[2017] UKFTT 0414 (TC)

TC05878

Appeal number: TC/2017/00103

Value Added Tax – default surcharge – assessment subsequent to filing of return and payment of tax – whether power to assess at that time – whether computer-generated notice amounts to assessment – Value Added Tax Act 1994, ss 59, 76

FIRST-TIER TRIBUNAL
TAX CHAMBER

DENTECH DENTAL (MATERIALS AND EQUIPMENT) LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE NICHOLAS PAINES QC
KAMAL HOSSAIN FCA FCIB

Sitting in public at Fox Court, 30 Brooke Street, London EC1 on 5 May 2017

Anthony Woon-Sam, Crown Accountants, for the Appellant

Mohammed Uddin, Appeals and Reviews Unit, HM Revenue and Customs, for the Respondents

DECISION

1. This is an appeal against a default surcharge imposed on the taxpayer company ("Dentech") by a computer-generated notice of assessment of surcharge issued by HMRC on 16 September 2016 in the sum of £877.55.

The facts

2. The primary facts were common ground between the parties. Dentech's VAT return and payment of tax for period 10 15, due on 7 December 2015, were sent late. Accordingly, HMRC served a VAT surcharge liability notice under section 59(2) of the Value Added Tax Act 1994. Dentech filed its VAT return for period 01 16 on time, but the payment of the tax due was late. HMRC sent a surcharge liability extension notice but, in accordance with their published policy, did not impose a surcharge as the amount of surcharge involved was less than £400.

3. In respect of period 07 16 the return was again filed on time (on 6 September 2016) but the payment of the tax due was late, being paid in instalments on 13 September and 3 October. Meanwhile, on 16 September, HMRC had sent the disputed notice of assessment, as well as further extending the taxpayer's surcharge liability period. The surcharge was calculated at 5% of the tax due for period 07 16, the rate applicable to a second default within a surcharge liability period.

The law

4. Default surcharges are governed by section 59 of the VAT Act and the assessment of them, along with penalties and interest under other legislative provisions, are governed by section 76. Section 59 provides, so far as material:

> (1) … if, by the last day on which a taxable person is required in accordance with regulations under this Act to furnish a return for a prescribed accounting period—
>
> (a) the Commissioners have not received that return, or
> (b) the Commissioners have received that return but have not received the amount of VAT shown on the return as payable by him in respect of that period,
>
> then that person shall be regarded for the purposes of this section as being in default in respect of that period.
>
> …..
>
> (4) Subject to subsections (7) to (10) below, if a taxable person on whom a surcharge liability notice has been served—

(a) is in default in respect of a prescribed accounting period ending within the surcharge period specified in (or extended by) that notice, and
(b) has outstanding VAT for that prescribed accounting period,

he shall be liable to a surcharge equal to whichever is the greater of the following, namely, the specified percentage of his outstanding VAT for that prescribed accounting period and £30.

5. Subsection (5) provides that the specified percentage is 2% of the outstanding VAT for a first default in a surcharge period, 5% for a second default, 10% for a third and 15% thereafter. Subsection (6) then provides

(6) For the purposes of subsections (4) and (5) above a person has outstanding VAT for a prescribed accounting period if some or all of the VAT for which he is liable in respect of that period has not been paid by the last day on which he is required (as mentioned in subsection (1) above) to make a return for that period; and the reference in subsection (4) above to a person's outstanding VAT for a prescribed accounting period is to so much of the VAT for which he is so liable as has not been paid by that day.

6. Subsection (7) provides that a person shall not be treated as in default or liable for a surcharge if

he satisfies the Commissioners or, on appeal, a tribunal that, in the case of a default which is material to the surcharge

(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

(b) there is a reasonable excuse for the return or VAT not having been so despatched.

7. We shall refer to all of this as “reasonable excuse”.

8. Section 76(1) provides

(1) Where any person is liable—

(a) to a surcharge under section 59, section 59A, paragraph 16F of Schedule 3B or paragraph 26 of Schedule 3BA, or
(b) to a penalty under any of sections 60 to 69B , or
(c) for interest under section 74, or
(d) a penalty under regulations made under section 135 of the Finance Act 2002 (mandatory electronic filing of returns) in connection with VAT,

the Commissioners may, subject to subsection (2) below, assess the amount due by way of penalty, interest or surcharge, as the case may be, and notify it to him accordingly; and the fact that any conduct giving rise to a penalty under any of sections 60 to 69B or the regulations may have ceased before an assessment is made under this section shall not affect the power of the Commissioners to make such an assessment.

9. Section 76 goes on to provide in section 76(3)(a) that in the case of a surcharge under section 59 the assessment is to be of an amount due in respect of the prescribed accounting period in respect of which the taxpayer "is" in default.

The issues

10. The issues in the appeal concern the interpretation of sections 59 and 76, together with a further issue concerning section 84(3), which we explain below. For Dentech, Mr Woon-Sam maintained that the assessment of 16 September 2016 was bad in law for three reasons:

(1) It had been automatically generated by a computer, whereas the concept of an assessment required that a person acting on behalf of HMRC should decide whether to make an assessment in Dentech's case and, if so, how much of the maximum liability under section 59 to assess for. This interpretation of section 76 was said to be supported by section 83(q), which creates a right of appeal in respect of the amount of a surcharge assessed under section 76 and section 84(6), which confines the tribunal's power on an appeal to reducing an assessment to "the amount which is appropriate" under section 59.

(2) Dentech were not liable to a surcharge as of 16 September, the date of the purported assessment, so no assessment could lawfully be raised.

(3) By virtue of section 84(3) of the Act, HMRC could not assess a surcharge unless they had determined (i.e. assessed under section 73) the amount of VAT payable by Dentech in respect of the accounting period in question; they had not done this.

11. The first two of these grounds of challenge repeat submissions that Mr Woon-Sam made on behalf of another taxpayer in *Loftus Engineering Services v HMRC* (TC/2015/04188). As in that case, the second issue that Mr Woon-Sam raises does not arise on the facts; in both the *Loftus* case and this case the tax had not been paid (or fully paid) as at the date the assessment was issued. We nevertheless deal with the point of law, which was fully debated. We do not consider any of the grounds to be well founded in law.

(1) Computer-generated assessment

12. We observe that (unlike some assessments to be made by HMRC under the Act, notably assessments to "the best of their judgment") an assessment of a surcharge under section 59 is a purely mathematical exercise, consisting in multiplying the

outstanding VAT by the appropriate percentage specified in section 59(5). HMRC did not need to assess the outstanding VAT, since Dentech had filed a timely return. Albeit that the legislation under consideration was different, the decision of the Court of Appeal in *Donaldson v HMRC* [2016] EWCA Civ 761 fortifies us in our conclusion that the computer-generated notice of assessment in the present case was an assessment that complied with section 76(1).

13. *Donaldson* concerned paragraph 4 of schedule 55 to the Finance Act 2009, which makes a taxpayer liable to a penalty of £10 per day for late filing of an income tax return if HMRC decide that a penalty should be payable, in which case they must assess the penalty (paragraph 18). One of the issues in the *Donaldson* case was similar to the issue before us; it arose out of the fact in that HMRC had not given individual consideration to Mr Donaldson's case but had decided in principle, before Mr Donaldson's default occurred, that the penalty should be imposed on all taxpayers liable for it; a computer had been programmed to issue penalty assessments in accordance with that decision. It was argued that that did not satisfy the requirement for a decision, which meant an individual decision in each defaulting taxpayer's case.

14. The express requirement for both a decision and an assessment was a feature of schedule 55 that is not present in the provisions we are considering. We should add that it was not separately argued in *Donaldson* that the additional requirement for an assessment imported a duty to give individual consideration to taxpayers' cases.

15. The Court of Appeal (paragraphs 14 and 15 of the judgment) agreed with the Upper Tribunal that the legislation did not contemplate a decision in respect of each potentially liable taxpayer, given that it would be impractical to exercise a discretion in respect of taxpayers individually; it contemplated an advance decision that all eligible taxpayers should suffer the penalty. The court was fortified in this conclusion by the provision in paragraph 23 of the schedule for the taxpayer to avoid liability by satisfying HMRC or the tribunal on appeal that there was a reasonable excuse for the default.

16. We consider that the requirement for an assessment under section 76 of the VAT Act is likewise satisfied by HMRC programming a computer to perform the purely mathematical task of calculating a surcharge under section 59. We accept that section 76 gives HMRC a discretion to assess or not (which they have exercised by deciding not to assess surcharges of less than £400); but we do not consider that it imports a requirement to decide on an individual basis whether to assess or not; nor do we consider that it imports a requirement (and we doubt that it even gives a power) to assess an individually determined amount less than the amount produced by the statutory calculation. We so conclude for the same reasons as the Court of Appeal gave in *Donaldson.*

17. First, to do these things would be impractical; not only would it involve time-consuming investigations, but there are no obvious criteria by which to decide whether or how much to assess in any individual case. Secondly, Parliament has made provision for extenuating circumstances by giving the taxpayer an opportunity to show a reasonable excuse under section 76(7). The placing of the onus of raising

that issue upon the taxpayer is inconsistent with there being any duty of HMRC to consider issues of mitigation or excuse of their own motion as part of the assessment exercise.

18. We do not consider that sections 83(q) and 84(6) support Mr Woon-Sam's argument; section 83(q) simply creates the right of appeal and section 84(6) confines the tribunal's powers to reducing a surcharge to the amount which is "appropriate under" section 59. This must refer to the amount produced by the calculation mandated by section 59(5), and undermines any suggestion that the legislation gives any power to fix some different amount.

(2) Whether liability for a surcharge ceases upon late filing of a return or payment of VAT

19. Mr Woon-Sam's starting point – entirely logically – was section 76(1). It gives power to assess "where a person is liable"; Mr Woon-Sam stressed the use of the present tense. We agree with him that, in order for HMRC to be able to assess Dentech to a surcharge on 16 September, it had to be possible on that date to state accurately that "Dentech is liable for a surcharge". Next Mr Woon-Sam took us – again entirely logically – to section 59(4). That makes a taxpayer liable for a surcharge if he "is in default" and "has outstanding VAT". Again Mr Woon-Sam stressed the use of the present tense. Mr Woon-Sam's argument is that it cannot be said that a taxpayer "is" in default" and "has" outstanding VAT on a date if he has filed the return and paid the VAT by that date, even if belatedly.

20. The reason why Mr Woon-Sam's argument breaks down, in our view, is that the concepts of "is in default" and "has outstanding VAT" are defined elsewhere in section 59. Subsections (1) and (6), which we have set out above, respectively provide (a) that a person is to be regarded for the purposes of section 59 as being in default if on the last day for filing or payment HMRC have not received the return or have received the return but not the VAT and (b) that a person has outstanding VAT for the purposes of subsections (4) and (5) if some or all of the VAT has not been paid by the last day for payment.

21. In the present case the last day for filing and payment was 7 September 2016; on that date HMRC had received the return but not the VAT. A person considering Dentech's liability position as of 16 September would have been required (a) to treat Dentech as being in default by virtue of section 59(1)(b) and (b) to conclude under section 59(4) that Dentech had outstanding VAT of the amount that should have been, but was not, paid by 7 September. That is so despite the fact that some of the VAT had by then been paid belatedly on 13 September and would have been so even if all the VAT had been paid belatedly before 16 September. Put simply, a situation of being in default and having outstanding VAT is created by not filing and/or paying by the due date; once created, it is irreversible.

22. Mr Woon-Sam argued that section 59 is concerned with non-payment, not with late payment. But we do not find that to be a meaningful or workable distinction. All that HMRC can know is that a due date has passed without filing and/or payment

having taken place. They cannot know whether a taxpayer is about to file and/or pay belatedly.

23. Mr Woon-Sam also drew our attention to the final clause (following the semi-colon) in section 76(1). He said that the draftsman had provided expressly in the case of penalties that cessation of the conduct giving rise to a penalty did not affect HMRC's power to assess a penalty; the draftsman had refrained from providing in the case of surcharges that cessation of the default did not affect the power to assess a surcharge; accordingly cessation of the default did remove the power.

24. The difficulty with this argument is that the draftsman did not need to provide that the power to assess a surcharge was unaffected in these circumstances. That is because he had defined being in default and having outstanding VAT in section 59(1) and (6) in a manner which already led to the result that the power to assess a surcharge was unaffected by belated filing or payment. In *Loftus Engineering* (where, as here, the point did not actually arise on the facts) the tribunal found it likely "that the thinking behind this legislation is that section 59 defaults are excluded from this qualification precisely because by their nature they are concluded events: either the return has been submitted, and the tax paid on time, or not; whether these obligations are complied with six days later, or six months later, or not at all, can be said to be irrelevant to liability under section 59". For the reasons we have given, we share this interpretation.

25. The tribunal went on to acknowledge that sections 59(4) and 76(3)(a) could have been drafted in the past tense and that "some of the sections covered by the proviso in section 76(1) refer likewise to concluded events". Mr Woon-Sam described this as puzzling, as it appeared to undermine the tribunal's earlier conclusion. In our view, while sections 59(4) and 76(3)(a) could have been drafted in the past tense, the effect of the language in fact used is clear; the final clause of section 76(1) simply did not need to refer to section 59(1) in order to produce the result that HMRC contend for.

26. We consider that the purpose of the inclusion of the final clause in section 76(1) was to exclude any argument in penalty cases that a penalty could not be assessed if, by the time of the assessment, the punishable state of affairs had been rectified. Section 60, for example, enables a penalty to be imposed where a person dishonestly "does" or "omits" an action for the purpose of evading VAT; section 62 enables a penalty to be imposed where a person "gives" or "prepares" an incorrect certificate of certain types. Where a taxpayer had repented and had corrected a dishonest statement, or discovered and corrected an inaccuracy in a certificate, before a penalty was imposed, it might have been argued that the penalty could no longer be imposed on the grounds that liability only exists while the taxpayer "is" doing the punishable things. Parliament wished to exclude such an argument.

27. It does not seem to us to be fruitful to examine whether the clause was indeed necessary in respect of any or all of the penalty provisions; the clause was in our view included in order to remove any room for argument. The effect of the various subsections of section 59 is clear beyond argument and the non-inclusion of section 59 in the final clause of section 76(1) is not sufficient to reverse that effect.

(3) The absence of an assessment of the VAT

28. Section 84(3) apples to appeals under, *inter alia*, section 83(q). It prevents an appeal where "the amount which the Commissioners have determined to be payable as VAT" has not been paid or deposited, except in cases of hardship. We cannot accept that the section has any impact at all on HMRC's ability to assess a surcharge; it regulates only the ability of a taxpayer to appeal once an assessment has been made.

29. For all the above reasons we dismiss this appeal.

30. 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.

NICHOLAS PAINES QC
TRIBUNAL JUDGE

RELEASE DATE: 15 May 2017