



**TC03415**

**Appeal number: TC/2013/06021**

*VAT surcharge – reasonable excuse – insufficiency of funds – appeal dismissed*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**M.A.T. ELECTRICS LIMITED**

**Appellant**

**- and -**

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

**TRIBUNAL: JUDGE JENNIFER TRIGGER**

The Tribunal determined the appeal on 25 November 2013 without a hearing under the provisions of Rule 26 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (default paper cases) having first read the Notice of Appeal dated 21.08.2013; letter dated 21.08.2013; letter dated 23.07.2013; letters dated 24 and 28.05.2013; letter dated 28.06.2013; Value Added Tax Notice of Assessment of Surcharge and Surcharge Liability Notice Extension dated 15.02.2013 and marked 22.02.2013 and VAT Notice of Assessment and Surcharge and Surcharge Liability Notice Extension dated 17.05.2013; NatWest Statement of Account No. 25158031 from 9.05.2013 – 15.05.2013 and the Respondents' Statement of Case submitted on 1.10.2013 together with the documents and correspondence numbered 1–43 inclusive contained in the Respondents' bundle.

## DECISION

### Introduction

1. This is an appeal by M.A.T. Electrics Limited against a penalty levied under the VAT default surcharge regime. The penalty falls into the 5% rate and was computed by HMRC at £1,736.14 for the period 03/13.

### Legislation

2. The default surcharge regime is found in section 59 of the Value Added Tax Act 1994 (“VATA”). This prescribes:

“59. *The default surcharge*

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

*(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.*

*[(1A) a person shall not be regarded for the purposes of this section as being in default in respect of any prescribed accounting period if that period is one in respect of which he is required by virtue of any order under section 28 to make any payment on account of VAT.]*

*(2) Subject to subsections (9) and (10) below, subsection (4) below applies in any case where -*

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

*(b) the Commissioner serve notice on the taxable person (a “surcharge liability notice”) specifying as a surcharge period for the purposes of this section a period ending on the first anniversary of the last day of the period referred to in paragraph (1) above and beginning subject to subsection (3) below on the date of the notice.*

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

*(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.*

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

*(a) in relation to the first such prescribed accounting period, the specified percentage is two percent;*

*(b) in relation to the second such period, the specified percentage is five percent;*

*(c) in relation to the third such period, the specified percentage is ten percent; and*

*(d) in relation to each such period after the third, the specified percentage is fifteen percent.*

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

*(7) If a person who, apart from this subsection, would be liable to a surcharge under subsection (4) above satisfies the Commissioners or, on appeal, a tribunal that, in the case of the default which is material to the surcharge -*

*(a) the return or, or as the case may be, the VAT shown on the return was despatched at such a time and in such a manner that it was reasonable to expect that it would be received by the Commissioners within the appropriate time limit, or*

*(b) there is a reasonable excuse for the return or VAT not having been so despatched,*

*he shall not be liable to the surcharge and for the purposes of the preceding provisions of this section he shall be treated as not having been in default in respect of the prescribed accounting period in question (and, accordingly, any surcharge liability notice the service of which depended upon that default shall be deemed not to have been served). ...”*

The Value Added Tax Regulations 1995 provides so far as is relevant:

VAT to be accounted for on returns and payment of VAT

“40 *Save as the Commissioners may otherwise allow or direct –*

*(a) any person making a return shall account therein for all his output tax and all VAT for which he is accountable by virtue of Part XVI of these Regulations in respect of the period to which the return relates, and the amounts to be entered on that return shall be determined in accordance with these Regulations; and*

*(b) any person required to make a return shall pay to the Controller such amount of VAT as is payable by him in respect of the period to which the return relates no later than the last date on which he is required to make that return.”*

Section 71 of VATA provides so far as is relevant:

“71 (1) *For the purposes of any provisions of section 59 to section 70 which refers to a reasonable excuse for any conduct –*

*(a) an insufficiency of funds to pay any VAT due is not a reasonable excuse; and*

*(b) where reliance is placed on any other person to perform any task, neither the fact of that reliance nor any dilatoriness or inaccuracy on the part of that person relied upon is a reasonable excuse.*

71 (2) *In relation to a prescribed accounting period, any reference to sections 59 to 69 to credit for input tax includes a reference to any sum which in a return for that period is claimed as a deduction from VAT due.”*

The Finance Act 2009 provides so far as is relevant:

108. Suspension of penalties during currency of agreement for deferred payment.

(1) *This section applies if –*

*(a) a person (“P”) fails to pay an amount of tax falling within the Table in subsection (5) when it becomes due and payable,*

*(b) P makes a request to an officer of Revenue and Customs that payment of the amount of tax be deferred; and*

*(c) an officer of Revenue and Customs agrees that payment of that amount may be deferred for a period (“the deferral period”).*

(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 payment.*

(3) *But if –*

*(a) P breaks the agreement (see subsection (4)); and*

*(b) an officer of the Revenue and Customs serves on P a notice specifying any penalty to which P would become liable apart from subsection (2),*

*P becomes liable, at the date of the notice, to the penalty.*

*(4) P breaks an agreement if –*

*(a) P fails to pay the amount of tax in question when the deferral period ends, or*

*(b) the deferral is subject to P complying with a condition (including a condition that part of the amount be paid during the deferral period) and P fails to comply with it.*

*(5) The taxes and penalties referred to in subsections (1) and (2) are –*

*TAX*

*Value added tax*

*PENALTY*

*Value Added Tax surcharge under section 59(4) or 59A(4) of VATA 1994*

*...”*

## **Background**

3. From a schedule provided by HMRC, which was accepted by the Appellant, it was in default as follows: the 09/12 return payment was £36,800.94 and was due to be paid on 31 October 2012 or 7 November 2012 (the latter allowing for the 7 additional calendar days afforded to those paying electronically).

4. The payment was made in three tranches by Faster Payments on 13 November 2012, 7 December 2012 and 19 December 2012. A further default occurred in the period 12/12 when payment due on 7 February 2013 was received by Faster Payments on 18 February 2013. The default which is the subject of this appeal occurred during the 03/13 period, when payment due by 7 May 2013 was received by HMRC on 15 May 2013 by Faster Payments. It was accepted by the Appellant that the payment was late.

5. The Appellant requested a review on the surcharge relating to the 03/13 period by letter dated 24 May 2013. The letter stated that there had been a delay in payment due to “... *having problems with my HMRC PAYE account for the last couple of months with payments coming back and being misallocated on our account, as well as not being able to gain access to any of my end of year forms. I thought everything had been sorted out but it looks as though there is a universal problem with our accounts. ... Apart from a late payment last quarter which was caused by one of my customers going into liquidation, I have a good payment track record and make it a priority to ensure this is always the case with regards to HMRC.*”

6. By letter dated 23 July 2013 from HMRC to the Appellant, HMRC upheld the surcharge imposed for the 03/13 period following a review and informed the Appellant that:

“Our record show that your VAT return for the period 03/13 was submitted on 30/04/13 and the Direct Debit for £34,722.81 failed. An electronic payment for £34,722.81 was received by HMRC on 16/05/13. As you have stated that you have problems with the Direct Debit payment, I have checked with the bank who confirmed there was no issue at their end. I contacted the Direct Debit team who said the Direct Debit failure can suggest an insufficiency of funds or that your bank was advised to cancel the Direct Debit by you. You were then contacted by HMRC who requested bank statements from you to ensure it wasn't an insufficiency of funds for the periods 09/12, 12/12 and 03/13. You responded by e-mail stating that the bank statements are with your accountants and so unavailable. The surcharge for the period 03/13 will therefore remain in force...”

7. In respect of the surcharge liability notice for the period 12/12 the Appellant spoke to HMRC on 18 February 2013. On that occasion the Appellant indicated that late payment was due to Direct Debit failure and the Appellant was advised on the possibility to account for tax via a range of alternative schemes available.

8. Furthermore, when the Appellant entered the default surcharge regime for the period 09/12 and a surcharge liability notice was served on the Appellant on 16/11/2012, the surcharge liability notice detailed the potential financial consequences attached to the risk of a further default. In particular a surcharge liability notice contains the standard paragraph as follows:

“Please remember –

Your VAT returns and any tax due must reach HMRC by the due date. If you expect to have any difficulties contact either your local VAT office, listed under HM Revenue & Customs in the phone book as soon as possible, or the National Advice Services on 0845 010 9000”.

The reverse of each notice details how surcharges are calculated and the percentages used in determining any financial surcharge, in accordance with section 59(5) of VATA.

9. As HMRC upheld the surcharge for the period 03/13 on the basis that no reasonable excuse existed, the Appellant appealed the decision.

### **Appeal**

10. By Notice of Appeal dated 21 August 2013 the Appellant appealed to the Tribunal Service. The ground relied upon can be summarised as follows:

- (a) The Appellant had been under increasing financial pressure since the summer of 2012, when funds receivable on a large contract began to fall in arrears. By 31 March 2013 debts of almost £135,000 had accumulated across two main contracts together with six other smaller ones. The six smaller contracts had been confirmed as irredeemable.
- (b) The Appellant's bank, NatWest, had refused to permit an extension of the Appellant's overdraft facility. In particular on 10 May 2013 an extension had been refused despite the fact that cleared funds would have been banked on 13 May 2013 to remedy the breach in the overdraft limit.

- (c) The Appellant's Finance Director, Mrs Guest, became pregnant in October 2012. She was absent from work due to difficulties with the pregnancy particularly from March 2013 onwards. Mrs Guest commenced maternity leave on 31 May 2013. A member of staff was employed as a replacement on 8 April 2013. She resigned on 14 June 2013 and a second replacement member of staff left after less than a week in post. It was not until July 2013 that a permanent replacement member of staff was found for Mrs Guest. Nevertheless, despite these difficulties, Mrs Guest made herself available to assist the Appellant.
- (d) The Appellant invested in a new software system in the spring of 2013. The transition to the system was problematic. Some of the problems were due to key staff issues.

### **Respondents' case**

11. By Statement of Case submitted on 1 October 2013 HMRC responded to the Appellant's appeal. The basis of that response can be summarised as follows:

- (a) The electronic due date for the period 03/13 was 7 May 2013. The return was received on time, electronically on 30 April 2013.
- (b) The surcharges had been correctly issued in accordance with section 59(4) of VATA payment having been received by HMRC after the due date.
- (c) The first default was recorded for the period 09/12 and the Appellant entered the default surcharge regime. The potential financial consequences attached to the risk of a further default were made known to the Appellant from that point onwards given the information printed on the Surcharge Liability Notice issued.
- (d) By virtue of Regulation 40 of the Value Added Tax Regulations 1995 there is a statutory obligation on a person required to make a return to pay the VAT to HMRC.
- (e) The Appellant had a valid Direct Debit Mandate in place but the Direct Debit payments for the periods 09/12 and 12/12 had both failed. Payment in both instances subsequently being received via the BACS Faster Payment method as was also the case for the period 03/13.
- (f) On 18 February 2013 the Appellant had spoken to HMRC about making payment for the period 12/12. On that occasion the Appellant had been advised of the possibilities to account for tax via a range of alternative schemes available because the Appellant had indicated that there were recurrent Direct Debit payments.
- (g) On 30 April 2013 when submitting the return for the period 03/13 the Appellant would have received an automated on screen acknowledgement which stated:

*"The tax due as declared on this return [Value of tax due] will be debited from your bank account on [collection dates]. If you have submitted this VAT return on behalf of the VAT registered entity, you must print this acknowledgement and present to the account holder/authorised signatory of the account prior to the stated Direct Debit collection date."*

- (h) Despite issues with the Appellant's new software system in spring 2013 the return for the period 03/13 was received on time. Accordingly HMRC deemed that on or before 30 April 2013 the amount of tax due had been successfully calculated.
- (i) The Direct Debit payment for the period 03/13 failed when called for and the Appellant confirmed that there were insufficient funds available to pay the tax when due.
- (j) VATA section 71(1) precludes insufficiency of funds of itself from providing reasonable excuse for defaults.
- (k) As a result of cash flow issues from the summer of 2012 onwards the Appellant had a combined debit of £135,000 by 31 March 2013.
- (l) The Appellant's VAT returns indicated that in the year 31 March 2013 the outputs (net of tax) were £2,252,840. The debit was less than 0.06% of that amount.
- (m) As tax due for the period 03/13 was £34,722.81 which was less than 7.5% of the declared outputs of net tax of £494,244. The Appellant did not contend that insufficient funds were actually received in the period 03/13 to pay the VAT tax when due.
- (n) The Finance Director's maternity leave commenced after the due date for the period 03/13. Furthermore the maternity leave commenced after full payment had been received for that period. Arrangements had been made to cover the Financial Director's absence and additional staff were employed before the Finance Director took her maternity leave. The Appellant had made a timely submission of the return for the period 03/13 and acknowledged there was an sufficiency of funds. The potential consequences of a further default had been made clear to the Appellant. It was not clear why the other directors of the Appellant could not have contacted HMRC prior to the due date to discuss possible payment arrangements. The Finance Act 2009 section 108 contains provision that there is no liability to a default surcharge for a period when contact is made with HMRC prior to the due date in order to arrange a payment deferment and this is agreed by HMRC.
- (o) The Appellant has not contended that they contacted HMRC on or before the due date for the period 03/13 to initiate payment processes or to seek advice.
- (p) The Appellant requested a "little leeway and understanding". HMRC has no authority to mitigate the quantum as the rates of surcharge are specified in section 59 of VATA.

## **Decision**

### **Reasonable Excuse**

12. I will deal first with the issue of reasonable excuse.

13. Section 59A(8) of VATA provides that a taxable person will not be liable to a surcharge if he satisfies the Commissioners or, on appeal, this Tribunal that he has a reasonable excuse for the default. The legislation specifically excludes insufficiency of funds and an error made by another relied upon.

14. I found as a fact that when the Appellant entered the default surcharge regime for the period 09/12 and the Surcharge Liability Notice was served on the Appellant on 16 November 2012 the Appellant was informed of the potential financial consequences attached to the risk of a further default. Furthermore, the Appellant was made aware that it could contact the local VAT office or the National Advice Service if it expected to have difficulties with submitting VAT returns or any tax due by the due date. Each notice set out clearly how the surcharges were calculated and the percentages used in determining the financial surcharge.

15. The Appellant's Direct Debit Mandate had failed for the 09/12 and 12/12 periods. This occurred for the period 03/13 also.

16. The Appellant was advised by HMRC on 18 February 2013 of alternative ways to account for the VAT during a telephone conversation concerning payment in respect of the period 12/12.

17. On 30 April 2013 when the Appellant submitted the VAT return for 03/13 the Appellant would have received an automated onscreen acknowledgement informing the Appellant that the tax due would be debited from the Appellant's bank account on a specified date. At that time the Appellant would have known the amount of tax due.

18. There was no evidence before me that the Appellant had sought any further clarification as to the various methods of paying electronically and the length of time that such payments required. Furthermore there was no evidence that the Appellant's Finance Director or the other directors of the Appellant had contacted HMRC prior to the due date to inform HMRC that the Appellant would be unable to make the payment by the due date or in the alternative that there was concern about the Appellant's cash flow.

19. I did not accept that the Appellant's cash flow problems amounted to a reasonable excuse. The Appellant had been in the default surcharge regime since 09/12. It was aware of the consequences of failing to make payment by the due date but did not avail itself of any of the avenues available to prevent a further default surcharge being levied.

20. I did not consider that the difficulties experienced by the Appellant regarding cover for the Finance Director's maternity leave amounted to a reasonable excuse. Mrs Guest did not commence her maternity leave until 31 May 2013 and she had a replacement in post on 8 April 2013 to assist her. There were personnel available to attend to the filing of the return and the payment of the VAT by the due date. As the return for 03/13 was filed before the due date and the tax due was known to the Appellant, the Appellant had adequate time to discuss with HMRC possible payment arrangements prior to that due date. The Appellant failed to take this action.

21. I did not accept that the difficulties experienced by the Appellant after installation of a new software system in the spring of 2013 amounted to a reasonable excuse. The Appellant had been able to file the return on time despite these problems and the tax due was known by the Appellant despite the claimed inadequacy of the software system.

22. The Appellant did not plead that insufficient funds were actually received in the period 03/13 to pay the tax due. The combined debt of £135,000 was less than 0.06%

of the outputs (net of tax) recorded in the Appellant's VAT returns for the year ended 31 March 2013 in the sum of £2,252,848. Furthermore in the specific period of 3/13 the tax due of £34,722.81 was less than 7.5% of the declared outputs of net tax of £494,244. The Appellant pleaded that any breach of the overdraft limit imposed by NatWest in honouring the VAT Direct Debit on 10 May 2013 would have been minimal and this would have been cleared by funds banked on 13 May 2013. The Appellant questions the grounds of which its bank refused to honour the VAT payment in May 2013 and considers that the bank "*has at best been less than understanding in this regard.*" The difficulty identified did not in my opinion amount to a reasonable excuse. The Appellant was aware that Direct Debits had been dishonoured because of insufficiency of funds. The Appellant had a responsibility to make alternative arrangements and to discuss the matter with HMRC. I found as a fact that the Appellant had not taken the care to be expected of a diligent and prudent taxpayer seeking to comply with its obligations.

23. The legislation is designed to penalise lateness, irrespective of length, and is to be strictly applied. I therefore reject the grounds of appeal.

24. My findings were as follows:

- (a) There was no reasonable excuse for the late payment of VAT in the 03/13 period.
- (b) The default surcharge had been properly levied in relation to the late payment.

25. I therefore dismiss the appeal and confirm the surcharge.

26. 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.

**JUDGE JENNIFER TRIGGER  
TRIBUNAL JUDGE**

**RELEASE DATE: 19 March 2014**