issued in April 2018 is deemed to be served at the time when the envelope would be delivered in the ordinary course of post. The "contrary is proved" if the appellant demonstrates, on the balance of probabilities, that they did not receive the notice. I do not consider that the appellant has demonstrated that it (the company) did not receive the notice, even if Mr Hershey had not received a copy of it from the mail department of the appellant.

54. In addition, I find that HMRC had advised the appellant's accountants in February 2018 that payments were not being made on time. As noted above, any failure of communication within the accountants cannot amount to a reasonable excuse for the appellant's failure to make payments on time.

55. Viewed objectively, I do not consider that the fact that Mr Hershey personally did not see the relevant HMRC correspondence can amount to a reasonable excuse: all the relevant information was provided in HMRC's letter of November 2017, which was received and acted on to an extent. A taxpayer acting reasonably would not be reliant on a reminder from HMRC to comply with their obligations.

56. I conclude, therefore, that the appellant did not have a reasonable excuse for the failures.

Proportionality

57. The approach for this Tribunal with regard to proportionality is set out by the Upper Tribunal in *Trinity Mirror* (§63):

> "The correct approach is to determine whether the penalty goes beyond what is strictly necessary for the objectives pursued by the default surcharge regime, as discussed in detail in *Total Technology* and whether the penalty is so disproportionate to the gravity of the infringement that it becomes an obstacle to the achievement of the underlying aim of the directive which, in this context, we have identified as that of fiscal neutrality".

The Upper Tribunal in *Trinity Mirror* considered the preceding case law in both *Total Technology* and *Enersys* in making its decision and setting out this approach.

58. Further guidance was given as the decision in *Trinity Mirror* also approved of the conclusion of the Upper Tribunal in *Total Technology* that the penalty scheme as a whole was proportionate and fair, and quoted §84 of the decision in *Total Technology* which considered that:

> "[the] 'reasonable excuse' exception strikes a fair balance. The gravity of the infringement is reflected in the absence of 'reasonable excuse' and the amount of the penalty reflects the extent of the default, that is to say the amount of tax not paid by the due date."

59. With regard to the circumstances of the appellant, the Upper Tribunal in *Trinity Mirror* noted (§66) that:

> "the absence of any financial limit on the level of surcharge may result in an individual case in a penalty that might be considered disproportionate … we cannot ourselves readily identify common characteristics of a case where such a challenge to a default surcharge would be likely to succeed."

60. There is, unfortunately, nothing exceptional about the high turnover/low profit nature of the appellant: I consider that, if the Upper Tribunal in *Trinity Mirror* had considered that this would be exceptional, it would have been readily able to identify those characteristics. The fact that the penalty could be considered to be large in comparison to the appellant's profit and corporation tax liability also does not make this an exceptional case: the same would apply to any taxpayer with a high turnover/low profit business model which made late payments of VAT and thus entered the surcharge regime.

61. I note that the case of *Márton,* raised by the appellant, related to a fixed rate fine which did not take into account the circumstances of an individual case. The 'reasonable excuse' exemption provided by UK law means that the surcharge penalty regime does take into account the circumstances of an individual case. The surcharge penalty regime also does not impose fixed fines: the decision in *Trinity Mirror* makes it clear that the regime is not made disproportionate by the penalty being based on the relevant VAT.

62. With regard to the appellant's submissions as to the importance of 'good faith', I note that the CJEU in *Louloudakis* concluded that ignorance of the law does not provide exoneration from penalties but that "where determination of the arrangements applicable has given rise to difficulties, account must be taken of the good faith of the offender when determining the penalty actually imposed" (§77). That is, that 'good faith' should be a factor where the law and/or its application is unclear. The 'good faith' element which the appellant contends is relevant is, in my view, already accounted for in the exception available in UK law for a 'reasonable excuse', as noted in *Total Technology* and considered in the context of *Perrin*.

63. I do not consider that the CJEU's decision in *Louloudakis* gives any reason to find this penalty disproportionate: there is nothing complex or unclear about the POA regime and its application to the appellant. The penalty is not disproportionate simply because the appellant and its advisers were 'confused' by the POA regime and Mr Hershey had not seen the surcharge notice for the 02/18. All of the relevant requirements were clearly set out in the HMRC letter of 22 November 2017.

64. I conclude, therefore, that the penalty is not so disproportionate as to constitute an obstacle to the underlying aim of the legislation.

Decision

65. For the reasons set out above, the appeal is dismissed.

Right to apply for permission to appeal

66. 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.

ANNE FAIRPO
TRIBUNAL JUDGE

RELEASE DATE: 12 JULY 2021