



TC04110

Appeal number: TC/2014/03635

Value Added Tax – Surcharge for late payment of Tax; whether reasonable excuse for failure - Yes; appeal allowed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

J BEWS & SONS

Appellant

- and -

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

Respondents

**TRIBUNAL PRESIDING MEMBER PETER R SHEPPARD FCIS, FCIB, CTA
DR HEIDI POON, CA, CTA, PhD**

Sitting in public at George House, Edinburgh on 23 October 2014

The Appellant was unrepresented

Mrs E McIntyre, Officer of HMRC, for the Respondents

DECISION

Introduction

1. The appellant runs a small business based in Kirkwall, Orkney.
- 5 2. The appeal under consideration was made by the Appellant on 24 June 2014 against surcharges of £406.72 and £61.00, assessed by the Respondents for the late payment of the VAT due for the respective periods ending 28 February 2013 and 28 February 2014.
- 10 3. At the hearing Mrs McIntyre for HMRC explained to the Tribunal that the latter of these surcharges had been assessed in error as both the payment and return had in fact been received by the due date. HMRC had written to the Appellant on 11 August 2014 notifying them that the surcharge had been withdrawn. The Tribunal therefore had only to consider the surcharge for £406.72.
- 15 4. Prior to the hearing the Appellant had contacted the Tribunal and said that in view of the costs and time involved to travel from Orkney to attend the hearing he would not be attending and was happy for the hearing to proceed in his absence.
5. At the hearing HMRC requested for the appeal to continue under the terms of Rule 33 of The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 which states;-
20 “If a party fails to attend a hearing the Tribunal may proceed with the hearing if the Tribunal-
 - (a) Is satisfied that the party has been notified of the hearing or that reasonable steps have been taken to notify the party of the hearing; and
 - (b) Considers that it is in the interests of justice to proceed with the hearing.”
- 25 6. As the Tribunal had ascertained that the Appellant had received notification of the hearing and was happy for the hearing to go ahead without him the Tribunal decided that it was in the interests of justice to proceed with the hearing and granted HMRC’s request.

Legislation

- 30 7. The VAT Regulations 1995 Regulation 25(1) contains provisions for the making of returns and requiring them to be made not later than the last day of the month following the end of the period to which it relates. It also permits HMRC to vary that period, which they do in certain circumstances eg by allowing a further seven days for those paying electronically.
- 35 8. Regulation 25A(3) requires the provision of returns using an electronic system.

9. Section 59 of the VAT Act 1994 sets out the provisions whereby a Default Surcharge may be levied where HMRC have not received a VAT return for a prescribed accounting period by the due date, or have received the return but have not received by the due date the amount of VAT shown on the return as payable.

- 5 10. A succinct description of the scheme is given by Judge Bishopp in paragraphs 20 and 21 of his decision in *Energys Holdings UK Ltd* [2010] UKFTT 20 (TC) TC 0335 which are set out below.

10 20”*The first default gives rise to no penalty, but brings the trader within the regime; he is sent a surcharge liability notice which informs him that he has defaulted and warns him that a further default will lead to the imposition of a penalty. A second default within a year of the first leads to the imposition of a penalty of 2% of the net tax due. A further default within the following year results in a 5% penalty; the next, again if it occurs within the following year, to a 10% penalty, and any further default within a year of the last to a 15% penalty. A trader who does not default for a full year escapes the regime; if he defaults again after a year has gone by the process starts again. The fact that he has defaulted before is of no consequence.*

15 21. *There is no fixed maximum penalty; the amount levied is simply the prescribed percentage of the net tax due. The Commissioners do not collect some small penalties; this concession has no statutory basis but is the product of a (published) exercise of the Commissioners’ discretion, conferred on them by the permissive nature of s 76(1) of the 1994 Act, providing that they ‘may’ impose a penalty, and their general care and management powers. Even though the penalty is not collected, the default counts for the purpose of the regime (unless, exceptionally, the Commissioners exercise the power conferred on them by s 59(10) of the Act to direct otherwise). Similarly, where the monetary penalty is nil, because no tax is due or the trader is entitled to a repayment (.....) the default nevertheless counts for the purposes of the regime, subject again to a s 59(10) direction to the contrary.”*

- 20 11. Section 59(7) VAT ACT 1994 covers the concept of a person having reasonable excuse for failing to submit a VAT return or payment therefor on time.

12. Section 71 VAT Act 1994 covers what is not to be considered a reasonable excuse.

Case law

35 *Customs and Excise Commissioners v Steptoe* [1992] STC 757

HMRC v Total Technology (Engineering) Ltd [2012] UKUT 418 (TCC)

Alan Kincaid T/A A K Construction [2011] UKFTT 225 (TC)

Electrical Installation Solutions Ltd [2013] UKFTT 419 (TC)

Lynx Comms Ltd [2014] UKFTT 487 (TC)

Facts

13. Mrs McIntyre for the Respondents referred to a schedule in the bundle entitled
5 schedule of defaults which detailed late payments and late returns in the period
30 November 2010 to 28 February 2014.

14. The details of the defaults are as follows:

10 In the quarter ended 30 November 2010 tax declared as due on the Appellant's
VAT return was £4,145.52. The return was due by 31 December 2010 but was
not received by HMRC until 18 January 2011. Payment of £4,106.20 was made
on time leaving only £39.32 outstanding and this was received by HMRC on
9 February 2011. The Appellant had sent the return and part of the payment late
so a surcharge was due. As this was the first failure a Surcharge liability notice
was issued but no penalty was levied.

15 In the quarter ended 30 November 2011 tax declared as due on the Appellant's
VAT return was £3,381.07. The return was due on 31 December 2011 but was
not received by HMRC until 3 January 2012 which was in time when the seven
extra days for payments made electronically referred to in paragraph 7 above is
taken into account. Payment was received late on 12 January 2012. As the
20 payment was late a surcharge of 2% was due. HMRC adopt a policy of not
collecting any surcharges that are less than £400. As 2% of £3,381.07 is less than
£400 no penalty was levied but the surcharge liability period was extended a
further 12 months and the surcharge rate for a future failure was increased to 5%.

25 In the quarter ended 31 August 2012 tax declared as due on the Appellant's VAT
return was £5,185.32. The return was due on 30 September 2012. It was received
by HMRC on 5 October 2012. The amount due was paid on 10 October 2012. As
explained above where payment is made electronically the due date is extended
by seven days. Although the return was submitted within this period the payment
was made three days later so a surcharge of 5% of the tax due could have been
30 levied. As 5% of £5,185.32 is less than £400 no penalty was levied but the
surcharge liability period was extended a further 12 months and the surcharge
rate for a future failure was increased to 10%.

35 In the quarter ended 28 February 2013 tax declared as due on the Appellant's
VAT return was £4,067.27. The return was due on 31 March 2013 but was not
received by HMRC until 1 April 2013. The amount was not received by HMRC
until 16 April 2013. As the Appellant had sent the payment late a surcharge was
incurred. Thus the Respondents assessed a surcharge of 10% of the tax paid late
that is £406.72. In addition the surcharge liability period was extended by 12
months and the surcharge rate for a future failure was increased to 15%.

5 In the quarter ended 28 February 2014 tax declared as due on the Appellant's VAT return was £2,129.34. The return was due on 31 March 2014. As HMRC thought payment of £406.72 of the amount due was paid late they levied a surcharge of 15% of that sum being £61. As explained above HMRC accept that this was an error as both return and payment had been received by 7 April 2014 so this surcharge has been removed.

Appellant's written submissions

15. Craig Bews for the Appellant wrote to HMRC Default Appeals team on 23 April 2013. This letter stated:-

10 "I refer to Notice of assessment of Surcharge dated 12 April and my dad's phone call about this.

There are two customers who have accounted for about two thirds of our sales over the last year. They are both very prompt payers and we have no trouble with them.

15 At the end of March we sent them invoices for over £11,000 and expected the usual prompt payment. It was a few days later that we discovered they were on holiday and would not be back before the VAT had to be paid.

20 Dad went to our bank but was told lending is no longer dealt with in Orkney but by a relationship manager who would not deal with our request for at least a week. So much for modern banking!

As soon as our customers came back from holiday, they paid us and we paid you.

Due to circumstances beyond our control, we were unable to pay the VAT at the due date but paid as soon as we got the funds."

25 16. Details from the Appellant's bank statement were included in the papers before the Tribunal. These show an amount of £11,707.78 was credited to the Appellant's bank account on 16 April 2013 and the same day the VAT due to HMRC of £4,067.27 was paid.

30 17. In the Notice of Appeal dated 24 June 2014 the Appellant makes similar points to those made in the letter of 23 April 2013 set out above. The Appellant draws attention to the case of *Alan Kincaid T/A A K Construction* where reasonable excuse was allowed. In the Notice of Appeal the Appellant also referred to HMRC guidance which says "an insufficiency of funds is not a reasonable excuse for failing to pay on time unless attributable to events outside the customer's control."

Respondent's submissions

18. At the hearing Mrs McIntyre for HMRC said that the surcharge had been calculated accurately. It was clear that payment had been made late. She said that it does not matter that payment was only a few days late it was nevertheless late.

5 19. She criticised the Appellant for not contacting HMRC to let them know of the difficulties. She said that negotiation of a Time To Pay arrangement may have been possible. She considered that delayed payments are a normal hazard of trade.

20. In respect of a question from the Tribunal as to the possibility of the application of the decision in the case of *Steptoe*, Mrs McIntyre said that HMRC currently preferred the decision of the First-tier Tribunal in the *Electrical Installation Solutions Ltd* case which refers to the *Steptoe* decision. She said that HMRC had tried to get details from the Appellant such as the breakdown of the credits to the account to establish how much related to each customer but this had not been provided.

21. She said that banks usually advise customers of changes in terms and conditions and suggested that the Appellant must have failed to pick this up.

22. The Appellant's letter of 23 April 2013 was taken by HMRC as a request for a review. The result of that review was given in a letter to the Appellant dated 26 June 2013 which advised that HMRC did not consider the Appellant had reasonable excuse for the failure. They considered that the reason for the failure was insufficiency of funds which is specifically excluded as a reasonable excuse by the VAT Act 1994 Section 71(1)(a).

23. In respect of the case of *Alan Kincaid T/A A K Construction* where reasonable excuse was allowed HMRC pointed to paragraph 18 of the decision which discusses reasonable excuse. It states "*The Tribunal assesses whether the trader had reasonable excuse from the perspective of a prudent business person exercising reasonable foresight and due diligence with a proper regard for the fact that the tax would become payable on particular dates.*"

24. Mrs McIntyre also pointed to paragraph 12 in the First-tier Tribunal decision in the case of *Move Up Lofts Limited* which states "*In Kincaid, the First-tier Tribunal was considering 'reasonable excuse' in the context of the construction industry scheme legislation which does not have a provision analogous to section 71(1)(a) VATA requiring the Tribunal not to regard an insufficiency of funds as a reasonable excuse.*"

Decision

35 25. The level of the penalties and whether or not they are disproportionate is discussed at length in the Upper Tribunal's decision in *HMRC v Total Technology (Engineering) Ltd*. The decision also discusses the fact that there is no power of mitigation available to the Tribunal. The only power in this respect is that if the tribunal considers the amount of the penalty is wholly disproportionate to the gravity of the offence, if it is not merely harsh, but plainly unfair, then the penalty can be

discharged. For example in *Energys Holdings Ltd* the Tribunal discharged a potential penalty of £130,000 for the submission and payment of a return submitted one day late.

5 26. The level of the penalties has been laid down by parliament and unless the surcharges have not been issued in accordance with legislation or have been calculated inaccurately the Tribunal has no power to discharge or adjust it other than for the reason outlined in paragraph 27 below.

10 27. The only other consideration that falls within the jurisdiction of the First-tier Tribunal is whether or not the Appellant has reasonable excuse for his failure as contemplated by Section 59(7) VAT Act 1994.

28. In the correspondence the Appellant has accepted that the payment for the VAT return for the period to 28 February 2013 had been made late.

15 29. The VAT Act 1994 Section 71(1) specifies that an insufficiency of funds is not regarded as a reasonable excuse. However the reason for the lack of funds might be. The Appellant pointed to two unforeseen events that caused his lack of funds. Firstly two customers who are normally very prompt payers had gone on holiday. When the Appellant realised that he was not going to be paid in time for him to meet his VAT return payment he visited his bank to arrange a short term loan. He was then confronted with a second unforeseen difficulty in that the bank on Orkney no longer dealt with lending but this was now done by a relationship manager who would not deal with the request for at least a week.

25 30. The Appellant might be criticised for not advising HMRC of his difficulty. Negotiation of Time To Pay arrangements may have been possible for example. Nevertheless the Tribunal considers that the two unforeseen events outside the Appellant's control, when taken together, provide the Appellant with a reasonable excuse for the late payment. The Appellant was well aware of the date the payment was due and tried to make arrangements with his bank. On the same day that he received funds from one of his customers he paid the outstanding VAT bill.

30 31. The Tribunal observes that two customers constituted over two-thirds of the business of the company and therefore the decisions of *Steptoe* and *Electrical Installations Ltd* could have had a bearing on the case but insufficient evidence in support of such an argument was presented by the appellants.

35 32. The Appellant has established that there was a reasonable excuse for the late payment of the return for the period ending 28 February 2013 and therefore the Tribunal allows this appeal.

40 33. 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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**PETER R SHEPPARD
PRESIDING MEMBER**

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RELEASE DATE: 7 November 2014