



TC04937

Appeal number: TC/2015/07005

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

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

BINDERY MACHINERY SERVICES

Appellant

- and -

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

**TRIBUNAL: JUDGE W RUTHVEN GEMMELL WS
 MEMBER CHARLOTTE BARBOUR CA CTA**

Sitting in public at Edinburgh on 25 February 2016

Margaret Sharp and Douglas Pearson for the Appellant

Mark Boyle, Officer of HMRC, for the Respondents

DECISION

5 1. Bindery Machinery Services (“BMS”) appealed against a VAT Default Surcharge of £5,009.01, in respect of the period 08/15, for failure to pay the requisite amount of VAT by the due date.

10 2. BMS is a small company operating in specialised machinery, in particular refurbished second hand book binding machines, with much of its trading activities overseas. Mr James Brown, the Managing Director, was unable, because of business commitments, to attend on the day of the hearing but submitted a letter setting out his company’s position. Margaret Sharp, an Executive Director of BMS, and their Accountant, Douglas Pearson, gave evidence and were credible witnesses.

15 3. BMS paid VAT on a quarterly basis and Section 59 of the VAT Act 1994 (“VAT”) requires a VAT return and payment of VAT due on or before the end of the month following the relevant calendar quarter. The due date is extended by seven days where payment is made electronically.

The Facts

20 4. BMS paid its VAT for the quarter 08/14 which was due on 7 October 2014 on 17 October 2015 and was accordingly 10 days late. As this was the first default within a 12 month period no monetary surcharge was levied but a surcharge liability notice was issued on 17 October by HMRC advising BMS that any further defaults would incur a surcharge if they were within a 12 month period.

25 5. BMS paid its VAT for the quarter 11/14, which was due on 7 January 2015, on 29 January 2015 and was, accordingly, 22 days late. As this was the second default a surcharge liability notice was issued for an amount of £604.63, being 2% of the amount due to be paid. Both the VAT and the surcharge were paid on 29 January 2015.

30 6. BMS paid its VAT for the quarter 08/15, which was due on 7 October 2015, on 9 October 2015 and was accordingly two days late. As this was the third default a surcharge liability notice was issued for an amount of £5,009.01, dated 16 October 2015, which was exhibited to the tribunal. This explained that the surcharge was 5% of £100,180.33 of the tax outstanding at the due date. The notice stated that “we have also extended the surcharge period previously notified to you to 31 August 2016. If you did not receive a previous notification of your surcharge period, please note your surcharge period begins on the date of this notice and ends on 35 31 August 2016. If you default again for an accounting period ending between the date of this notice and 31 August 2016 you may receive a 10% surcharge and your surcharge period will be extended”.

40 7. On 28 October 2015 BMS wrote to HMRC appealing the 16 October 2015 notice and stating “instructions were left for our administrative assistant to process a BACS online payment to HMRC first thing on Monday, 5th October. On checking the bank

- on my return to the office on Friday 9 October I found no transactions for HMRC were showing. I immediately processed two same day online payments for the full amount, being £100,180.33. Two payments were necessary as our online limit is £100k. Again, a copy of our bank printout is enclosed. We do appreciate that these
- 5 two payments fall two days after the due date and apologise for this staff error. However, I must write to you as this surcharge represents nearly two weeks wages for our employees, it is a huge amount of money. In these difficult times for manufacturing I would ask you to please forgo this surcharge in this once instance. We will put measures in place to ensure that this does not happen again. We also
- 10 appreciate that business is a two-way street and would welcome your comments on the repayment from you for the period ended 28 February 2014, the return for which was submitted on 7 March 2014 but the repayment of £209,808.84 was not received by us until 9 April 2014, a period of 33 days. We understood that HMRC are allowed 30 days for repayments”.
- 15 8. HMRC replied by letter dated 20 November 2015 to BMS stating that they did not accept that BMS had a reasonable excuse for the default for the default surcharge period 08/15. The letter stated “this is because genuine admin mistakes, honestly and acting in good faith, are not considered as reasonable excuses for surcharging purposes. It is the (sic) ultimately the directors of the company who have the overall
- 20 responsibility to ensure that the return and any payments due are paid on time”.
9. BMS appealed to the tribunal on 2 December 2015 and stated that there was a “genuine administration error”.

Legislation

10. See Appendix 1

25 Cases Referred To

11. See Appendix 2

BMS Submissions

12. BMS tabled at the hearing and referred the tribunal to the case of *Ripon Farm Services Limited* a VAT default surcharge case during which a “time to pay”
- 30 arrangement had been requested from HMRC. Margaret Sharp stated that she had not asked for a time to pay arrangement in relation to the 08/15 payment because she thought it was being dealt with by the BMS administrator, Toni Brown, who dealt with all tax administration matters.
13. BMS further stated that the reason the 08/15 payment was late was because Toni
- 35 Brown was conscious of the very difficult cash flow problems the company had on 7 October 2015 that to make the payment may have caused complications with BMS’s bankers. It was explained that cash flow was tight, primarily because of a delay in receipt of a payment from an overseas customer for £248,000 and which was not received until 9 October 2015.

14. BMS often had an insufficiency of funds because of their trading activities with many overseas customers which resulted in the use of letters of credit which added complexity and often delay to the payment process. It was explained that whereas some payments are made even before the delivery of machinery, some are delayed.

5 15. BMS say that insufficiency of funds was a reasonable excuse in the *Ripon* case where their activities were seasonal. BMS say they had an insufficiency of funds because of the nature of their sales and that is a reasonable excuse.

10 16. It was noted that in the *Ripon* case, the tribunal had referred to the case of *Customs & Excise Commissioners v. Steptoe* 1992 STC 757 and stated “although an insufficiency of funds to pay any VAT due is not a reasonable excuse, the underlying cause of any insufficiency of funds if entirely unforeseen and outside the control of the taxpayer, may constitute a reasonable excuse”.

15 17. BMS were asked for the reasons for the previous two VAT defaults which had resulted in surcharge liability notices and they confirmed that they were also late because of cash flow problems as a result of late payment of funds due to them.

18. BMS stated that they feel it is unfair that HMRC can delay making a repayment to them, as stated in their letter of 28 October 2015.

20 19. BMS say that they dispute that there were three defaults within a 12 month period and, accordingly, that the 08/15 default should be charged at 2% and not 5%. It was explained that the system works on a rolling period and that to come out of the default surcharge period the taxpayer needs to submit each of the next four quarters VAT returns and payments by the due date. Following the first default, any subsequent default extends the period and this is set out in the surcharge liability notice.

25 20. BMS say that they would have found it difficult in the 1½ days whilst they were awaiting the payment of £248,000, which they had been awaiting for weeks, to make a Time to Pay request.

21. BMS say that they acted responsibly, honestly and, as soon as they realised the payment had not been made on 7 October 2015, they put the matter right by making the payment.

30 **HMRC’s Submissions**

35 22. HMRC say that there is no dispute that the three payments were late as a matter of fact and that it is immaterial how many days late they were; that the directors of the company admit that there was an administrative error; that the surcharge was correctly assessed; that there was no reasonable excuse; and that the surcharge was proportionate.

23. HMRC drew the tribunal’s attention to Section 59(1), (2), (4), (5) and (7) VATA and Regulations 25 and 40 of the VAT Regulations 1995 which set out the incidence of the default surcharge and, in particular, that the taxpayer would be liable to a

surcharge unless it satisfies the commissioners or, on appeal, a tribunal that “there is a reasonable excuse for the return all the VAT not having been so despatched”.

24. HMRC also drew attention to Section 108 of the Finance Act 2009 which provides relief or a suspension of penalties during the currency of an agreement for deferred payment commonly known as a ‘Time to Pay’ agreement.

25. HMRC reminded the tribunal that there is no statutory definition of what is a “reasonable excuse” but referred to Section 70 VATA which states that when considering an appeal, a tribunal is not entitled to take into account, amongst others, “the insufficiency of funds available to any person for paying any VAT due or for paying the amount of the penalty”. HMRC furthermore referred to Section 71(1) VATA which states that “(a) an insufficiency of funds to pay any VAT due is not a reasonable excuse; and (b) where reliance is placed on any other person to perform any task, neither the fact of that reliance nor any dilatoriness or inaccuracy on the part of the person relied upon is a reasonable excuse.”

26. HMRC distinguish the *Ripon* case from the circumstances with BMS because in *Ripon* although a lack of funds was accepted as a reasonable excuse, the taxpayer had made an attempt to arrange with HMRC a Time to Pay arrangement, were in regular contact with HMRC, had a genuine belief that the Time to Pay arrangement would be forthcoming and that there was an unexpected reduction in their banking facilities. HMRC say that there is no evidence that BMS attempted a Time to Pay agreement, that there was no arrangement in place and no unexpected reduction in BMS’s bank facilities.

27. HMRC referred the tribunal to the *Trinity Mirror* case as authority that the default surcharge regime as a whole was not inherently disproportionate and stated that this judgement is binding on this tribunal.

28. HMRC referred the tribunal to the *Clean Car Company Limited*, a 1991 VAT and Duties tribunal decision, where the tribunal chairman stated “it has been said before in cases arising from default surcharge is that the test of whether or not there is a reasonable excuse is an objective one..... One must ask oneself: was what the taxpayer did a reasonable thing for a reasonable trader conscious of and intending to comply with his obligations regarding tax, but having the experience and other relevant attributes of the taxpayer and placed in the situation that the taxpayer found himself at the relevant time, a reasonable thing to do?...It seems to me that Parliament in passing this legislation must have intended that the question of whether a particular trader had a reasonable excuse should be judged by the standards of reasonableness which one would expect to be exhibited by a taxpayer who had a responsible attitude to his duties as a taxpayer, but who in other respects shared such attributes of the particular appellant as the tribunal considered relevant to the situation being considered”.

29. HMRC referred to *Garnmoss Limited T/A Parham Builders* and to Judge Hellier’s statement: “What is clear is that there was a muddle and a *bona fide* mistake was made. We all make mistakes. This was not a blameworthy one. But the Act does not

provide shelter for the mistakes, only for reasonable excuses. We cannot say that this confusion was a reasonable excuse. Thus this default cannot be ignored under the provisions of subsection (7)”. HMRC also referred to *Award Farmers International Limited* where the tribunal accepted a mistake as a reasonable excuse on the grounds of the taxpayer’s age and failing memory.

Decision

30. The tribunal had sympathy with the position that BMS found itself in, particularly in relation to the payment due on 7 October 2015, when they had been awaiting receipt of £240,800 for several weeks previously.
- 10 31. There were clearly a number of factors which resulted in the payment not being made, including the confusion between Margaret Sharp and Toni Brown as to whether or not a Time to Pay communication had been made with HMRC; the concerns clearly stated by Douglas Pearson that Toni would have been very concerned at the cash flow position on 7 October 2015 prior to the payment of £248,000 which had
15 been expected several weeks before, and the consequences that might have had for the company’s relationships with its bankers; and the administrative error that the payment was simply not made whatever the consequences for the relationship with the company’s bankers.
- 20 32. The tribunal is required to consider the issue of reasonable excuse within the terms of the law and, in itself, insufficiency of funds to pay any VAT is not a reasonable excuse. The underlying cause of any insufficiency of funds, if entirely unforeseen and outside the control of the taxpayer, may constitute a reasonable excuse, as stated in the *Customs & Excise Commissioners v Steptoe* case.
- 25 33. In this case, the likelihood of there being an insufficiency of funds when a VAT payment was due to be made, had occurred on at least two previous occasions for the same reasons and so could not, in any objective sense, be regarded as an unforeseen reason or occurrence by the time the 08/15 payment was due.
- 30 34. The issue of the failure to receive the £248,000, whilst unfortunate, was foreseeable, as it arose several weeks before the VAT payment was due and it is the tribunal’s view that, applying the test laid down of a reasonable trader conscious of and intending to comply with his obligations regarding tax, BMS could have taken steps during that period of time to consider other sources of finance for meeting the payment or, if that were unrealistic, contacting HMRC concerning a Time to Pay arrangement.
- 35 35. The tribunal noted the exemplary behaviour of BMS when Margaret Sharp realised that the payment had not been made and that she did so immediately thereafter, when BMS also had the funds to be able to do so.
36. For the above reasons, the tribunal are unable to consider that BMS has shown a reasonable excuse for the late payment and must therefore dismiss the appeal.

37. 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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**W RUTHVEN GEMMELL WS
TRIBUNAL JUDGE**

RELEASE DATE: 2 MARCH 2016

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Appendix 1

Legislation

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Sections 59, 59A, 70 and 71 Value Added Tax Act 1994
Regulations 25 and 40 Value Added Tax Regulations 1995
Section 108 Finance Act 2009

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Appendix 2

Cases Referred To

Trinity Mirror plc v Revenue and Customs Commissioners [2015] UKUT 421
30 *The Clean Car Company* [1991] Tribunal Decision number 5695
Garnmoss Ltd T/A Parham Builders v HMRC [2012] TC 02001
Award Framers International Limited v HMRC [2014] TC 03365
Ripon Farm Services v HMRC [2015] TC 04829