



TC04050

Appeal number: TC/2013/06493

*VAT default surcharge - insufficiency of funds - whether reasonable excuse
- no - whether penalty excessive - no - appeal dismissed*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

C K DIRECT PETERBOROUGH LTD

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE MICHAEL S CONNELL
MRS BEVERLEY TANNER**

**Sitting in public at SSCS Byron House 2a Maid Marion Way Nottingham on 2 July
2014**

The Appellant did not attend and was not represented

Mr Tom Eyre, Officer of HM Revenue and Customs, for the Respondents

DECISION

The Appeal

5 1. C K Direct (Peterborough) Ltd ('the Appellant') appeals against a default surcharge of £13,179.28 imposed by HMRC on 17 May 2013, in respect of the VAT period ended 31 March 2013, for its failure to submit, by the due date, payment of VAT due. The surcharge was calculated at 15% of the VAT due of £87,861.87.

2. The point at issue is whether or not the Appellant has a reasonable excuse for making late payments.

10 3. The Appellant did not attend the hearing and was not represented. The appeal was listed to be heard at 2.00pm. The Tribunal allowed a further 45 minutes for someone from the Appellant Company to attend. The Tribunal was satisfied that the Appellant had been notified of the date, time and venue of the hearing and that it was in the interests of justice to proceed.

15 Background

4. The Appellant has been in the VAT default surcharge regime from period 04/11. Prior to the default under appeal there had been seven previous defaults.

20 5. The Appellant was on a quarterly basis for VAT. Section 59 of the VAT Act 1994 requires VAT returns and payment of VAT to be made on or before the end of the month following each calendar quarter. [Reg. 25(1) and Reg 40(1) VAT Regulations 1995.]

25 6. HMRC have discretion to allow extra time for both filing and payment when these are carried out by electronic means. [VAT Regulations 1995 SI 1995/2518 regs. 25A (20), 40(2)]. Under that discretion, HMRC allow a further seven days for electronic filing and payment.

30 7. In respect of the default period under appeal, as payment was made electronically, the due date for the 03/13 period was 7 May 2013. The return was received on 7 May 2013 and the VAT payment in seven instalments between 13 May 2013 and 10 July 2013.

8. A taxable person who is otherwise liable to a default surcharge may nevertheless escape that liability if he can establish that he has a reasonable excuse for the late payment which gave rise to the default surcharge. Section 59 (7) VATA 1994 sets out the relevant provisions : -

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

40 (a) the return 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

5 (b) there is a reasonable excuse for the return or VAT not having been so despatched then 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.

9. Section 59(7) must be applied subject to the limitation contained in s 71(1) VATA 1994 which provides as follows : -

10 ‘(1) For the purposes of any provision of section 59 which refers to a reasonable excuse for any conduct -

(a) any insufficiency of funds to pay any VAT due is not a reasonable excuse.’

15 Although an insufficiency of funds to pay any VAT due is not a reasonable excuse, case law has established the principle that the underlying cause of any insufficiency of funds may constitute a reasonable excuse

10. The onus of proof rests with HMRC to show that the surcharge was correctly imposed. If so established, the onus then rests with the Appellant to demonstrate that there was reasonable excuse for late payment of the tax. The standard of proof is the ordinary civil standard of the balance of probabilities.

Appellant’s contentions

11. The Appellant does not dispute that its VAT payment for the periods 03/13, was late.

12. The Appellant’s grounds of appeal are that it had cash flow problems. In its Notice of Appeal to the Tribunal, Mr Tony Ricciardi the Managing Director of the Appellant said:

30 “Prior to submitting the return we did realise that cash flow would not allow us to pay in full and we therefore spoke to your helpline for advice. We offered to pay £15,000.00 per week until the liability was cleared but was told that it would not be possible to make weekly payments but that if we paid that amount each week, then the likelihood of legal action was highly unlikely. We, however, did not expect to have a 15% £13,179.28 penalty added onto the £87,861.87 liability.

35 We have suffered in excess of £35,000.00 worth of bad debts for the year 2012-2013, with a few more expected over the next month or so. On top of this loss we have major, valuable blue chip companies which had advised us that their payment terms had changed from 30 days (as if) to 60 days +!! Whereas we are targeting more non-account customers to aid the cash flow, we need the blue chip companies to keep the direct employees at the current level.

40 Until such time as there is legislation to ensure that major companies pay on time, smaller/medium size companies will continue to struggle with cash

flow and we need all the assistance we can in this economic climate to continue to trade and ensure profitability.

When I rang VAT Payments helpline on 7th May, and asked about the request above. I was told that someone would ring back with a decision. We received a call on 8th May refusing the instalments over weeks with the excuse that we had time to pay in instalments in the previous VAT Period.

We do not consider this a viable reason for refusal, so not only were we denied this we were then issued with the maximum penalty of an additional £13,179.28”.

HMRC's contentions

13. Period 03/13 had a due date of 7 May 2013 for electronic payments and returns. The VAT Return was received electronically by HMRC on 7 May 2013. The Appellant paid their VAT due of £87,861.87 by six Faster Payment Service (FPS) transactions and one BACS payment. The first payment of £12,000.00 was received on 13 May 2013. The final payment by BACS was received on 10 July 2013. As all payments were received by HMRC after the due date the Surcharge Liability Notice Extension was correctly issued.

14. The first default was recorded for period 04/11 and the Appellant entered the Default Surcharge regime. The potential financial consequences attached to the risk of further default would have been known to the Appellant from this point onward, given the information printed on the Surcharge Liability Notice issued.

15. Included within the notes on the reverse of the Surcharge Liability Notice, is the following, standard, paragraph:

"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 Service on 0845 010 9000".

16. The reverse of each notice details how surcharges are calculated and the percentages used in determining any financial surcharge in accordance with the VAT Act 1994 s 59(5).

17. The requirements for submitting timely electronic payments can in any event be found-

- In notice 700 "the VAT guide" paragraph 21.3.1 which is issued to every trader upon registration.
- On the actual website www.hmrc.gov.uk
- On the E-VAT return acknowledgement.

18. The Surcharge has therefore been correctly issued in accordance with the VAT Act 1994 s 59(4), payment having been received by HMRC after the due date.
19. With regard to the Appellant's grounds of appeal, it is specifically stated in s 71(1) VATA 1994 that any insufficiency of funds to pay any VAT is not reasonable
5 excuse.
20. HMRC may allow additional time for payment if requested. Any request must be made prior to the date on which the VAT falls due. The Appellant requested Time to Pay the VAT due for the period 12/12 and this was agreed by HMRC. As a result the Default Surcharge for this period was cancelled.
- 10 21. The Appellant requested a further Time to Pay the VAT due for the period 03/13. As this concession had been given to the Appellant for the previous quarter, the Time to Pay request was refused.
- 15 22. HMRC contend that traders, having been granted this concession in the past, have no guarantee that it will be given again. A Time to Pay agreement is designed to be a short term solution to enable the Appellant to get over a short term financial difficulty, not a method of making continuous late payments.
23. The Appellant has been in the Default Surcharge regime since period 04/11. The Appellant was issued with a Surcharge Liability Notice Extension at the rate of 15% for periods 03/12, 06/12 and 12/12.
- 20 24. HMRC contend that the Appellant would have been aware that the Default Surcharge for the period 03/13 would be calculated at the maximum rate of 15% as they had received three previous Surcharge Liability Notice Extensions at this rate. The Appellant was also aware that the Time to Pay request had been refused and HMRC maintain they had no expectation that any Surcharge Liability Notice
25 Extension for the period would be cancelled.
25. The Appellant has stated that they were suffering cash flow problems and that they had bad debts worth £35,000.00 for period 2012/13.
26. The VAT Returns for the year ending 31 March 2013 show that the total value of sales and other outputs excluding VAT was £2,732,075. The Appellant's bad debts of
30 £35,000 is therefore less than 1.3% of the total sales less VAT and the Default Surcharge of £13,179.28 for the period 03/13 is less than 2% of the total value of sales net of VAT £816,625.
27. HMRC contend that the recessionary climate affecting the UK at the date of the defaults affected all businesses and as such there is nothing exceptional affecting this
35 business which can be agreed as a reasonable excuse.
28. In response to the statement that the Appellant considers that the penalty should be cancelled, or at the very least reduced: HMRC contend that surcharges are fixed by statute and once a default occurs a surcharge accrues at the percentage rate applicable.

Neither the Commissioners nor the Tribunal have the power to reduce the amount due to mitigating circumstance.

29. The Appellant indicates in its Notice of Appeal that the surcharge is unfair and excessive. The case of *Total Technology (Engineering) Limited v HMRC* was heard in the Upper Tribunal when it was held that:

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- 1) There is nothing in the architecture of the default surcharge system which makes it fatally flawed.
- 2) The Tribunal found that the default surcharge penalty regime does not breach EU law on the principle of proportionality.
- 3) In order to determine whether or not a penalty is disproportionate, the Upper Tier Tribunal addressed the following factors:
 - (a) The number of days of the default
 - (b) The absolute amount of the penalty
 - (c) The ‘inexact correlation of turnover and penalty’
 - (d) The ‘absence of any power to mitigate’

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The Upper Tribunal Chamber President, Mr. Justice Warren and Judge Colin Bishopp decided that none of these factors leads to the conclusion that the Default Surcharge regime infringes the principle of proportionality.

Conclusion

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30. The Appellant was clearly aware of the due date for payments of its VAT and the potential consequences of late payment.

31. The Appellant’s grounds of appeal are that it was suffering cash flow shortages at the time of the default.

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32. In *Customs & Excise Commissioners –v- Steptoe* [1992] STC 757 the tax-payer argued that although the proximate cause of his default was insufficiency of funds, the underlying cause of that insufficiency, namely the unexpected failure by a major customer to pay him on time, amounted to a reasonable excuse. The Court determined on a majority, that the statutory exclusion of insufficiency of funds as an excuse did not preclude consideration of the underlying cause of insufficiency and that a trader might have a reasonable excuse if it were caused by an unforeseeable or inescapable event or when, despite the exercise of reasonable forethought and due diligence, it could not have been avoided. The Court nevertheless made it clear that the test had to be applied strictly.

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33. To decide whether a reasonable excuse exists where insufficiency of funds causes the failure, the Tribunal must take for comparison an individual in a similar situation to that of the actual tax-payer who is relying on the reasonable excuse defence. The Tribunal should then ask itself, with that comparable person in mind, whether notwithstanding that person’s exercise of reasonable foresight, due diligence and a proper regard for the fact that the tax would become payable on the particular dates,

the Appellant could not have avoided the insufficiency of funds which led to the failures.

5 34. The Tribunal accepts that the underlying cause of the defaults may have been cash flow shortage. However the Appellant has not provided any information to show that the cash flow shortage was entirely unforeseeable, outside the normal hazards of trading or due to events beyond its control.

10 35. The Appellant requested Time to Pay but was refused. HMRC will usually agree Time to Pay where it believes that the tax-payer is genuinely unable to pay in full and on time. Also, that by allowing him extra time, it will mean that he can pay what is due and that he will return to making future payments in full and on time. In this case the Appellant had been in the VAT default surcharge regime since 04/11 and had previously been afforded Time to Pay. Whether or not to agree to a deferral of VAT due is entirely within the discretion of HMRC and the Tribunal has no jurisdiction to interfere with the exercise of that discretion.

15 36. The Appellant says that the surcharge is excessive and unfair. For the reasons submitted by HMRC and set out in paragraph 28 above, this is not a ground of appeal which can be considered by the Tribunal. Legislation lays down the surcharges to be applied in the event of VAT being paid late and surcharges are applied at a rate which is fixed by statute and is determined by the number of defaults in any surcharge liability period. Penalties are therefore commensurate with the number of defaults and
20 the amount of VAT paid late.

37. The burden of proof is on the Appellant to show that it has a reasonable excuse for the late payment of VAT for the period 03/13. In the Tribunal's view, for the reasons given above, that burden has not been discharged.

25 38. The appeal is accordingly dismissed and the surcharge upheld.

39. 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
30 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.

35 **MICHAEL S CONNELL**
TRIBUNAL JUDGE

RELEASE DATE: 7 October 2014

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