



TC04232

Appeal number: TC/2013/09538

VAT default surcharge - payment made late - insufficiency of funds - whether reasonable excuse - no - whether penalty disproportionate - no - appeal dismissed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

LEN PANG CHEAH t/a L P C SHADES

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE MICHAEL S CONNELL
MR NOEL BARRETT**

**Sitting in public at Bradford Appeals Tribunal, Phoenix House, Rushton Avenue
Bradford on 6 October 2014**

Len Pang Cheah the Appellant in person

Ms. Nadine Newham Officer of HM Revenue and Customs, for the Respondents

DECISION

The Appeal

1. Len Pang Cheah ('the Appellant') appeals against a default surcharge of £933.67
5 reduced to £907.48 imposed by HMRC on 13 September 2013, in respect of the VAT
period ended 30 July 2013, (period 07/13), for his failure to submit, by the due date,
payment of VAT due. The surcharge was calculated at 15% of the VAT due of
£6,224.48.
2. The Appellant had also submitted a (late) appeal against an earlier default
10 surcharge of £1,208.16 imposed by HMRC on 14 December 2012, in respect of the
VAT period ended 3 October 2012, for his failure to submit, by the due date, payment
of VAT due. The surcharge was calculated at 15% of the VAT due of £8,491.07. The
surcharge was however withdrawn by HMRC prior to the hearing following a review.
3. The point at issue is whether or not the Appellant has a reasonable excuse for
15 making the late payment in respect of period 07/13.

Background

4. The Appellant's business has been VAT registered since July 1989. The main
business activity is the sale of computer consumables on the internet and at trade fairs.
5. The Appellant has been in the VAT default surcharge regime from period 01/10.
20 He says that he has suffered difficult trading conditions since 2008 and has been given
'Time To Pay' (TTP) several times in the past.
6. The Appellant paid VAT on a quarterly basis. Section 59 of the VATA 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
25 1995.]
7. 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.
8. In respect of the 07/13 default, as payment was made electronically the due date
30 was 7 September 2013. The return was received on 31 August 2013. At the date the
VAT default surcharge was imposed, on 13 September 2013, the amount of VAT
outstanding was £5,190.81, a payment of £174.59 having been made by way of offset
from the Appellant's 04/13 return and the sum of £859.08 having been made by way
35 of offset from the Appellant's 10/13 return.
9. 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 :

‘(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 –

- 5 (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
- 10 (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.

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

‘(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.’

20 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

25 11. 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

30 12. The Appellant does not dispute that his VAT payment for the period 07/13, was late. In a letter dated 1 October 2013 to HMRC asking for a review of the decision to impose the surcharge, the Appellant said that “business was slow at the end of 2012 and the beginning of 2013” and that he “did not make important sales at Christmas”.

13. The Appellant’s stated grounds of appeal in his Notice of Appeal dated 12 December 2013, were:

35 “Trading conditions have been extremely challenging since autumn 2008, then in September 2010 we had a major break-in when £60k of goods was stolen. My insurance company refused to pay compensation because there was a difference between the alarm specification and the actual alarm installed. My insurance broker advised me to sue my alarm company, but

40 their contract only had a maximum compensation of £1,000.00. I intend to engage a solicitor when I have sufficient funds. Unfortunately after this catastrophic event, all my suppliers reduced my credit limit, hence I had

5 problems paying my suppliers and also my VAT, resulting in surcharges for
previous periods. I informed HMRC of my situation and appeal against the
surcharges but was refused. As I was still having problems paying my VAT, I
10 contacted an HMRC officer who suggested that I should approach my bank
for assistance. When I did so I was told by my NatWest bank manager (part
of RBS), that my account would be immediately transferred to their special
management unit. My new account manager promptly made me repay my
overdraft facility at a higher rate of £616.86 per month. Trading conditions in
the latest quarter were very challenging.... The margin for trading on the
15 internet is being squeezed to less than 10%. Imposing a 15% surcharge of
£933.67 will cause severe hardship to my business and might jeopardise my
efforts to carry on trading. All my remaining staff have taken a pay cut and in
some cases I owe them back pay. I am a small business proprietor suffering
immense hardship.”

14. At the hearing the Appellant reiterated and expanded on his business’s
difficulties. He accepted that the burglary had occurred three years prior to the
default under appeal but said that it had taken his business far longer than expected to
recover. His line of business being internet-based was extremely competitive.

20 15. His authorised overdraft in 2010 was £70,000, but following the burglary his
bank wanted to transfer £30,000 to a formal loan arrangement and for him to pay off
the balance of £40,000 by way of monthly payments of £616, which he found
extremely difficult. His children had loaned him money but this caused difficulties
25 within the family. He got into serious financial difficulties having County Court
judgements entered against him and a charging order against his property. He made a
small gross profit in the last few years but after overheads and costs of finance he had
actually made a loss.

30 16. The Appellant said that he suffered a heart attack in August 2014 and an earlier
hearing had to be postponed. His doctor told him that he was working too hard and
that stress had more than likely precipitated the attack. He had now recovered and was
trading at a small profit and paying his VAT on time. In 2013 he owed his suppliers in
excess of £50,000 and was still trying to pay that off. He had to, in order to ensure
that its suppliers continued to provide him with stock.

HMRC’s contentions

35 17. The Period 07/13 had a due date of 7 September 2013 for electronic VAT
Payments and Returns. The Appellant paid his VAT electronically. The tax due was
£6,224.48. As the £5,109.81 was not paid on time the Surcharge was correctly
imposed.

40 18. The Appellant entered the Default Surcharge Regime following a default in
period 10/10. He then defaulted in periods, 04/11, 07/11, 04/12, and 07/12, and again
in period 07/13 which is the period under appeal.

19. The potential financial consequences attached to the risk of default should have been known to the Appellant from the information printed on the 10/10 Surcharge Liability Notice.

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

10 *"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".*

15 21. 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).

22. 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.
- 20 • On the actual website www.hmrc.gov.uk
- On the E-VAT return acknowledgement.

23. The Surcharge has therefore been correctly issued in accordance with the VAT Act 1994 s 59(4).

25 24. 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 a reasonable excuse.

30 25. HMRC may allow additional time to pay ("TTP") if requested. Any request must be made prior to the date on which the VAT falls due. The Appellant made no contact with HMRC prior to the due dates for payment and did not make any request for a time to pay arrangement. The Appellant was well aware of TTP agreements, having by his own admission had several such agreements in the past. There was no TTP in place prior to the defaults in regard to the payment the subject of this appeal as the Appellant had been informed by HMRC that they would not grant any further TTP agreements.

35 26. Due to cash flow problems arising from the burglary, a review of the 10/10 surcharge was requested in October 2011. The surcharge was withdrawn and subsequent surcharges amended. A surcharge was not issued for the 01/11 period as the Appellant had requested Time to Pay. As contact had been made with HMRC prior to the due date, and under s 108 of the Finance Act 2009 the surcharge was

inhibited. At the time the Appellant was informed that he may not be eligible for any further TTP's given that several had been allowed in the past.

5 27. HMRC appreciate the loss of stock would have caused financial difficulties. However, whilst the burglary was a reasonable excuse for the 10/10 and 01/11 periods, it cannot be considered so for the 07/13 period.

28. In the letter dated 1 October 2013, it is stated that business was slow at the end of 2012 and the Appellant did not make important sales at Christmas. HMRC contend that this argument is nothing out of the ordinary in the recent difficult financial climate and is in essence a normal hazard of business.

10 29. The Appellant runs a cash business, so the VAT due is paid to the business at the point of sale. Although there is nothing to prevent the Appellant using the VAT collected in the business, the VAT due to HMRC must be paid in full by the due date.

15 30. As HMRC were unable to assist with further TTP's the Appellant was advised to contact the bank for assistance. A bank statement has been provided which shows the Appellant's account was overdrawn by £27,663.51 on the 6 September 2013. The Appellant was contacted by telephone and he stated the overdraft limit at this point was £30,000. The VAT due for the period was £6,224.48, and therefore based on the information given by the Appellant. At this point there were insufficient funds available to settle that VAT liability.

20 31. HMRC contend that the excuses adduced by the Appellant do not amount to a reasonable excuse. Specifically, the reasons for the default appear to be no more than typical business risks and problems encountered generally by businesses on a regular basis.

25 32. The Appellant says that the surcharge is entirely disproportionate to the delay which has occurred. The case of *Total Technology (Engineering) Limited v HMRC* was heard in the Upper Tribunal when it was held that:

- 30 1) There is nothing in the architecture of the Default Surcharge system which makes it fatally flawed.
- 30 2) The Tribunal found that the DS penalty does not breach EU law on the principle of proportionality.
- 30 3) In order to determine whether or not a penalty is disproportionate, the Upper Tier Tribunal addressed the following factors:
 - 35 (a) The number of days of the default
 - 35 (b) The absolute amount of the penalty
 - 35 (c) The 'inexact correlation of turnover and penalty'
 - 35 (d) The 'absence of any power to mitigate'
- 40 4) The Upper Tribunal Chamber President, Mr. Justice Warren and Judge Colin Bishopp decided that none of these leads to the conclusion

that the Default Surcharge regime infringes the principle of proportionality

Conclusion

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33. The Appellant was clearly aware of the due date for payment of his VAT and the potential consequences of late payment.

34. The Appellant's first ground of appeal is that he was suffering cash flow shortages at the time of the default.

10 35. 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
15 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.

20 36. To decide whether a reasonable excuse exists where insufficiency of funds causes the failure the Tribunal must take for comparison a person 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
25 the fact that the tax would become payable on the particular dates, those factors would not have avoided the insufficiency of funds which led to the failures.

30 37. The Tribunal accepts that the underlying cause of the defaults may have been a severe cash flow shortage. However the Appellant has not been able to provide any information to show that the cash flow shortage was entirely unforeseeable, outside the normal hazards of trading or due to events beyond his control. As HMRC say, whilst the burglary was a reasonable excuse for the 10/10 and 01/11 periods, it cannot be considered so for the 07/13 period as this was almost three years later.

35 38. 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. However, although business was slow at the end of 2012 and the beginning of 2013, as HMRC say, this is in essence a normal hazard of business, and in any event was eight months before the default.

40 39. The burden of proof is on the Appellant to show that he has a reasonable excuse for the late payment of VAT for the period 07/13. In our view, for the reasons given above, that burden has not been discharged.

40. The Appellant's second ground of appeal is that the surcharge is disproportionate. We do not consider the surcharge unfair. Legislation lays down the surcharges to be applied in the event of VAT being paid late and surcharges are applied at a rate which fixed by statute and is determined by the number of defaults in any surcharge liability period. Further, for the reasons submitted by HMRC and set out in paragraph 32 above, in our view the default surcharge cannot be regarded as disproportionate.

41. The appeal is accordingly dismissed and the surcharge upheld.

42. 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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MICHAEL S CONNELL
TRIBUNAL JUDGE

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RELEASE DATE: 16 January 2015

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