



TC04039

Appeal number: TC/2014/03154

Penalty for late payment of PAYE – 2012/13 – cash flow difficulties – sudden withdrawal by major client – change of banking requirements - reasonable excuse - yes – appeal allowed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

PSC PHOTOGRAPHY LIMITED

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE Judith Powell
MEMBER Mr Michael Sharp FCA**

Sitting in public at Bedford Square, London on 2 September 2014

**Mr Steve Smith, Director, for the Appellant
Ms Hellie Lai, presenting officer with HMRC, for the Respondents**

DECISION

The Appeal

5 1. This is an appeal against a penalty determination issued by HMRC under
Schedule 56 Finance Act 2009 to the Appellant for its failure to make monthly
payments of PAYE on time in 2012/2013. Each of the monthly payments was made
late but the total due for the year has now been paid in full. Each of the payments
was made fairly soon after the due dates. The Appellant agrees that the penalty has
10 been calculated correctly if it is payable. It will be payable unless the Appellant can
show it has a reasonable excuse.

2. The Appellant said in its Notice of Appeal that it had done its best to get
through the downturn and had no idea that a late penalty would apply.

The facts

15 3. The director of the Appellant company gave oral evidence and elaborated on the
background to its failure to pay on time. We found the following facts.

4. The Appellant's original business involved taking still life photography for
magazines but changed over the years to concentrate on e photographic work for
major high street retailers. For the calendar year 2011 the company's turnover was
20 £475,228 and the profit was £7414 and in the following calendar year of 2012 the
turnover was £457,058 and it sustained a loss of £28,000. Sums due to the company
at the end of 2011 amounted to £72,915 and at the end of 2012 to £57,499. The
Appellant employed a small team of 9 or 10 people in the relevant period.

5. In November 2011 the Appellant started work on what it expected to be a
25 lucrative contract for a high street retailer client, TR Lewin. This was to involve
helping the client produce a style guide and the client had its own in house team
working on the same project. Some initial work was done by the Appellant company
from November onwards which was invoiced and the Appellant was paid. The main
work was due to start in February 2012 and employees of the Appellant company
30 were available to do this but just before the expected start date the client said it
wished to postpone the start date to May 2012 for its own cash flow reasons. TR
Lewin had the copyright to the work which had been done and there was no penalty
clause in the contract that provided for compensation for the Appellant if the project
was terminated before completion. This was in line with how the Appellant had
35 always done business. Eventually the client decided to finish the project without
further input from the Appellant. This was a major setback for the Appellant who had
retained staff to work on the project and they were not fully utilised during this period
but were still being paid whilst the Appellant continued to hope the project would be
started again after the initial delay. Fortunately, some six months later, the Appellant
40 won a lucrative contract but the loss of the TR Lewin contract had an adverse short
term effect on cash flow.

6. Possibly exacerbated by the financial consequences caused by the delay and subsequent termination of the TR Lewin contract, but also as a result of the general economic conditions the Appellant's bank (RBS/NatWest) abruptly changed its banking arrangements in November 2012 and asked the Appellant to reduce its overdraft from £125,000 down to £90,000 and make monthly repayments of £10,000. The Appellant was unable to do this and so the Bank cancelled the overdraft facility of £125,000, increased the existing business mortgage by the amount of the overdraft and imposed a monthly repayment requirement of £5,550. This imposed a financial strain on the Appellant which it had not expected. The Appellant had to take emergency steps to remedy its situation which it has now done by selling its building. This allowed it to repay its bank debt and it now trades well without outside finance.

7. Prior to the two events recorded above the Appellant had suffered a downturn in its business for several years due to the prevailing economic conditions. The nature of its business is such that in a general downturn clients which are themselves suffering financial setbacks will economise by not using, or by limiting their use of, the Appellant's services and during this period a couple of clients went out of business.

8. In the previous year the Appellant had agreed a time to pay arrangement with HMRC. The Appellant concluded from conversations its director had with HMRC that it would not be able to arrange a further time to pay arrangement for 2012/2013 and referred to a note of a telephone conversation the Respondents produced to us which was dated 4 November 2011. This note recorded that the time to pay arrangement then agreed would "be the final concession for this company".

9. We accept that HMRC made contact with the Appellant several times during the year in question after payment dates for PAYE had been missed. On a number of those occasions (for Months 4, 7, 9, 10 and 12) the Appellant referred to cash flow difficulties. In November 2012 reference was also made to the loan restructuring. HMRC did not make contact with the Appellant in relation to Months 3, 5, and 8.

10. We concluded that the Appellant was aware that it would incur penalties for the late payments. There was sufficient evidence of this in the telephone conversation records. However we also accept that the Appellant was unaware of how the penalties were calculated. This meant that it was surprised by the amount of the penalty. We accept that the payments made by the Appellant were correctly allocated by HMRC; the Appellant suggested that if it had been aware of the way in which the penalties were calculated it would have allocated payments differently and this might have resulted in the penalty being less. We can see that this might have been the case but there is no evidence that the allocation was done incorrectly by HMRC in the absence of other instructions from the Appellant.

Submissions

11. The Respondents said that the Appellant did not have a reasonable excuse for its failure to pay on time and that general cash flow problems could not be a reasonable excuse. They say that the Appellant may have mentioned cash flow difficulties but did

not request time to pay prior to the due date and they also said that the records of the phone conversations that HMRC had with the Appellant show that the company must have been aware of its exposure to penalties. They said that the penalty cannot be reduced because the tax was paid fairly soon after the due date; this is not how the penalty system operates. it is intended as a deterrent against late payment rather than as compensation for the delay in receiving funds.

12. The Appellant said it had done its best in difficult times and that the loss of the work from TR Lewin and the withdrawal of the overdraft in the relevant year made things particularly difficult. It felt that the penalty was inappropriate given the fairly short interval between the due date for payment and actual payment.

Our decision

13. We are only in a position to decide whether the Appellant did or did not have a reasonable excuse for the late payment of the PAYE in all or in some of the months in question during 2012/2013. We cannot mitigate the amount of the penalty if we decide that the Appellant does not have a reasonable excuse. We accept that the Appellant had financial difficulties during the year in question. The records of the amounts due to it at the end of 2011 and 2012 are consistent with it having made efforts to collect fees due to it and we were impressed with the clear account of Mr Smith about the nature of its difficulties with the TR Lewin contract and with the Bank. It is perhaps a pity that he had not made the situation sufficiently clear to HMRC before the hearing.

14. We have already said we are satisfied that the Appellant understood that it was late making payment and it would be liable for a penalty. We acknowledge it did not know how the penalty was calculated. This is something it could have established fairly easily and it might possibly have been able to organise the way in which it allocated the payments it made as and when it had the funds to do so and might have incurred a lower penalty as a result. It did not do so. We are satisfied it made payments as soon as it was able to do so. We are also satisfied that its cash flow difficulties prevented it from making payments on time. We would not have found that unspecified cash flow difficulties would be a reasonable excuse but in this case the cash flow problems stemmed from two particular underlying problems stemming from the TR Lewin contract and the Bank's change of attitude about borrowing arrangements. It is evident that these two factors severely affected a business that was already weakened by the economic downturn. They were the direct cause of the problems it encountered in 2012/2013 and they followed on from each other and caused cash flow problems throughout that year. We found the evidence of the director that the cancellation of the TR Lewin contract was unexpected and was a significant loss to the business and whilst there is always a risk that a contract will not be concluded we found it was not unreasonable in all the circumstances for the Appellant to expect the customer to finalise things after the initial delay. We also found that the bank's change of attitude was wholly unexpected and it was not unreasonable for the Appellant to have been taken by surprise by their attitude. We conclude that the Appellant had a reasonable excuse for its failure to pay the PAYE on time in that year and we allow its appeal. We believe that the action it took in

5 selling its building, finding the new contract to replace the TR Lewin contract and repaying its bank borrowings as well as making sure that new contracts contained additional protection against unexpected cancellation could not have prevented the failure to pay on time in 2012/2013 so that the excuse continued during the period to which the appeal related.

10 15. 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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**JUDITH POWELL
TRIBUNAL JUDGE**

RELEASE DATE: 30 SEPTEMBER 2014

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