TC01296

Appeal number TC/2011/01464

VAT surcharge. Onus of Proof. Jusilla v Finland. Article 6 ECHR.

FIRST-TIER TRIBUNAL

TAX

MASS INFORMATION SYSTEMS LIMITED **Appellant**

- and -

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

TRIBUNAL: GERAINT JONES Q.C.
MR MARK BUFFERY

Sitting in public at The County Court, Reading on 22 June 2011.

Mr. Bolt (Company Chairman) for the Appellant

Mr. Braeger, for the Respondents

DECISION

Introduction.

1. The appellant, Mass Information Systems Ltd, appeals to this Tribunal against surcharges imposed against it by HMRC in respect of the late submission of VAT returns and/or the late payment of VAT due for payment in respect of its VAT quarters ended 31 December 2008, 31 March 2009, 30 June 2009, 30 September 2009, 31 January 2010 and 31 July 2010.

2. If surcharges are to be imposed the surcharge regime requires that appropriate Surcharge Notices are served by HMRC upon the taxpayer said to be in default. In that way, if the taxpayer disputes that there has been the alleged default, it is on notice of the default allegation and can take steps to dispute it, if so advised. The Surcharge Notices are also important because the default regime works on a ratchet effect with a surcharge being levied at a higher percentage of the VAT due if a taxpayer's default record is persistent. At the time relevant to this appeal the ratchet effect was to take the surcharge from its initial 2%, then to 5%, then to 10% and then to 15% of the VAT due.

3. The surcharge regime is conditional upon the appropriate Surcharge Notices having been properly served.

The Burden of Proof.

4. Before we turn to the facts of this appeal and to our conclusions in respect of it, it is appropriate that we set out the law as we now perceive it to be. In G. Deacon & Sons v Commissioners of Inland Revenue 33TC 66 Mr Justice Donovan dismissed a request for a case to be stated in respect of conclusions drawn by General Commissioners, holding that from the primary facts adduced in evidence, they were entitled to draw the inferences that they drew against the then appellant, Mr Deacon.

5. In Johnson v Scott (1987) STC 476 Mr Justice Walton expressly considered where the onus of proof lay in a case where an appellant was challenging amended assessments that had been upheld by the Commissioners. He observed that counsel for the Crown had correctly accepted that where, as in that case, neglect on the part of the taxpayer had to be established, the onus of establishing such neglect lay with the Crown. He went on to hold that if a finding of neglect is made, and justified on the evidence, that enabled the Crown to make assessments for the purpose of making good any tax lost as a result of such neglect. He went on to observe that if that stage was reached, then the onus would pass to the taxpayer to adduce evidence to show that the assessment is too large.

6. His Lordship desisted from indicating whether the onus that then shifted to the taxpayer was a legal burden or an evidential burden, but usually a reference to a party then having a burden to adduce evidence, refers to an evidential rather than a legal burden. It is also relevant to observe that in that case the learned judge was considering section 50(6) of the Taxes Management Act 1970 in its original, unamended, form. The learned judge also emphasised that where the Crown's case

was based upon inferences drawn from primary facts, such inferences had to be "fair" inferences. One would not have expected otherwise. The Court of Appeal upheld that judgment. It was a case in which the taxpayer failed, by adducing acceptable or probative evidence, to discharge the evidential burden upon him of showing that the inferences drawn by the Crown were not fair or appropriate.

7. I set out the foregoing because it is often, incorrectly, stated that once an assessment is raised or a surcharge demanded, the burden of proving that it is incorrect rests upon the taxpayer. That may be an approximation of the de facto position in respect of an assessment (but not a surcharge) but it fails to analyse the true legal position.

8. In our judgment the true legal position now has to be considered bearing in mind the amendments to section 50 of the Taxes Management Act 1970, the most recent having come into effect from the 1st April 2009, but more importantly having in mind the decision of the European Court in the **Jussila v Finland (2009) STC 29** where, in the context of default penalties and surcharges being levied against a taxpayer, the Court determined that Article 6 of the European Convention on Human Rights was applicable, as such penalties and surcharges, despite being regarded by the Finnish authorities as civil penalties, nonetheless amounted to criminal penalties despite them being levied without the involvement of a criminal court. At paragraph 31 of its judgment the court said that if the default or offence renders a person liable to a penalty which by its nature and degree of severity belongs in the general criminal sphere, article 6 ECHR is engaged. It went on to say that the relative lack of seriousness of the penalty would not divest an offence of it inherently criminal character. It specifically pointed out, at paragraph 36 in the judgment, that a tax surcharge or penalty does not fall outside article 6 ECHR.

9. This is a case involving surcharges which are in the nature of penalties. The European Court has recognised that in certain circumstances a reversal of the burden of proof may be compatible with Article 6 ECHR, but did not go on to deal with the issue of whether a reversal of the burden of proof is compatible in a case involving penalties or surcharges. This is important because a penalty or surcharge can only be levied if there has been a relevant default. If it is for HMRC to prove that a penalty or surcharge is justified, then it follows that it must first prove the relevant default, which is the trigger for any such penalty or surcharge to be levied.

10. In our judgement there can be no good reason for there to be a reverse burden of proof in a surcharge or penalty case. A surcharge or penalty is normally levied where a specified default has taken place. The default might be the failure to file a document or category of documents or it may be a failure to pay a sum of money. In such circumstances there is no good reason why the normal position should not prevail, that is, that the person alleging the default should bear the onus of proving the allegation made. In such a case HMRC would have to prove facts within its own knowledge; not facts peculiarly within the knowledge of the taxpayer.

The Evidence.

11. Mrs Knight gave evidence on behalf of the appellant. Her evidence in chief was given by her adopting her witness statement, in the form of a Solemn Declaration, declared 27 April 2011. Mrs Knight described herself as the appellant's Office Manager and said that she had worked for the company since April 2006. The effect of her evidence was that she is in charge of the day-to-day administrative and office affairs which, she stated, included opening and dealing with all the post, although dealing with it might involve passing it on to some other person, if appropriate.

12. Mrs Knight's evidence is that in May 2010, just before she was due to go on annual leave, she received from HMRC a document headed "Demand Notice For Immediate Payment" dated the 14 May 2010, demanding payment of £20,658.13. She said that her reaction was to telephone HMRC where she spoke to a Mr Knight (a simple coincidence) and she made notes during that telephone conversation. She then referred to further correspondence with HMRC but did not deal with events that have taken place prior to May 2010.

13. During Mrs Knight's oral evidence she was referred to page 12 of the respondent's bundle, being a document headed Surcharge Liability Notice Extension dated the 15 May 2009. She said that she had no recollection of receiving that document and had not seen it until the appeal bundle was received in April 2011. She was adamant that if, when opening the post, she had seen this document she would not have ignored it but would have drawn its contents to the attention of Mr Bolt.

14. The Notice of the 15 May 2009 was sent to the appellant at its Ocean House address. Mrs Knight's evidence is that the company moved from that address on the 04 or 05 May 2009 and that although the company initially put in place a mail forwarding arrangement with the Royal Mail, that soon came to an end because Royal Mail would not operate a mail forwarding service for a business that had operated from serviced offices where several other companies shared the same postcode.

15. Mrs Knight next referred to the document at page 15, being a Notice of Assessment of Tax and Surcharge dated 14 August 2009. That document was also sent to the appellant's old address at Ocean House. Mrs Knight's evidence is that it did not come to her attention. She said that if she had received it *"I would have panicked"*. She was adamant that if it had been received she would not have ignored it but would have referred it to Mr Bolt.

16. Mrs Knight next referred to the document at page 17 in the bundle, headed Advice of Production of Surcharge, dated 21 December 2009. That was also sent to the appellant's Ocean House address. Mrs Knight's evidence is that it was not received or, certainly, not seen by her - the person who opened all the post.

17. Mrs Knight then referred to the document at page 19 in the bundle, being a Value Added Tax Return which contains the appellant's details pre-typed onto the form. That was also sent to the appellant's Ocean House address. Mr Braeger made the point

that that document must have been received because it had been returned, in its original format, to HMRC.

18. We can be certain that that return was sent to HMRC because at page 34 of the bundle appears a letter dated 17 November 2009 (the same date as the VAT return is dated) which is plainly a covering letter that was sent to HMRC with that VAT return.

19. The covering letter of 17 November 2009 says, in its middle paragraph *"Whilst writing I note that our address stated on your records is still Bracknell, we did write when we moved in May 2009 to give our new address."*

20. Mrs Knight then referred to the document at page 20 in the bundle, being a document headed Notice of Assessment of Tax and Surcharge dated 13 November 2009 which was also sent to the old address, Ocean House, Bracknell. Mrs Knight said that this document was not received or, certainly, not seen by her and she was adamant that had it been received by her it would have set alarm bells ringing and she would have acted upon it.

21. Mrs Knight then referred to the document at page 22 in the bundle headed Advice of Production of Surcharge dated 19 November 2009, also sent to the appellant's old address. She said that she had not seen it previously.

22. By reference to the document at page 25 in the bundle, headed Notice of Assessment of Surcharge dated 12 February 2010, Mrs Knight said that that had been addressed to the appellant's new premises at Innovation House. Nonetheless, she said that it had not been received and that had it been received or opened by her she would most certainly have reacted to it.

23. Mrs Knight was cross examined and accepted that the document at page 9 in the bundle, dated 13 February 2009, had been received by her as she had reacted to it and written appealing against the default notice. In our judgement Mrs Knight's reaction to that letter, which she certainly received, is what one might have expected had she received the other documents which, as set out above, she has said she did not receive.

24. By reference to the document at page 11 in the bundle, being the VAT Return for the period ended March 2009, she said that it had been received as it had been sent to the Ocean House address prior to the appellant moving from that address.

25. The next witness was Mr Bolt who gave evidence in accordance with his witness statement dated 27 April 2011. He stated that its contents were true and correct. He was insistent that had default notices been received he would most certainly have discussed them with HMRC and dealt with them, rather than ignoring them.

26. It seemed that that was the end of the evidence as Mr Braeger said that he did not intend to call any evidence. We pointed out that given the onus of proof upon the respondent, that might create difficulties for HMRC. Mr Braeger then said that he would like to give evidence which raised the unusual and unsatisfactory situation of an advocate seeking to give evidence. Nonetheless, we permitted it.

27. Mr Braeger gave evidence by reference to page 19 in the bundle and said that the number printed immediately to the right of the address block and at the bottom of it, only ever appears on an original blank VAT return when it is sent to the taxpayer for completion. He explained that it does not appear if a duplicate is issued. That evidence seemed to be borne out by the absence of any such number appearing on the duplicate VAT return which appears at page 14 in the bundle.

28. Mr Braeger said that HMRC had no record of any mail being returned but gave no details of the enquiries, if any, that he had made into that matter. In cross examination he simply said that he had *"checked the records"*.

Findings of Fact.

29. We accept the evidence given by Mrs Knight. We accept her as a witness of the truth whose evidence, in our judgement, was given in a measured, fair and careful manner. She was an employee who had certain duties and functions to fulfil, particularly, so far as is relevant to this appeal, by reference to dealing with incoming post. We consider it to be almost inconceivable that if Mrs Knight had received the various Notices which she said, in terms, she had not received or seen, she would not have acted upon them just as she reacted to the Notice of 13 February 2009 (page 9) that she accepts she received. She reacted to that letter by writing to HMRC on 24 February 2009 (page 31). We consider it quite unrealistic to think that Mrs Knight would not have done something similar had she received later Notices demanding far greater sums of money than that demanded by the Notice of 13 February 2009. It makes absolutely no sense that she should have ignored those later Notices, if received. Indeed, that would have been a gross dereliction of duty.

30. We have already referred to the middle paragraph of Mrs Knight's letter of 17 November 2009 where she stated that a letter had been sent to HMRC in May 2009 giving the appellant's new address. We do not consider that Mrs Knight would have made that statement if it had not been true. During her oral evidence she was certain that such notification had been sent to HMRC, in writing, although we observe that no file copy of the appropriate letter was produced to us. Nonetheless, we believed and accepted that evidence.

31. We find as a fact that the various Notices that Mrs Knight said were not received by the appellant, were not received by it.

32. We accept the evidence given by Mr Braeger that only an original VAT return has a number shown at the bottom of the address box. We also accept his evidence that his enquiries have not revealed any mail that ought to have been delivered to the appellant, being returned to HMRC. We can go no further than that as he gave no details of the nature and extent of any enquiries undertaken.

Conclusions.

33. Given our above findings of fact it must follow that because the various Notices, which are a pre-condition or trigger for the surcharge amounts being demanded, those surcharges or penalties cannot stand. However, that does not apply to the surcharge of

£1,288.31p in respect of the VAT quarter ended 31 December 2008 in respect whereof we are satisfied, on the balance of probabilities, that the appropriate Surcharge Notice was received given that Mrs Knight responded to it.

34. This appeal was also to proceed on the basis of a "reasonable excuse" argument. In respect of the surcharges that we have set aside we need not consider that further argument. In respect of the surcharge that we uphold we do not consider that the reasonable excuse argument has any merit.

DECISION.

35. The appellant's appeal is allowed in part.

36. The surcharge sums are set aside in respect of the VAT quarters ended 30 June 2009, 30 September 2009, 31 January 2010 and 31 July 2010. The surcharge sum of £1288.31p in respect of the VAT quarter ended 31 December 2008, is upheld.

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.

GERAINT JONES QC.

TRIBUNAL JUDGE

RELEASE DATE: 5 JULY 2011