



TC02541

Appeal number: TC/2012/06791

*INCOME TAX – late payment of PAYE – penalties under Schedule 56
Finance Act 2009 – taxpayer unaware of new penalty regime – financial
difficulties of taxpayer– whether reasonable excuse – appeal dismissed*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

JOHN MILLS LIMITED

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE NICHOLAS ALEKSANDER
GILL HUNTER**

Sitting in public at 45 Bedford Square, London on 30 January 2013

Isaac Obeng, Financial Controller of the Appellant for the Appellant

Paula O'Reilly, an officer of HMRC, for the Respondents

DECISION

Introduction

5 1. This is an appeal against penalties of £88,710.84 assessed under Schedule 56 Finance Act 2009 in respect of late payment of PAYE by the appellant in respect of the tax year 2010/11. The amount of penalties was later reduced to £78,134.63.

2. Mr Obeng, the Appellant's Financial Controller, represented the Appellant ("JML"), and Ms O'Reilly represented HMRC. In addition to the evidence of Mr
10 Obeng, we also had before us a bundle of documentary evidence.

The facts

3. We find the background facts to be as follows.

4. In the tax year 2010/11, JML was late in paying its PAYE in respect of each of the 11 periods ended 5 May 2010 to 5 March 2011. The total amount paid late was
15 £1,953,365.96. There was no dispute about the amounts of PAYE due each month or that the payments were late. Under paragraph 6 (7) Schedule 56 Finance Act 2009 a penalty of 4% of the late paid PAYE was assessed. The penalty assessed was £78,134.63.

5. Moreover, it was agreed that JML had also consistently made late payments of
20 PAYE since at least the tax years 2003/04 (HMRC were not able to retrieve JML's PAYE compliance records prior to that year). In the tax years 2003/04 to 2009/10, JML made only 11 out of 84 payments of PAYE by the due date. On 59 occasions, HMRC had to enforce payment of PAYE instalments by making determinations under regulation 78 of the PAYE Regulations. HMRC also made 7 distraint calls to enforce
25 payment. At the end of 2009/10, JML had £254,944 owing in PAYE, and this was only paid on 8 June 2010 following service of a statutory demand.

6. It was also common ground that in the tax year 2011/12 (i.e. after the penalties in dispute were levied) JML made payments of PAYE on time.

7. JML supplies retailers with various hardware products. Most of the goods are
30 sourced in the Far East, and are sold to retailers on "sale or return" basis. Cash flow is critical to the business, it has to pay a deposit to manufacturers before they even start manufacturing stock, and the balance is due even before the goods reach the UK. On reaching the UK, import duties and VAT are payable. Retailers pay JML on average 72 days from the end of the month in which the stock is delivered. The net result is
35 that it may be six months from the date JML pays the manufacturer until the date it is itself paid by the retailer.

8. In 2010/11 the UK economy was in recession, and there was a dramatic reduction in sales by JML. As it supplied retailers on a "sale or return" basis, stock was returned by retailers to JML. JML's cash resources were stretched, and it entered

into a sale/leaseback of its IT equipment to raise £1 million, and in addition it had a capital injection from shareholders and others. In 2009/10 Woolworths, JML's largest customer, ceased trading. Woolworths represented approximately one third of JML's turnover.

5 9. JML had been in contact with HMRC's Business Support Service in relation to payment of corporation tax, and had reached a time to pay agreement with HMRC for that tax. However Mr Obeng told us that he was not aware that businesses could seek time to pay arrangements with HMRC in respect of PAYE. No such arrangement had been sought.

10 10. Mr Obeng told us that although JML had been making late payments of PAYE prior to 2010/11, HMRC had not complained about this and had not levied penalties. Mr Obeng also told us that JML had an arrangement with HMRC for someone to come to JML's offices to collect a cheque for PAYE instalments.

15 11. Mr Obeng also told us that he was not aware of the introduction of the PAYE penalty regime for 2010/11, and that at no time during 2010/11 had HMRC warned JML of the risk of penalties. If JML had been fully aware of the penalty regime, they would have taken steps to ensure that payments were made by the due dates, as they had done for the current year.

20 12. HMRC's electronic records showed that a standard-form penalty default letter was issued to JML on 28 May 2010. Although HMRC do not keep copies of this letter on their files, a copy of the form of the letter which would have been sent was produced. In its first line the letter stated: "We have sent you this warning letter because it appears that you have not paid your PAYE on time. You may be liable to a penalty if you pay late more than once in a tax year...." The letter directed the recipient to HMRC's website for further information on penalties. Ms O'Reilly, for
25 HMRC, informed us that HMRC had checked its records and these indicated that there were no problems regarding the sending of electronically generated letters on that day. HMRC did not receive the letter back via Royal Mail returned letter service. Mr Obeng stated that JML had not received this letter.

30 13. At the hearing, HMRC produced details of their records of telephone calls and visits made by HMRC to the appellant. These records indicated that JML had been warned about the new PAYE penalty regime as early as a distraint call made on 11 January 2010, and on numerous subsequent calls. In addition Mr Obeng
35 acknowledged that JML had received HMRC's "Employers Bulletin" which explained the penalty regime, and which also made reference to the Business Support Service.

14. HMRC's payment records also show that it was not the case that HMRC visited JML each month to collect the PAYE cheque.

40 15. We consider that HMRC's records of its telephone conversations with and visits to JML were more likely to be correct than Mr Obeng's statement that he had never been warned about penalties. In particular, we find that it is more likely than not that

HMRC did warn JML about penalties. We also find that HMRC's records indicating that a penalty warning letter had been sent on 28 May 2010 were correct and we find that it is more likely than not that it was received by JML but either no attention was paid to it or it was simply overlooked.

5 16. Our impression of JML is that it has had difficulties with its liquidity since at least 2003, and has managed its cash-flow (at least in part) by delaying paying its PAYE. We also find that the insolvency of Woolworths in 2009/10 was not the cause of JML's failure to pay its PAYE instalments in 2010/11 on time. In reaching this finding we note that the fact of Woolworth's insolvency had not been mentioned by
10 JML until a late stage in the hearing, when we had discussed with Mr Obeng the implications of paragraph 16(2)(a) of Schedule 56 (see below) and the *Steptoe* case. More importantly, the pattern of JML's late payment had started well before Woolworth's insolvency, and was present even when the UK economy was performing well. Finally, JML is now making PAYE payments on time. All of these
15 factors, when considered together, support our finding that JML's late payments were not attributable to Woolworth's insolvency.

17. HMRC wrote to the appellant on 30 September 2011 notifying it that a penalty in respect of late payment of PAYE in respect of tax year 2010/11 had been incurred. The appellant requested that the penalty decision be reviewed and HMRC wrote to the
20 appellant on 30 May 2012 informing the appellant that the penalty decision should be upheld.

The statutory provisions

18. The new penalty code for late payments of tax was introduced by Schedule 56 to the Finance Act 2009. The relevant paragraph of the Schedule, applying to late
25 payments of PAYE, was paragraph 6, which came into force on 6 April 2010 (SI 2010/466 art 3). Although newly enacted, paragraph 6 was amended with effect from 25 January 2010 (SI2011/132 art 2(b)) by paragraphs 1 and 6 of Schedule 11 Finance (No2) Act 2010. However, the difference in wording of the two versions of paragraph
30 6 has no material impact on the outcome of this appeal, and we therefore set out only the amended version of the legislation.

24. The amended paragraph 6 reads as follows:

- (1) P [the taxpayer] is liable to a penalty, in relation to each tax, of an amount determined by reference to—
 - (a) the number of defaults that P has made during the tax year (see
35 sub-paragraphs (2) and (3)), and
 - (b) the amount of that tax comprised in the total of those defaults (see sub-paragraphs (4) to (7)).
- (2) For the purposes of this paragraph, P makes a default when P fails to
40 make one of the following payments (or to pay an amount comprising two or more of those payments) in full on or before the date on which it becomes due and payable—

- (a) a payment under PAYE regulations;
- (b) a payment of earnings-related contributions within the meaning of the Social Security (Contributions) Regulations 2001 (SI 2001/1004);
- 5 (c) a payment due under the Income Tax (Construction Industry Scheme) Regulations 2005 (SI 2005/2045);
- (d) a repayment in respect of a student loan due under the Education (Student Loans) (Repayments) Regulations 2009 (SI 2009/470) or the Education (Student Loans) (Repayments) Regulations (Northern Ireland) 2000 (SR 2000 No 121).
- 10 (3) But the first failure during a tax year to make one of those payments (or to pay an amount comprising two or more of those payments) does not count as a default for that tax year.
- (4) If P makes 1, 2 or 3 defaults during the tax year, the amount of the penalty is 1% of the amount of the tax comprised in the total of those defaults.
- 15 (5) If P makes 4, 5 or 6 defaults during the tax year, the amount of the penalty is 2% of the amount of the tax comprised in the total of those defaults.
- (6) If P makes 7, 8 or 9 defaults during the tax year, the amount of the penalty is 3% of the amount of the tax comprised in the total of those defaults.
- 20 (7) If P makes 10 or more defaults during the tax year, the amount of the penalty is 4% of the amount of the tax comprised in the total of those defaults.
- 25 (8) For the purposes of this paragraph—
- (a) the amount of a tax comprised in a default is the amount of that tax comprised in the payment which P fails to make;
- (b) a default counts for the purposes of sub-paragraphs (4) to (7) even if it is remedied before the end of the tax year.
- 30 (9) The Treasury may by order made by statutory instrument make such amendments to sub-paragraph (2) as they think fit in consequence of any amendment, revocation or re-enactment of the regulations mentioned in that sub-paragraph.
- 35 19. It can be seen from paragraph 6(7) that ten defaults in the tax year renders a taxpayer such as JML liable to a penalty of 4% of the total amount of tax comprised in those defaults.
20. Schedule 56 also contains provisions (paragraph 16) removing liability for a penalty where there is a "reasonable excuse" for the failure. As was the case with paragraph 6, paragraph 16 was amended as regards PAYE payments with effect from 40 25 January 2011 (SI 2011/132 art 3). The amendments are not material to this appeal. The amended paragraph 16 reads as follows:

(1) If P satisfies HMRC or (on appeal) the First-tier Tribunal or Upper Tribunal that there is a reasonable excuse for a failure to make a payment—

5 (a) liability to a penalty under any paragraph of this Schedule does not arise in relation to that failure, and

(b) the failure does not count as a default for the purposes of paragraphs 6, 8B, 8C, 8G and 8H.]

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

10 (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

15 (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."

Discussion

20 21. We have considered the arguments put forward by Mr Obeng above but consider that none of the points raised constitute a "reasonable excuse" for the purposes of paragraph 16.

25 22. In particular, the financial difficulties in which JML found itself cannot amount to a reasonable excuse unless attributable to events outside JML's control. We have no doubt that in the general economic downturn trading conditions for JML have become more difficult. These are, however, the consequences of normal trading, albeit in adverse economic conditions. As Lord Donaldson MR said in *Customs and Excise Commissioners v Steptoe* [1992] STC 757 at 770:

30 ...if the exercise of reasonable foresight and of due diligence and a proper regard for the fact that the tax would become due on a particular date would not have avoided the insufficiency of funds which led to the default, then the taxpayer may well have a reasonable excuse for non-payment, but that excuse will be exhausted by the date on which such foresight, diligence and regard would have overcome the insufficiency of funds.

35 23. In this case, JML did not exercise reasonable foresight nor did it display a proper regard for the date on which its PAYE was due and payable. Indeed, Mr Obeng stated that if he had known that penalties were to be imposed JML would have made arrangements to ensure that they paid the tax on the due date.

40 24. Although Woolworth's insolvency was outside JML's control, our finding is that JML's late payments were not attributable to this insolvency.

25. Moreover, we do not consider that this is a case in which HMRC have acted unfairly. As we have found, we considered it more likely than not that the appellant did receive HMRC's warning letter 28 May 2010. In addition HMRC warned JML of the penalty regime in a number of telephone calls. This is in addition to the thorough explanation of the penalty regime given in the Employers Bulletins sent to every employer by HMRC and which Mr Obeng confirmed had been received by JML.

26. Finally, we note that JML had not agreed any time to pay arrangement with HMRC.

27. For these reasons, we do not consider that the appellant had a reasonable excuse for its failure to make its PAYE payments on time.

28. We therefore dismiss this appeal.

29. 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.

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**NICHOLAS ALEKSANDER
TRIBUNAL JUDGE**

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RELEASE DATE: 12 February 2013