



TC04311

Appeal number: TC/2014/05249

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

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

MPH JOINERY LTD

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE MICHAEL S CONNELL
MR PETER R SHEPPARD**

Sitting in public at Alexandra House, The Parsonage, Manchester on 24 November 2014

Mr John Young for the Appellant

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

DECISION

The Appeal

- 5 1. MPH Joinery Limited ('the Appellant') appeals against a VAT default surcharge of £6,625.50 imposed by HMRC on 12 July 2013, in respect of the VAT period ended 31 May 2013, for its failure to submit, by the due date, payment of VAT due ("the first default"). The surcharge was calculated at 15% of the VAT due of £44,170.01.
- 10 2. The Appellant also submits a late appeal against a default surcharge of £8,430.22 imposed by HMRC on 11 October 2013, in respect of the VAT period ended 31 August 2013, for its failure to submit, by the due date, payment of VAT due ("the second default"). The surcharge was calculated at 15% of the VAT due of £56,201.51.
3. The point at issue is whether or not the Appellant has a reasonable excuse for making the late payments.

15 Background

4. The Appellant has been registered for VAT since 3 March 2011. The company's business is that of bespoke joinery and shop fitting. The directors are Mr J Young and Ms R Sanders.
- 20 5. The Appellant has been in the VAT default surcharge regime from period 08/11.
6. The Appellant was on a quarterly basis for submission of VAT returns. VAT returns and payment of VAT are required to be made on or before the end of the month following each accounting period. [Section 25 VAT Act 1994 and Reg 25(1) and Reg 40(1) VAT Regulations 1995.]
- 25 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.
- 30 8. Section 59 of the VAT Act 1994 provides for a default surcharge to be levied for failure to provide a return within the prescribed time limit and also for failure to make payment on time.
9. In respect of the first default, as payment was made electronically the due date for the 05/13 period was 7 July 2013. The return was received on 5 July 2013 and the VAT payment on 3 August 2013, therefore almost a month late.
- 35 10. In respect of the second default, as payment was made electronically, the due date for the 08/13 period was 7 October 2013. The return was received on 11 October 2013 and the VAT payment by way of twelve instalments, between 14 October 2013 and 18 July 2014.

5 In year 11/12 a repayment of more than 36K was due, which was only received after providing documentation. The majority of this documentation had already been submitted by other means either by MPH or MPH's customers. Of course, HMRC could not have seen bank statements, so these would have been required and this is accepted. The repayment was eventually received about nine months after the end of tax year 11/12. The repayment was paid directly into our VAT account.

10 In year 12/13, a smaller repayment was due and although it amounted to 5K, it took the intervention of our member of parliament to secure our repayment, this was agreed in December 2013 and we received the repayment into our VAT account in January 2014.

15 For the period of 08/13, the VAT due was in a total of VAT which was outstanding in November 2013, which amounted to over 100K. We negotiated a time to pay agreement. This agreement has been fully adhered to; the VAT has been paid in full, leaving only surcharges outstanding. We had previous time to pay agreements prior to this, but we renegotiated these in November 2013.

20 As the full amount of VAT subject to the time to pay agreement was paid in full, we feel some recognition should be given to the work and commitment to the agreement should be acknowledged. Whilst the argument that insufficiency of funds is not a reasonable excuse for late payment of VAT, surely the fact that VAT due has been paid as agreed should be considered when appealing against surcharges. Also, since the last time to pay agreement was implemented, all VAT returns and payments have been made.

25 MPH Joinery is a young company. In 2011 a director absconded from the company leaving all documentation and the company's finance in chaos. It took a great deal of time, work and heartache to turn the company around and get all relevant documentation and procedures into good order. This impacted on the day to day running of the company for quite some time and whilst it is not an excuse, we feel this could and should be taken into consideration when looking at how the company acted with regard to its obligations to HMRC.

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35 Finally in the past 5 years it has been increasingly difficult to borrow money from banks to help businesses, so it was impossible to raise funds to pay VAT from that source. Although the company had funds due to it, it is not possible to control customer's payments. Although funds are promised they generally do not arrive as expected thus creating a major difficulty for business and resulting in surcharges being imposed. As a new business, we were unable to raise short term loans and thus were penalised through technically no fault of our own. Bank statements for the periods in question will show that it was impossible to pay VAT and keep the business afloat due to funds available at the relevant times.

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45 Finally, we would ask you to take in to consideration that due to the action we have taken, we have been able to make the business profitable, doubled turnover, employ 14 people fulltime and supply

work for between 12 and 20 sub-contract self-tradesmen and pay all old and current VAT.”

5 16. At the hearing, Mr Young on behalf of the Appellant summarised the company’s main grounds of appeal, as follows:

- 10 i. A CIS repayment was due for two previous years of 11/12 and 12/13, which took more than nine months to be received from HMRC.
- 15 ii. That a Time to Pay (TTP) agreement was made for the full amount of VAT (including 08/13), which was paid in full as agreed and that some recognition should be given for this.
- 20 iii. That in 2011 the finance director of the company absconded leaving all documentation and finances in chaos resulting in a lot of time and work to turn the company around impacting on the day to day running for a long time. Whilst not an excuse, Mr Young said that this should be taken into consideration with regard to its obligations to HMRC.
- 25 iv. That it has been increasingly difficult to borrow money from banks during last five years, so it was impossible to raise funds to pay VAT from that source. Although the company had funds due to it, it was not possible to control customer’s payments and although funds are promised they generally do not arrive. This creates a major difficulty for business and results in surcharges being imposed.
- 30 v. He states that the Appellant could have closed in November 2014 under the pressure of liability to HMRC. This would have left a shortfall to HMRC of over £100k, but the directors chose to meet their commitments, and have done so. The Appellant feels that this should be recognised by assisting with the appeal against imposed surcharges.

HMRC’s contentions

35 17. The Appellant entered the Default Surcharge Regime following a default in period 08/11. The company then defaulted in seven subsequent periods, prior to the default periods under appeal.

40 18. With effect from the period 01/13 the Surcharge Liability Notice V160 advises a trader how the surcharges are calculated and the percentages used. Subsequent Surcharge Notices advise the trader of the percentage used to calculate the current surcharge, if one has been issued, and/or the percentage which will be used in calculating the surcharge for any subsequent default

19. The potential financial consequences attached to the risk of default should have been known to the Appellant from the information printed on the 08/11 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. As can be seen from the number of defaults, the Appellant has been suffering from cash flow problems for several years.

25 24. However 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 excuse.

30 25. 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 made no contact with HMRC prior to the due dates for payment and did not make any request for a Time to Pay arrangement.

35 26. HMRC has previously assisted the Appellant by agreeing to Time to Pay (TTP) arrangements. A TTP arrangement is given to a trader as a short term solution to financial/cash flow difficulties which they may be experiencing, thus allowing them time to put measures in place to ensure that future liabilities can be paid on time. However in respect of these appeals, contrary to the Appellant's assertion, it did not agree such an agreement prior to the due dates of the periods under appeal.

27. HMRC contend that in respect of the repayments due under the Construction Industry Scheme (CIS), the Appellant should not have relied upon them to pay the VAT due and did not make a formal application for set-off.
- 5 28. Whilst the Appellant had a CIS repayment due, the company had received the VAT due for the periods under appeal and therefore should have had these monies available at the due date to pay the VAT.
29. HMRC also contends that as the Appellant owed other taxes to HMRC (e.g. PAYE), any repayment would be set against those first before any balance available could have been set off against the VAT liability.
- 10 30. The Appellant states that since the last TTP agreement, all VAT returns and payments have been made on time. HMRC contends that irrespective of whether the TTP was adhered to, the fact remains that payment was made after the due date and therefore the surcharges were correctly due and payable.
- 15 31. The Appellant states that in 2011, a director of the company absconded leaving all documentation and finances in chaos resulting in a lot of time and work to turn the company around and that this impacted on the day to day running of the company. The Appellant states that this should be taken into consideration with regard to its obligations to HMRC. HMRC acknowledges that the Appellant has worked hard to overcome this situation, but contends that more than sufficient time elapsed between
20 the incident and the due dates for the periods under appeal.
32. HMRC contends that the Appellant's arguments regarding its financial difficulties are nothing out of the ordinary, and in essence are normal business risks. As a VAT registered company the Appellant charged VAT to their customers and is required by law to pay this by the due date.
- 25 33. HMRC therefore contend that the surcharges in respect of the periods 05/13 and 08/13 have been correctly issued in accordance with VATA 1994 s 59(4), payment having been received after the due date.

Conclusion

- 30 34. The Appellant was clearly aware of the due dates for payment of its VAT and the potential consequences of late payment.
- 35 35. The Appellant's first ground of appeal is that it was suffering cash flow shortages at the time of the defaults.
- 40 36. In *Customs & Excise Commissioners v Steptoe* [1992] STC 757 the taxpayer 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.

5 37. 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 taxpayer 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,
10 those factors would not have avoided the insufficiency of funds which led to the failures.

15 38. The Tribunal accepts that the underlying cause of the defaults may have been cash flow shortages. 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 its control

39. The Appellant could have requested time to pay but did not do so.

40. 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.

20 41. The burden of proof is on the Appellant to show that it had a reasonable excuse for the late payment of VAT for the periods 05/13 and 08/13. In the Tribunal's view, for the reasons given above, that burden has not been discharged.

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

25 43. 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)"
30 which accompanies and forms part of this decision notice.

35 **MICHAEL S CONNELL**
TRIBUNAL JUDGE

RELEASE DATE: 4 March 2015

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