TC01827

Appeal number: TC/2011/05956

Appeal against penalty for failure to make PAYE payments on time – reasonable excuse – cash flow difficulties – failure by HMRC to advertise new penalty system – reallocation – appeal dismissed

FIRST-TIER TRIBUNAL

TAX

CHIEFTAIN TRAILERS LIMITED **Appellant**

- and -

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

TRIBUNAL: J. BLEWITT (JUDGE)

Sitting in public at Belfast on 15 November 2011

Mr Thompson, for the Appellant

Mr Chapman, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

The Appeal

1. By Notice of Appeal dated 2 August 2011 the Appellant appealed against the penalty of £13,024.15 incurred as a result of making late PAYE payments in the tax year 2010/2011.

2. The grounds of appeal relied upon by the Appellant and set out in the Notice of Appeal are:

(a) That the Appellant was experiencing cash flow management difficulties;

(b) That HMRC failed to advertise the new penalties adequately and did not inform the Appellant directly of the severity and operation of the new penalty regime, as a result of which the Appellant did not take steps to mitigate the penalties;

(c) That in the case of ***Kincaid v HMRC*** *[2011] UKFTT 225* the Tribunal accepted that cash flow difficulties could amount to reasonable excuse;

(d) That the Appellant wishes to reallocate payments made for 2010/2011 which would reduce the amount of the penalty.

Law

3. The parties agreed that the relevant legislation is Schedule 56 of the Finance Act 2009, which provides for penalties to be imposed in respect of tax payable under the PAYE regulations:

"1)A penalty is payable by a person ("P") where P fails to pay an amount of tax specified in column 3 of the Table below on or before the date specified in column 4.."

4. Schedule 56 paragraph 6 (1) to (8) provides for the amount of the penalty:

6(1)P is liable to a penalty under this paragraph of an amount determined by reference to the number of defaults in relation to the same tax that P has made during the tax year.

(2)P makes a default in relation to a tax when P fails to pay an amount of that tax in full on or before the date on which it becomes due and payable.

(3)But the first failure during a tax year to pay an amount of tax does not count as a default in relation to that tax during that tax year.

(4)If P makes 1, 2 or 3 defaults during the tax year, P is liable to penalty of 1% of the total amount of those defaults.

(5)If P makes 4, 5 or 6 defaults during the tax year, P is liable to penalty of 2% of the total amount of those defaults.

(6)If P makes 7, 8 or 9 defaults during the tax year, P is liable to penalty of 3% of the total amount of those defaults.

(7)If P makes 10 or more defaults during the tax year, P is liable to penalty of 4% of the total amount of those defaults.

(8)In this paragraph—

(a)in accordance with sub-paragraph (1), the references in sub-paragraphs (4) to (7) to a default are references to a default in relation to the tax mentioned in sub-paragraph (3),

(b)the amount of a default is the amount which P fails to pay, and

(c)a default counts for the purposes of sub-paragraphs (4) to (7) even if the default is remedied before the end of the tax year.

5. If the taxpayer can show that there was a reasonable excuse for the failure to make payment on time, the liability does not arise:

16(1)Liability to a penalty under any paragraph of this Schedule does not arise in relation to a failure to make a payment if P satisfies HMRC or (on appeal) the First-tier Tribunal or Upper Tribunal that there is a reasonable excuse for the failure.

(2)For the purposes of sub-paragraph (1)—

(a)an insufficiency of funds is not a reasonable excuse unless attributable to events outside P's control,

(b)where P relies on any other person to do anything, that is not a reasonable excuse unless P took reasonable care to avoid the failure, and

(c)where P had a reasonable excuse for the failure but the excuse has ceased, P is to be treated as having continued to have the excuse if the failure is remedied without unreasonable delay after the excuse ceased.

Evidence and Submissions on behalf of the Appellant

6. There were three witnesses for the Appellant and I will deal with the evidence given by each in turn.

Mr McGee

7. Mr McGee is a qualified accountant employed by Moore Stephens who act on behalf of the Appellant.

8. Mr McGee exhibited a document showing that of the Appellant's total tax liability of £359,737.28, the sum of £335,951.01 had been paid. Mr McGee did not dispute that the Appellant's 2010/2011 PAYE payments had been made late but submitted, with reference to a document prepared on behalf of the Appellant, that if

the payments made were reallocated the penalty would be reduced to £1,734.16. By way of example, it was submitted that if the payment due on 19 June 2010 which was paid by the Appellant on 2 July 2010 was allocated to the liability which arose in July, instead of the May liability, then the result (in following Mr McGee's reallocation process for the whole of the 2010/2011 period) would be that the penalties would be charged at 2% as opposed to the 4% submitted by HMRC and the total amount of the penalty would be considerably reduced.

9. Mr McGee referred to HMRC's internal guidance *"DMBM520075 Debt and return pursuit: PAYE: Introduction to PAYE: Payments: Re-allocations and repayments"* which contains a section headed *"Noting Records"* which gives guidance as to the type of information which should be recorded where reallocation is carried out, including as an example the name and role of the person (such as accountant) who authorised the reallocation.

10. Mr McGee submitted that such a document envisages reallocation being carried out, yet in this case the suggestion that this be done was rejected by HMRC.

11. In cross examination Mr McGee accepted that the cheque sent in by the Appellant would be in the amount of the month's liability to which it related and that the allocation would also be determined by the payslip which accompanied the payment, which would state the month to which the payment was made.

12. Mr McGee clarified that the two figures contained on the document showing allocation made by HMRC under the heading "balance per HMRC" (£13,024.15 and £12,250.63) related to confusion in HMRC's correspondence where both had been quoted at different times. It was agreed by both parties that, subject to the issue of reasonable excuse, the correct figure of the penalty was £13,024.15.

Mr Quinn

13. Mr Quinn is the Managing Director of the Appellant Company. Mr Quinn explained that prior to 2008 30% of the Company's business was in Ireland and the remaining 70% in the UK. As a result of the current economic climate, Mr Quinn stated that the Company had been forced to make significant changes, with the result that 30% of the Company's business is in the UK and Ireland and the remainder in countries including as Scandinavia, Finland, France and Australia.

14. Mr Quinn stated that the Company had, since the start of the recession in 2008, been approximately two months in arrears but as a result of the cost cutting exercises carried out the Company is now up to date with PAYE payments.

15. In cross examination, Mr Quinn stated that he was not aware of the Business Payment Support Scheme offered by HMRC although he believed that there had been "Time To Pay" arrangements agreed with HMRC. Mr Quinn agreed that such arrangements were not in place for each of the months in which payments were made late and stated that if the Company had the money it paid its liability, if not payments were made in instalments.

Mrs Cavanagh

16. Mrs Cavanagh is a qualified chartered accountant who worked for the Appellant Company on a freelance basis approximately 3 to 4 days per month.

17. Mrs Cavanagh explained that she had been responsible for allocating the payments made by the Appellant against the longest outstanding debt, as was usual commercial practice and that she had not realised the impact of so doing on the potential penalties.

18. Mrs Cavanagh was referred to a standard warning letter issued by HMRC to taxpayers where PAYE was not paid on time. Mrs Cavanagh stated that she did not recall receiving such a letter and that even if she had read its contents she would not have changed the allocation procedure used by the Appellant Company as the letter made no reference to set penalties. Mrs Cavanagh accepted that she may not have seen the letter as she did not work at the Appellant Company full time, but added that she had not seen such a letter in the course of her employment for other companies either.

19. Mrs Cavanagh stated that the new penalty regime had been explained to her for the first time on 15 June 2011, at which time she immediately changed the allocation method used in order to minimise the Appellant's exposure to penalties by paying the new liabilities before the older ones.

20. In cross examination Mrs Cavanagh was referred to telephone records print outs exhibited by HMRC. In a telephone call to HMRC on 31 August 2010 the record indicated that Mrs Cavanagh was warned of local action and late payment penalties as the code "WLAP" was recorded on the log. Mr Cavanagh stated that she had not been informed that if all payments were late, set penalties in % sums of the liability would be incurred.

Submissions

21. Mr Thompson helpfully set out in writing the submissions on behalf of the Appellant. The three issues relied upon in support of the appeal were allocation, reasonable excuse and fairness/conscionable behaviour.

22. On the issue of allocation, Mr Thompson submitted that the level of penalties would be greatly reduced if Mrs Cavanagh had:

(a) Indicated a different allocation when submitting payments; or

(b) Submitted no allocation (as HMRC undertake to allocate to the best advantage of the taxpayer); or

(c) Was allowed to reallocate.

23. It was accepted that the allocations were made by Mrs Cavanagh on the erroneous assumption that it was in the best interests of the Appellant to pay the earliest liability first as is standard commercial practice.

24. It was submitted that there is no provision within the legislation allowing for error and that HMRC had itself misallocated one of the penalties which supports the assertion that the initial allocation should not be too heavily relied upon.

25. As regards reasonable excuse, Mr Thompson submitted that the Appellant fell behind in making payments a number of years ago, and that given the economic crisis and unavailability of credit it found it impossible to raise the necessary funds until recently.

26. Mr Thompson relied upon the following cases in support of his submission that cash flow has been accepted by the Tribunal in other cases as amounting to a reasonable excuse:

(a) ***N A Dudley Electrical Contractors v HMRC*** *[UKFTT] 260 (TC)*

(b) ***Kincaid v HMRC*** *[2011] UKFTT 225 (TC)*

27. Mr Thompson submitted that there had been a mistake of fact in this case in that Mrs Cavanagh was not aware of how the penalty regime operated and that the warning letter sent by HMRC to the Appellant (which was not accepted) did not outline the operation of the new regime. The allocations had, it was submitted, been made on the basis of a mistake in fact. The case of ***Anthony Leachman T/A Whiteley and Leachman v HMRC*** *[2011] UKFTT 261 (TC)* was cited by Mr Thompson in support of his submission.

28. The final ground relied upon by the Appellant was that of fairness and conscionable behaviour. The written submission on behalf of the Appellant state that *"the facts of this case are such that it is unclear that HMRC have behaved in a fair and conscionable manner at all times...it must have been obvious to HMRC from the start, particularly given its presumed knowledge of the client's payment practices, that such a penalty was likely to arise...it would have been fair for HMRC to make this clear to CTL at the earliest possible stage."*

29. Mr Thompson submitted that the warning letter sent out to taxpayers by HMRC does not explain the operation of the penalty system and that it would be fair for HMRC to make such points clear in a letter.

30. It was submitted that ignorance of the penalty system has led to the Appellant being punished for the assistance given by allocating its payments; a less diligent taxpayer who made no such effort would benefit. The intention of the legislation is to penalise delinquent taxpayers who made few payments, not the Appellant who made 22 payments. It was submitted that there are insufficient grounds for HMRC to charge the maximum penalty.

31. Mr Thomson cited the case of ***Hok Limited v HMRC*** *[2011] UKFTT 433 (TC)* in support of his contention that HMRC must act fairly, the purpose of the penalty system being to discourage default as opposed to generate cash. In this case, Mr Thompson submitted, HMRC had acted unfairly in demanding the penalty imposed.

Evidence and Submissions on behalf of HMRC

32. Mr Chapman helpfully set out the legislation which provides for the making of PAYE payments and determination of penalties, about which there was no dispute.

33. I was referred to a table showing the number of days each payment was made late, which covered the period 19 May 2010 to 22 April 2011 and which showed that each month the payments had been made late, ranging from 3 days to 59 days after the payment was due.

34. Mr Chapman relied on paragraph 16 (2) of Schedule 56 Finance Act 2009 which specifically excludes insufficiency of funds as a reasonable excuse, although he accepted that there were exceptions to the rule, such as occasions where cash flow difficulties were beyond the control of the taxpayer. It was submitted that the exception did not apply in this case as the Appellant had been habitually late in making payments for over 5 years, showing that there was a pattern of late payments as opposed to a single, unforeseeable event. Further, it was submitted that the fact that the Appellant is now making payments on time is support for the contention that it is not beyond the Appellant to meet the payment deadlines.

35. Mr Chapman referred me to a standard letter sent by HMRC to taxpayers who have made a PAYE payment late. Mr Chapman confirmed that HMRC's records showed that such a letter had been sent by HMRC to the Appellant on 28 May 2010. Mr Chapman also highlighted the fact that information is readily available on HMRC's website, addressing the issues of penalties and Time To Pay arrangements, the latter being available to taxpayers experiencing difficulties in meeting their liability.

36. Mr Chapman stated that information packs had also been sent out in February 2010 to all taxpayers making PAYE payments and that further information had been contained in monthly employer bulletins, copies of which were provided to me.

37. Records of telephone conversations between HMRC and Mrs Cavanagh were exhibited by Mr Chapman, showing that a number of messages had been left by HMRC for the Appellant to make contact and that Mrs Cavanagh had, on at least two occasions, spoken directly to an HMRC employee. On 31 August 2010, HMRC's record showed Mrs Cavanagh arranged time to pay over one month due to cash flow difficulties. The code "WLAP" was contained on the record which refers to "warned of local action and late penalty payments." A further telephone conversation on 29 October 2010 recorded Mrs Cavanagh's explanation that the Appellant was experiencing cash flow difficulties and that future payments would be sent by 22nd of the month. The code "WP" is contained on the record, which refers to "warned of penalties."

38. Mr Chapman submitted that the reallocation offer made by the Appellant could not be accepted by HMRC as the allocation had been specified by the Appellant when the payments were made. Furthermore, as the tax/NICs were deducted in specific months, the payments made relating to a specific month could not be changed to a different month in order to mitigate the penalty. Mr Chapman submitted that to do so

would be to defeat the purpose of the legislation, which was to ensure that all employers were treated equally and without unfair advantage.

39. Mr Chapman submitted that there had been no mistake of fact and that Mrs Cavanagh's ignorance of the law could not amount to such on the facts of this case.

Decision

Allocation

40. The reallocation process undertaken by Mr McGee and submitted to HMRC in an attempt to mitigate the Appellant's penalty in my view was misconceived. The fact that the penalties would be reduced if a different course of action had been taken does not amount to a reasonable excuse.

41. I found as a fact that the Appellant, through Mrs Cavanagh had determined the allocation process by which HMRC were bound. The payments made by the Appellant related to a specific month's liability, which was confirmed by the payslip. I found as a fact that there is no obligation on HMRC, of its own volition and without the consent of the taxpayer, to deliberately ignore such allocation; indeed had it done so, serious concerns would no doubt be raised.

42. Further, there was no attempt to reallocate payments until 2 August 2011; after all payments had been made. In my view this was simply too late. The purpose of the legislation is to ensure that all taxpayers are treated equally and that there is compliance with the legislation. To allow the Appellant to reduce his penalties so long after their imposition by reallocating payments would undermine the purpose of the legislation as the incentive to comply would be lost in the knowledge that penalties could be reduced or quashed.

43. I considered the guidance of HMRC to which I was referred. I accepted that reallocation is possible; however I found as a fact that the guidance makes clear that this would be done with the authority of the taxpayer. The guidance specifically states that where a payment is reallocated, a note should be made to include information such as "name and role of the person...who has authorised the payment reallocation." I found as a fact that this corroborated the conclusion that ultimate responsibility and authority rests with the taxpayer.

Reasonable excuse

44. Case law has made clear that there are occasions on which cash flow difficulties, albeit specifically excluded by the legislation, can amount to reasonable excuse. In many cases, it is not the cash flow difficulties per se that amounts to reasonable excuse, but rather the unexpected or unforeseeable cause of such difficulties.

45. I considered the case of ***N A Dudley Electrical Contractors v HMRC*** *[UKFTT] 260 (TC)* in which it is suggested that the everyday meaning of the words "reasonable excuse" should be used and not confined to exceptional circumstances.

46. The case of ***Kincaid v HMRC*** *[2011] UKFTT 225 (TC)* makes clear that each case must be considered on its own facts and reasonable excuse can be assessed from the perspective of a prudent business person exercising reasonable foresight and due diligence, with a proper regard for meeting tax liabilities. I bore in mind the guidance set down in the case of ***Kincaid v HMRC*** *[2011] UKFTT 225 (TC)*, which is not binding. I found that the facts of the case were wholly dissimilar to the case before me and did not provide any further assistance to the issues to be determined in this appeal.

47. There was no evidence before me that there had been any specific event which led to the Appellant's cash flow difficulties during the relevant period. To the contrary, the evidence was that the Appellant had been experiencing cash flow difficulties for some time prior to May 2010. Even applying the ordinary meaning to "reasonable excuse" I found as a fact that the absence of any reason for the Appellant's cash flow problems beyond those expected in the course of business in difficult economic circumstances, taken together with the fact that the problems had existed for some time yet not been resolved as would be expected of a diligent businessman seeking to comply with his obligations, cannot amount to a reasonable excuse.

48. I accepted that the Appellant is now meeting all liabilities in a timely manner, however I found as a fact that this could not amount to a reasonable excuse.

49. I noted that HMRC's telephone records showed that time to pay arrangements had been made on occasions and I considered Mr Quinn's evidence that this was not in respect of each of the months for which payments were made late as if the Appellant had sufficient funds the payments were made. I found as a fact the Appellant had not acted diligently in this regard. The evidence was clear that cash flow difficulties had been an issue for the Appellant since 2008; given the Appellant's knowledge that arrangements could be agreed with HMRC to allow additional time in order to meet its liabilities, I found as a fact that the absence of such arrangements for each of the periods in which late payments was indicative of the lack of care taken by the Appellant to comply with his tax obligations. I therefore found that this could not provide the Appellant with a reasonable excuse.

Mistake of fact

50. Mr Thompson sought to persuade the Tribunal that Mrs Cavanagh's lack of knowledge as to the penalty system and most advantageous process to use in allocating payments could amount to a mistake of fact. It was also submitted that the letter purported to have been sent to the Appellant by HMRC on 28 May 2010 did not explain the new penalty regime.

51. I considered the case of ***Anthony Leachman T/A Whiteley and Leachman v HMRC*** *[2011] UKFTT 261 (TC)* in which there had been what was deemed to be a "genuine mistake of fact...capable of amounting to a reasonable excuse" in that the taxpayer believed his accountant would file the P35 and the accountant believed that the taxpayer would attend to it. I found as a fact that the case was distinguishable on

the basis that it could not be said that any similar mistake of fact existed in the case before me. I found as a fact that Mrs Cavanagh's ignorance cannot be said to be a mistake of fact and the fact that standard commercial practice was followed in ignorance cannot amount to a reasonable excuse.

52. I accepted HMRC's evidence that a warning letter was issued to the Appellant on 28 May 2010. It may be that Mrs Cavanagh did not see the letter given that she was not employed on a full time basis; this does not mean that the letter was not sent and I found as a fact that this did not provide the Appellant with a reasonable excuse.

53. The fact that the penalty regime is not explained within the letter does not in my view amount to a reasonable excuse. The letter refers to potential penalties and a website link is given under the heading "More Information on Penalties." I accepted HMRC's evidence of telephone calls between Mrs Cavanagh and HMRC in which penalty warnings were given. Information is also widely available on HMRC's website, telephone help lines and bulletins. I found as a fact that advice and assistance had been available and provided to the Appellant. Case law has made clear that ignorance does not provide a taxpayer with a defence; the responsibility rested with the Appellant to ensure that it complied with the legislation and fulfilled its tax obligations. I found as a fact that the Appellant's lack of knowledge as to its obligations did not amount to a reasonable excuse.

Fair and Conscionable Behaviour

54. In ***Hok Limited v HMRC*** *[2011] UKFTT 433 (TC)* the Tribunal considered the issue of common law duty of fairness where the Appellant, having overlooked or forgotten to file the end of year returns, had not been notified of the imposition of penalties until the penalty notice was received. The Tribunal in that case took the view that HMRC had deliberately desisted from sending a penalty notice, which acts as a reminder.

55. As noted earlier, decisions of the First Tier (Tax) Tribunal are not binding and I did not accept that HMRC's conduct could be described as unfair on the facts of this particular case. A letter had been sent to the Appellant on 28 May 2010 warning of the potential for penalties. There had also been telephone calls between Mrs Cavanagh and HMRC which provided the opportunity for any assistance required to be sought.

56. I found as a fact that allocation was determined by the Appellant and it is the responsibility for the Appellant to ensure it is aware of its obligations. I did not accept that there is a duty on HMRC to interfere with the Appellant's processes by which tax where no advice had been sought in that regard. Information about the PAYE regime and penalties is readily available and I found as a fact that HMRC could not be deemed to have acted unfairly in this case.

57. I rejected the submission that the Appellant had been punished for assisting HMRC by allocating payments. The Appellant chose to allocate payments; ignorance cannot provide the Appellant with an excuse. I found as a fact that the Appellant had

not been diligent, on the basis that steps had not been regularly taken to ensure that its tax liabilities were met.

58. The legislation provides for circumstances in which penalties are imposed; I found as a fact that HMRC had not acted unfairly in applying the legislation where payments were consistently made late during the relevant period. I found as a fact that the submission that other taxpayers may not make payments at all does not mean there were insufficient grounds to impose penalties against the Appellant.

59. I was referred to paragraph 13 of ***Hok Limited v HMRC*** *[2011] UKFTT 433 (TC)* in which Mr Jones QC (Judge) stated that *"the penalty system has a legitimate aim, which is to ensure that appropriate filings take place in good time and to discourage default."* In this case the Appellant made late payments in every month during the relevant period. In applying the view expressed by Mr Jones QC, it cannot be said that the Appellant was punished unfairly; persistent late payments are the type of behaviour the legislation is designed to discourage and I found as a fact that HMRC had not acted in poor conscience or outside the purpose of the penalty system in imposing the penalties.

60. The penalties incurred might be considered harsh, but on the facts of this case I do not find that they were plainly unfair and therefore do not interfere with the penalties on grounds of proportionality or common law fairness.

61. The appeal is dismissed and penalties confirmed.

62. 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.

TRIBUNAL JUDGE
RELEASE DATE: 23 November 2011