[2015] UKFTT 0676 (TC)

TC04793

Appeal number: TC/2012/10500

DEFAULT SURCHARGE – provision of temporary social care workers to managed service companies – cash flow problems as a result of on-going delays in payment by client accounting for some 45% of the company's business – whether reasonable excuse – in the circumstances, no – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

SOCIAL CARE 4U LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE MALCOLM GAMMIE CBE QC
MRS CAROL DEBELL

Sitting in public at Bedford Square, London WC1 on 4 December 2013

David Mtsika-Mahwe (Accountant) of Muson & Hills LLP for the Appellant

Bruce Robinson (HMRC Officer) for the Respondents

DECISION

Introduction

1. Social Care 4U Ltd (the "Appellant") appeals against default surcharges levied for the three periods, 09/11, 12/11 and 03/12 totalling £16,592.79.

2. The Appellant had been in the default surcharge regime since period 09/10. In relation to the periods under appeal—

> (1) The due date for period 09/11 was 7 November 2011 for electronic submission and payment. The return was received on 19 October 2011 and payments were received between 6 December 2011 and 10 February 2012.
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> (2) The due date for period 12/11 was 7 February 2012 for electronic submission and payment. The return was received on 30 January 2012 and payments were received between 10 February 2012 and 4 May 2012.
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> (3) The due date for period 03/12 was 7 May 2012 for electronic submission and payment. The return was received on 25 April 2012 and payments were received between 4 May 2012 and 9 October 2012.

3. The Appellant had entered into 'time-to-pay' (TTP) agreements in the past but in respect of the period 06/11, a default surcharge was issued because no TTP was requested or agreed before the due date of 7 August 2011. Although the Appellants had told the Respondents on 19 October 2011, when the return for 09/11 was received, that the Appellant would be unable to pay in full by the due date, but that it would pay what it could by then and the balance as soon as possible thereafter, no TTP was made. A TTP agreement was requested for the period 12/11 but was refused, as was also the case for the period 03/12.

4. In its grounds of appeal the Appellant referred to a flood at the Appellant's offices that had occurred on 23 May 2012, caused by an overflow or leak from the flats above. This had evidently damaged computer equipment and records so that the Appellant was unable to trade properly from the premises for a period during June, July and August 2012 and had caused it considerable losses. All this, however, post-dated the occasion of the defaults for the three periods under appeal and cannot therefore represent a reasonable excuse for the defaults.

5. The Appellant's principal activity was the supply of labour for the domiciliary care industry in the London and Greater London areas. The Appellant's clients were managed services companies, such as Ranstad Sourceright, Matrix, Hays, Comensura and Beeline International (formerly Badnoch & Clark), and those companies' clients were the social care departments of London Boroughs such as Hackney, Haringey and Barnet and Redbridge.

6. The terms under which the Appellant operated were "pay when paid". In other words, the Appellant was paid when the managed service companies were paid. At the same time the managed services companies expected all care workers to be paid

weekly so as to avoid absenteeism or other reasons for non-appearance at work even when the managed services companies were withholding payment under their contractual terms with the Appellant. At least, this was what we were told by Mr Mahwe for the Appellants although we only saw the details relating to Ranstad Managed Services Ltd ("Ranstad") to which we refer below.

7. Between 2009 and 2010 the Appellant's turnover increased from £1,199,489 to £1,968,906 and from the VAT period 09/10 it started reporting VAT on an accruals basis because it was estimated that it had exceeded the permitted threshold for cash accounting. At around the same time Ranstad took over various appointments and in August 2010 the Appellant entered into new contracts with Ranstad relating to the provision of the services of care workers. Between 2009 and 2010 the revenue attributable to the Appellant's arrangements with Ranstad increased significantly from £108,479 to £901,323. This represented an increase from 9 per cent of the Appellant's turnover to 45.8 per cent of its turnover.

8. After 2010, the Appellant's turnover declined to some extent. Thus, in 2011 and 2012 (being the years which include the default period with which we are concerned) the Appellant's turnover declined to £1,859,862 and £1,370,938. Its revenues derived from Ranstad reduced to £850,819 for 2011 and £567,439 for 2012, representing 45.7 per cent and 41.4 per cent of turnover.

9. Starting early in 2010 the Appellants began to experience cash-flow problems under its contracts with Ranstad. Mr Mahwe for the Appellants produced a large number of e-mails together with a schedule summarising the principal features of the e-mails and aimed at exploring the underlying causes of the Appellant's insufficiency of funds, which he said was the cause of its defaults in periods in question. The e-mail summary records events from 22 February 2010 through to 16 May 2011.

10. We think it unnecessary to set matters out in great detail or to attempt a further summary of the material that Mr Mahwe produced to us. The essence of the cash flow problem revolved around the fact that the Appellant was having to pay the social care workers on a weekly basis but was only being paid by Ranstad monthly. In addition social care workers were evidently paid on production of a signed timesheet but the timesheet had to be entered on a purchase order system before Ranstad would pay the Appellant, and this was in effect not in the Appellant's hands but in Ranstad's. One further factor to which Mr Mahwe drew our attention and which he said compounded the Appellant's problems, was that under its 2010 arrangements with Ranstad, if a worker supplied by the Appellant converted to a permanent employee after 13 weeks consecutive assignment, this would apparently happen 'free of charge'. The Appellant would therefore lose that worker as part of its payroll with an adverse effect on its turnover.

11. Mr Mahwe provided the VAT returns for the periods of default together with detailed VAT report schedules of the payments, payments on account and various Ranstat self-billing invoices. He did not call any director or other witness on the Appellant's behalf to provide a more detailed explanation of the operation of Appellant's business, its relationship with Ranstad or of the cash flow difficulties from which it was said to have suffered.

12. Liability to the default surcharge is laid down by section 59 of the Value Added Tax Act 1994 and the relevant percentage charge for late payment of the tax is specified in sub-section (5). The consequences of a default may be avoided if the person concerned has a reasonable excuse but by section 71(1)(a) of the Act an insufficiency of funds to pay any VAT due is not a reasonable excuse.

13. Nevertheless, Mr Mahwe relied upon the decision of the Court of Appeal in *Customs and Excise Commissioners v Steptoe* [1992] STC 757 to say that in the Appellant's case, they were entitled to rely upon the underlying case of insufficiency rather than the insufficiency itself.

14. The relevant facts of *Steptoe* appear in the decision of Lord Justice Scott. Mr Steptoe was an electrical contractor who did 95 per cent of his work for the London Borough of Redbridge. The Redbridge Council was virtually his only customer and was an extremely slow payer. He was late in paying VAT in several quarters starting with that ending in November 1986 and continuing up to the end of November 1988. The VAT Tribunal concluded that the conduct of the Council was such that Mr Steptoe had a reasonable excuse for three of the four default surcharges that had been imposed but not the fourth because by the time that was incurred the Council had mended its ways and he could not rely on the excuse that in the fourth period his accountants were responsible for the delay.

15. Scott LJ nevertheless concluded that Mr Steptoe did not have a reasonable excuse because late payment was not an unforeseeable event in the conduct by the taxpayer of his business, such that the taxpayer should have made arrangements to secure his cash flow. If his profit margins were so slim or his financial circumstances such that was unable to secure his cash flow, he was nevertheless caught by what is now section 71(1)(a): "*The reason for the insufficiency of funds is, in such a case, itself an insufficiency of funds.*"

16. Lord Justice Scott was, however, in a minority. The Master of the Rolls, Lord Donaldson, and Lord Justice Nolan upheld the Tribunal's decision, which had concluded in favour of Mr Steptoe. In doing so Lord Donaldson summarised the different approaches of Scott and Nolan LJJ in these terms ([1992] STC 757 at 770):

> "The difficulty which then arises is that Parliament has not specified what underlying causes of an insufficiency of funds which lead to a default are to be regarded as reasonable or as not being reasonable. … Nolan LJ, as I read his judgment explaining and expanding on his judgment in *Customs and Excise Comrs v Salevon Ltd* [1989] STC 907, is saying that if the exercise of reasonable foresight and due diligence and a proper regard for the fact that the tax would become due on a particular date would not have avoided the insufficiency of funds which led to the default, then the taxpayer may well have a reasonable excuse for non-payment, but that excuse will be exhausted by the date on which such foresight, diligence and regard would have overcome the insufficiency of funds.
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> Scott LJ on the other hand is of the opinion that the underlying cause of the insufficiency of funds must be an 'unforeseeable or inescapable event'. I have come to the conclusion that this is too narrow in that (a) it gives insufficient weight to the concept of reasonableness and (b) it treats foreseeability as relevant in its own right, whereas I think that 'foreseeability' or as I would say

> 'reasonable foreseeability' is only relevant in the context of whether the cash flow problem was 'inescapable' or, as I would say, 'reasonably avoidable'. It is more difficult to escape from the unforeseeable than from the foreseeable."

17. At the hearing Mr Mahwe put forward a strong case on behalf of the Appellant for us to allow its appeal on the grounds, essentially, that it had had to surrender control of its cash flow to Ranstad and that Ranstad accounted for nearly half of its business. Nevertheless, the material put before us on this matter were the e-mails, invoices and VAT report figures, none of which however benefitted from an explanation provided by any witness (similar to Mr Steptoe) who could speak on behalf of the Appellant and who was directly involved in its business and its on-going relationship with Ranstad. As it is, our more detailed review of the papers that Mr Mahwe submitted on the Appellant's behalf and consideration of its arguments have lead us to conclude that the Appellant has not sufficiently demonstrated that it satisfies the *Steptoe* test.

18. We accept that the Appellant's arrangements with Ranstad created cash flow problems for the Appellants but apart from the detailed VAT reports for the periods in issue, much of the documentary material that Mr Mahwe submitted on the Appellant's behalf dated back to 2010 and did not provide us with a sufficiently clear picture for the default periods with which we are concerned in 2011 and 2012. We are prepared to accept that the earlier problems with Ranstad continued into those periods and Mr Mahwe produced correspondence with HSBC in January 2012 in which the Appellant had applied for but had been refused an overdraft facility.

19. That said, we find it difficult to conclude that the scale of the Appellant's problems for the periods of default left it in a comparable position to Mr Steptoe. Apart from a certain lack of clarity on the precise position for the actual periods of default, Ranstad certainly accounted for a large part of the Appellant's business but still less than half of it. Furthermore, this was not a business that was without cash altogether: its turnover provides some indication of the extent of its overall cash flow. Briefly, for this portion of its business, the Appellant had got itself into a situation where it had decided to use its available cash flow to pay its temporary social care workers for the services that they had provided through Ranstad to local councils while Ranstad was continuing to delay or was refusing full payment for those services.

20. To many people it may not seem unreasonable for a business such as the Appellant's, to prefer their social care workers instead of meeting their VAT obligations on a timely basis. Certainly, the Appellant sought to ensure that the outstanding amounts of VAT were paid as soon as they believed that they were able to do. The fact that they did suggest a degree of on-going cash generation capacity within the business but we do not believe that we have clear enough evidence for the periods of default in question to say that this was all that could be done given that the problems with Ranstad had emerged in 2010, well over 12 months before the relevant periods. Mr Steptoe was at risk of being offered no further work by the Council if he complained but there is no equivalent evidence in the Appellant's case nor any indication as to what steps were open to it vis-à-vis Ranstad to alleviate its VAT default position.

21. This Tribunal can only deal with the matter as the law requires and on the evidence received. Although, as *Steptoe* indicates, the type of issue that the Appellant faced in the conduct of its business with Ranstat is *capable* of providing a reasonable

excuse, in the end we are not satisfied in the Appellant's case, having regard to the material before us, that those problems were sufficiently severe to provide the Appellant with a reasonable excuse for the periods of default in question, having regard to section 71(1)(a) and the guidance provided by the Court of Appeal's decision in *Steptoe*. In short, we could see the cash flow issues that the Ranstad business raised for the Appellant but we had not enough evidence for the default periods to satisfy ourselves that the Appellant had a reasonable excuse for those defaults.

22. We therefore dismiss the Appellant's appeal.

23. 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.

MALCOLM GAMMIE
TRIBUNAL JUDGE

RELEASE DATE: 16 DECEMBER 2015