[2013] UKFTT 128 (TC)

TC02557

Appeal number: TC/2012/04841

INCOME TAX – Penalty for late payment of PAYE – whether cashflow difficulties constituted a reasonable excuse – whether the company had a time to pay arrangement - whether the company's belief that informing HMRC of their payment plans was sufficient to provide a reasonable excuse – whether there were special circumstances – whether the penalty was disproportionate – appeal dismissed and penalty confirmed

FIRST-TIER TRIBUNAL
TAX CHAMBER

AQUATINT BSC LIMITED **Appellant**

- and -

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

TRIBUNAL: ANNE REDSTON
(TRIBUNAL PRESIDING MEMBER)
TOBY SIMON

Sitting in public at 45, Bedford Square, London on 30 January 2013

Rob Primarolo and Roger Severn, directors of the Appellant, for the Appellant

Karen Weare, of HM Revenue & Customs Appeals and Reviews Unit, for the Respondents

DECISION

1. This was the appeal by Aquatint Limited ("the company") against a penalty of £5,489.16 for late payment of monthly PAYE and employees' National Insurance Contributions[1] during the year to 5 April 2011.

2. The Tribunal dismissed the appeal and confirmed the penalty.

This appeal

3. The appeal had previously been listed before a tribunal consisting of Judge Demack and Ms Helen Folorunso on 3 October 2012 who adjourned the case *sine die*.

4. The appeal was relisted before this tribunal. We were provided with a bundle of documents. An email in the bundle stated that the company had been directed to provide further evidence about its cashflow during the year in question.

5. Shortly before the commencement of the hearing, Mrs Weare provided us with a one page note which indicated that some evidence had been taken at the October hearing, and thus that it had been adjourned part-heard.

6. We asked both parties if they would prefer the hearing to be adjourned and relisted before the original tribunal, or whether they wanted to go ahead with this hearing, which would require that we start again from the beginning. The parties took time for consideration before requesting a new hearing before us.

7. We then considered the position under the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009, and in particular Rule 2. We decided that it was in the interests of justice to consent to the parties' request that we hear the case *de novo* rather than remitting it back to the original tribunal with directions. In so doing we took into account in particular the need to avoid delay, so far as consistent with proper consideration of the issues.

The issues in the case

8. The issues in the case were:

   (1) whether the company's cashflow difficulties provided a reasonable excuse for the late payments;

   (2) whether the company had a time to pay ("TTP") agreement with HMRC for one or more of the months for which a penalty has been charged, and if not,

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[1] For brevity, this decision refers to monthly PAYE payments, but should be read as referring also to payments of monthly NICs.

whether the company's communications with HMRC relating to delays in payment provided it with a reasonable excuse;

(3) whether there were any special circumstances;

(4) whether the penalty was disproportionate to the default.

The legislation

9. The relevant legislation is at Finance Act 2009, Schedule 56. The penalty amounts are set out at para 6, as follows:

(1) if payments are late for one month in a tax year, there is no penalty;

(2) if two to four months' payments are late, the penalty is 1% of the total PAYE for the tax year;

(3) if five to seven months' payments are late, the penalty rises to 2%;

(4) if eight to ten months' payments are late, the penalty rises further to 3%;

(5) if eleven or twelve months' payments are late, the penalty is 4%.

10. However, following the case of *Agar v R&C Commrs* [2011] UKFTT 773 (TC) HMRC have accepted that the legislation does not allow a penalty to be charged for a late payment of Month 12's PAYE.

11. FA 2009, Sch 56, para 9 allows the penalty to be reduced because of 'special circumstances':

> (1) If HMRC think it right because of special circumstances, they may reduce a penalty under any paragraph of this Schedule.
>
> (2) In sub-paragraph (1) "special circumstances" does not include—
>
> (a) ability to pay…

12. FA 2009, Sch 56, para 10 provides that a penalty is suspended "during currency of agreement for deferred payment". It reads as follows (where "P" stands for "a person"):

> (1) This paragraph applies if—
>
> (a) P fails to pay an amount of tax when it becomes due and payable,
>
> (b) P makes a request to HMRC that payment of the amount of tax be deferred, and
>
> (c) HMRC agrees that payment of that amount may be deferred for a period ("the deferral period").
>
> (2) If P would (apart from this sub-paragraph) become liable, between the date on which P makes the request and the end of the deferral period, to a penalty under any paragraph of this Schedule for failing to pay that amount, P is not liable to that penalty.
>
> (3) But if—

(a) P breaks the agreement (see sub-paragraph (4)), and

(b) HMRC serves on P a notice specifying any penalty to which P would become liable apart from sub-paragraph (2),

P becomes liable, at the date of the notice, to that penalty.

(4) P breaks an agreement if—

(a) P fails to pay the amount of tax in question when the deferral period ends, or

(b) the deferral is subject to P complying with a condition (including a condition that part of the amount be paid during the deferral period) and P fails to comply with it.

(5) If the agreement mentioned in sub-paragraph (1)(c) is varied at any time by a further agreement between P and HMRC, this paragraph applies from that time to the agreement as varied.

13. FA 2009, Sch 56, para 16 sets out the "reasonable excuse" provisions:

(1) Liability to a penalty under any paragraph of this Schedule does not arise in relation to a failure to make a payment if P satisfies HMRC or (on appeal) the First-tier Tribunal or Upper Tribunal that there is a reasonable excuse for the failure.

(2) For the purposes of sub-paragraph (1)—

(a) an insufficiency of funds is not a reasonable excuse unless attributable to events outside P's control,

(b) where P relies on any other person to do anything, that is not a reasonable excuse unless P took reasonable care to avoid the failure, and

(c) where P had a reasonable excuse for the failure but the excuse has ceased, P is to be treated as having continued to have the excuse if the failure is remedied without unreasonable delay after the excuse ceased.

14. FA 2009, Sch 56, para 11 reads:

(1) Where P is liable for a penalty under any paragraph of this Schedule, HMRC must—

(a) assess the penalty,

(b) notify P, and

(c) state in the notice the period in respect of which the penalty is assessed.

15. FA 2009, Sch 56 sets out the Tribunal's powers on appeal:

(1) On an appeal under paragraph 13(1) that is notified to the tribunal, the tribunal may affirm or cancel HMRC's decision.

(2) On an appeal under paragraph 13(2) that is notified to the tribunal, the tribunal may—

(a) affirm HMRC's decision, or

(b) substitute for HMRC's decision another decision that HMRC had power to make.

(3) If the tribunal substitutes its decision for HMRC's, the tribunal may rely on paragraph 9—

(a) to the same extent as HMRC (which may mean applying the same percentage reduction as HMRC to a different starting point), or

(b) to a different extent, but only if the tribunal thinks that HMRC's decision in respect of the application of paragraph 9 was flawed.

(4) In sub-paragraph (3)(b) "flawed" means flawed when considered in the light of the principles applicable in proceedings for judicial review.

The evidence

16. The Tribunal was provided with:

(1) the correspondence between the parties;

(2) a summary of the company's monthly PAYE payment history for the years 2009-10, 2010-11 and 2011-12;

(3) HMRC's computer records showing the dates on which the company paid its PAYE in 2011-12, the issue of the penalty warning letter and details of agent and company addresses;

(4) screenprints from HMRC's "Action History" for the company;

(5) extracts from the company's bank account and a letter dated 10 October 2012 from the company's bankers;

(6) extracts from the company's management accounts and from its aged debtors analysis;

(7) a copy of the company's statutory accounts for the year to 31 December 2010.

17. In addition, Mr Primarolo and Mr Severn gave oral evidence and were cross-examined by Mrs Weare.

The facts

18. Based on the evidence provided, we found the following facts.

The PAYE payments

19. The company's monthly PAYE bill was around £25,000.

20. The company was late paying its PAYE for Months 1-9. HMRC accepted, during the company's statutory review, that a TTP agreement had been agreed for Month 5 and removed it from the penalty calculation.

21. The shortest period for which payments were late was 41 days, the longest was 117 days.

22. The due date for payment of the company's PAYE was 19th of the following month, as all payments were made by cheque.

The company's business

23. The company was trading well until the recession hit during 2008. The company made a profit of £60,666 in the year to 31 December 2009 but in the following year the trading result was a loss of £88,216. Turnover reduced from £2.9m in 2009 to £2.7m in 2010.

24. The company had a net asset value at 31 December 2010 of almost £500,000, largely represented by fixed assets. Cash at bank and in hand was £1,249.

25. In June 2010 the company was transferred by its bank to a "specialist relationship manager". The letter from the bank stated that this transfer was because of "declining turnover, unprojected negative cashflow trends and creditor pressure".

26. The company asked the bank for an extension to its overdraft but was refused. It also tried to borrow money from other banks but because of the recession and reining in of bank lending, none would agree.

27. The company had a contractual obligation to pay £10,800 a month for its printing press. It asked its lender for a payment holiday, but the request was refused.

28. Bank statements were provided to the Tribunal for the company's current account covering the period 24 August to 13 September 2010. These showed that the account became overdrawn from time to time but that transfers were then made into the account. These were from a second account which held the proceeds from its invoice discounting facility. The current account also shows that a number of cheques were written during this period.

29. Two of the company's biggest customers, "Company C" and "Company P", largely suspended payment during the 2010 calendar year because of their own cashflow difficulties:

> (1) As at 31 May 2010, Company C owed the company £16,515 and Company P owed the company £68,322. Total debtors in that month were £497,072.
>
> (2) By August 2010, debts owed by Company C had reduced to £12,463 and those owed by Company P were £57,417, out of a total of £535,684.

(3) By December 2010, the amount due from Company C had increased again to £58,154, that due from Company P had dropped to £49,241, out of total debtors of £597,649.

30. Four members of staff were made redundant at the end of December 2010 and all salaries were cut by 10% for the months of July and August 2010.

31. The company had been wholly owned by Mr Severn but the trading difficulties led to the creation of 22 new shares which were sold to a new investor, Mr Hudson. Mr Hudson was appointed a director in August 2010.

32. The directors' loan account balance moved from £17,260 to nil over the year to 31 December 2010. This was the repayment of a loan to the company from Barry Gregory, a director of the company, which he made in 2008.

33. During the year to 31 December 2010, the directors took £169,232 of remuneration compared to £149,477 in the previous year. The Tribunal was told, and accepted, that the increase was to reflect Mr Hudson joining the board. Included in total directors' remuneration was £14,986 of pension contributions, compared to £24,274 the previous year.

34. In the first seven months of the calendar year, the company's management accounts show £3,492 of entertaining and a further £2,148 of staff refreshments.

The cashflow issue

Submissions

35. Mr Primarolo said that:

(1) the payment delays by two major customers had had a serious effect on the company's cashflow, which was "unforeseen and outside of our control"

(2) The position was so severe that Mr Severn, the owner of the business "ended up having to sell part of the company";

(3) The company was forced to use the expensive invoice discounting facility because it couldn't get cheaper bank loans;

(4) The company had taken steps to cut back on staff costs.

36. Mr Severn said that 100% of the proceeds received from the share sale was invested in the company. In cross-examination by Mrs Weare about recipients of the cheques shown in the bank statements, he said that the company had to pay some creditors such as their paper supplier, or would go out of business.

37. Mrs Weare submitted that the bank statement did not show that the company had an insufficiency of funds which was out of its control, but rather that the company had chosen to pay other creditors before HMRC.

38. She also said that analysis of the debtors showed that this was not a new problem, although she accepted it had become worse during 2010. She said that the company had had time to deal with its cashflow issues before the 2010-11 tax year.

Discussion

39. Our starting point is that for shortage of funds to constitute a reasonable excuse, it must be "attributable to events outside [the company's] control." We thus ask ourselves whether the company's cashflow problems were caused by factors outside its control, or whether the directors could, by making different choices, have found the money to pay their PAYE liabilities on time.

40. The evidence shows that this was a very difficult time for the company. It was making a loss, large debtors were deferring payment, and the bank had put it into a special high risk category. The company took steps to reduce costs, by cutting salaries in July and August and by making staff redundant. It also tried, without success, to raise funds from its bankers.

41. From the evidence we note the following facts:

(1) the company continued to pay its directors almost £150,000pa, including pension contributions of nearly £15,000.

(2) the £17,260 debt due to one of the directors was repaid to him during the year;

(3) while there was a reduction in salaries, this was only for the two months of July and August;

(4) the company continued to spend around £800 a month on entertaining and staff refreshments;

(5) the debt due from Company C had dropped back in August, so some cash must have come in during that period.

42. We were however unable to identify the reinvestment into the company of the monies from the share sale to Mr Hudson, in the accounts for the year to 31 December 2010. We would have expected this to be included as a director's loan. We considered whether to ask for further submissions on this point, but decided against it because the issue was relatively minor and would not change our decision, and it was in the interests of justice not to further extend the time to reach a decision in the case. There had already been one adjournment and one postponement.

43. The onus is on the company to prove its case, and the hearing was adjourned in October 2012 to allow it to produce more evidence. However, only one of two bank accounts was produced, and then for a period of less than a month. No monthly cashflow forecasts were provided. The company was asked by Mrs Weare and by the Tribunal about the cheques which were paid out of the bank account, and what decisions were made as to which creditors to pay, but the replies given (that some creditors needed to be paid to keep the business going) were in the most general terms.

44. Although we found this a difficult decision, in our judgment the company does not meet the threshold required by the legislation. On the facts of the case, there was sufficient money available to pay others, including the directors. We find that the company has not shown the insufficiency of funds to be "attributable to events outside [its] control" and so its cashflow problems cannot constitute a reasonable excuse.

The second issue: whether there was a TTP agreement

The date on which a TTP agreement is made

45. FA 2009, Sch 56, para 10(2) states that a TTP agreement may remove liability to a penalty.

46. However, this provision only eliminates the penalty for the period "between the date on which P makes the request and the end of the deferral period". It follows that an agreement made *after the due date* for payment cannot eliminate the penalty, because the trigger date has already passed and the person has become already liable to the penalty. In the absence of a reasonable excuse or special circumstances HMRC "must" then assess the penalty (FA 2009, Sch 36, para 11).

Submissions of the parties

47. The issue in dispute turns on what was agreed between the company and HMRC. Mr Primarolo contended that the company was "continually renegotiating its TTP" on a monthly basis. He also said that HMRC's records "don't reflect every conversation" and when asked to particularise said that he had once asked the HMRC officer to "put it on record that I have requested that I will be late every month" and was told "I am not going to put that on the record."

48. Mrs Weare said that although there was frequent contact, requests for deferment had always been made after the due date (with the exception of Month 5, for which HMRC had removed the penalty).

49. In view of the conflicting submissions, and in order to establish the facts, the Tribunal analysed HMRC's contemporaneous "Action History" record in detail, and also considered the other evidence provided in the bundle as well as oral evidence from Mr Primarolo and Mr Severn.

50. We have set out our analysis in the next section of this decision. Extracts from the Action History record are shown in italics, and the key date for each month is shown in bold. Our conclusions from this analysis are summarised in the following section.

Analysis of the transactions

51. On 17 May 2010 Mr Primarolo called requesting "*TTP for PAYE amt of £34,296 which was due on 19/4/2010*". The date makes it clear that the reference is to the previous year's overdue PAYE. Mr Primarolo offered to pay £24,296 by 10 June 2010 and £10,000 by 25 June. The HMRC officer referred the request to another department as it was over £10,000.

52. On 18 May 2010 HMRC called Mr Primarolo. The Action History records that the company had "*cashflow problems and will make full by 25/6/10. He will make payments by cheque. No other HMRC debt. Warned of int. also warned of Dist/ccp if default. I have agreed.*" We find that this statement "I have agreed" referred to the previous year's underpayment and not to the current year, because it naturally follows on from the previous day's conversation; it also refers to 25 June 2010, the same date as in the previous note.

53. On the same day, and probably as part of the same call, the HMRC Action History record says that Mr Primarolo "*said they will be making payments for 10/11 late instead pay due on 19 May it will be made from July 19 and month 2 will be made by 19 of following months. I have not agreed.*"

54. The due date for the **Month 1** payment was 19 May 2010. Payment was not made by the due date, and, based on HMRC's clear statement "I have not agreed", we find as a fact that there was no TTP agreement in place for that month.

55. On 20 May 2010 HMRC agreed a TTP instalment arrangement under which £24,296 would be paid on 10 June, £10,000 "monthly thereafter" with the "expected last payment" on 10 August 2010. A letter of the same date sets out a payment plan for £34,521.26 including interest. On the basis of the figures involved, we find as a fact that this TTP agreement related to the 2009-10 underpayment.

56. On 20 May 2010 Mr Primarolo also told HMRC that he wanted to pay 2010-11 "*1 month differed eg will pay month 1 in June and month 2 in July*". The Action History record says that HMRC "*could not agree*".

57. On 25 May 2010 a further conversation took place about the 2010-11 payments, with Mr Primarolo offering to pay "*by differing one month eg month 1 will be paid in June and June in July and August in Sept.*" HMRC records "*we have not agreed but he was not ready to agree*."

58. On 28 May 2010 a "clerical" note on the file states that "*No TTP agreed for CY*".

59. On 7 June 2010 Mr Primarolo called HMRC to renegotiate the TTP agreement as the company couldn't both pay the arrears and the current year's PAYE. HMRC agreed that "*mnth 1 will be paid now – future mnths on time and £3k to upyt.*" A separate note on the same day records "*tele call from tp inst arrgt agreed over 12 months beg 3006.*" Mrs Weare said that this reference was to 30 June. We find as a fact that this reference to an instalment arrangement is to the adjusted collection of the earlier year's underpayment: payments for "future months" were to be "on time". The call ends with the note "WLAIP" which Mrs Weare informed us means "Warning of Legal Action Interest and Penalties."

60. The due date for **Month 2** was 19 June 2010. No payment was made and we find as a fact that there was no TTP agreement in place.

61. On 8 July 2010 Mr Severn called HMRC and said that £3,000 had been paid, and "*TTP in place and the first instalment has been made. Also req mth 2 which will be made unsure of amt.*" On the same day a file note records "*reminder letter required, debt not included in the ttp current was to be paid on time.*"

62. **Month 3** PAYE was due to be paid by 19 July and **Month 4** by 19 August. we find as a fact that there was no TTP agreement in place by the due date, for either month.

63. On 24 August 2010 HMRC called the company and was told that it was "*running a couple of months behind. Month 3 will not be paid until 19/09/10 and month 4 19/10/10.*" The HMRC record continues "*unable to agree to this.*"

64. On 8 September 2010 HMRC called Mr Primarolo and was told that the Month 3 payment "*had been sent off yesterday with the TTP payment. Couldn't do month 4 for another week. Agreed to months 4/5 being paid by 19/9 or recovery will take place.*"

65. HMRC have accepted this as a TTP agreement for Month 5 and so excluded that month from the calculation of the penalty for that month[2]. Since the Month 5 payment was not in fact made by 19 September 2010 (it was paid on 30 October 2010) the terms of the agreement were not kept by the company. However, it may be that there is further evidence, not provided to the Tribunal, which informed HMRC's decision to remove this month from the penalty calculation. No submissions were made by either party and we have not considered Month 5 further.

66. The due date for **Month 6** was 19 October 2010. Again, there was no TTP agreement.

67. On 25 October HMRC called the company and was told that the Month 6 payment had just been made. Mr Primarolo was "*reminded of payt dates, adv that if does not keep on top of inyear pymt runs risk of TTP being cancelled. WLAP*[3]"

68. The due date for **Month 7** and **Month 8** were 19 November and 19 December 2010. There was no TTP agreement for either month.

69. On 24 December there was a further conversation. Mr Primarolo has provided the Tribunal with his notes of the call. They read as follows:

> "Agreed to put mth 8 (£25,933) into arrears with debt owing from last year (approx £14k) & then I to call in New Year after mth & has cleared and [HMRC officer] will write agreement to me: ie keep current year up to date and pay £4k per month off arrears. Explained would be about a month late with current year payments."

70. The Action History record of the same call is consistent with the company's evidence:

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[2] Month 5 was included in the original penalty calculation notice, but removed on review

[3] Mrs Weare informed the Tribunal that this meant "warning of legal action and penalties".

> "tele call from tp inst arrgt agreed. Rob Primarolo the dir rang he stated he is sending a chq today for mth 7 of £27.198.89 and £3k re the arrears, explained that if the current is not kept up2date then proceedings will comm.
>
> Dir explained that co still struggling because of the recession, He advd that they can pay mth 9 by the 19/1 but will have a problem with mth 8 after long conversation agreed for t/p to pay mth 7 and 9 and then have time to clear mth 8 with the arrears. Co to pay £4k initially but their intention is to clear that mth asap. Agreed to this but did insist that all future debts must be made on time."

71. The Tribunal understands from the parties' evidence that HMRC agreed to collect the overdue payment for Month 8 over a period of time. This is then confirmed in further internal notes on 11 January 2011.

72. On 11 January Mr Primarolo called and renegotiated this agreement, asking if he could pay "£4k pm re 09/10 and mth 8" The record says "*agreed as long as dd set up.*" A revised instalment arrangement was agreed on the same day.

73. We find that the agreement, as amended, was to collect Month 8 over a period of a year. It clearly does not constitute a statutory TTP arrangement as the Month 8 payment was already due by the time it had been negotiated.

74. The **Month 9** payment was due on 19 January. No further communication took place before that date and the payment was not made on time. As a result, there is no TTP agreement and no reason to think one was in place.

75. No penalty was charged for Months 10 or 11 because no PAYE was held to be due. The Tribunal found this to be highly unusual, but as it has not been challenged by HMRC and neither party has provided evidence to the Tribunal, we have accepted the position.

Conclusions from the detailed review

76. The result of the Tribunal's review is that we find as a fact that the company did not have a TTP agreement for any of the months in question. In particular we note that:

(1) most of the references to a TTP agreement in the Action History record refer to that agreed for the 2009-10 underpayment.

(2) in January 2011, HMRC agreed to delay collection of the Month 8 PAYE amount. This was described as a TTP agreement, but it was for debt that had already become due. As we said earlier in this decision, it is clear from the wording of FA 2009, Sch 56, para 10(2) that a TTP agreement must come before the payment date if a penalty is to be avoided.

77. In making this finding we also take into account the company's submission that not all calls were recorded by HMRC. The Action History notes do, in fact, record the company's statement that they will be paying late each month; even if a further

statement to this effect had been made, it would not have changed our decision. Given the detailed and contemporaneous nature of the Action History record, and the absence of any specificity as to dates or times of the alleged missing calls, we have accepted the HMRC record as accurate. We are fortified in this finding by the fact that, where other evidence does exist (as it does in relation to the calls made on 24 December 2010), it supports the Action History record.

78. We also find as a fact that the directors did not *agree* with HMRC that payments would be late – rather, they imply told HMRC when the company was going to pay. During the year, HMRC several times record Mr Primarolo's request that all payments be made a month late, but this offer was explicitly not accepted by HMRC

79. Nevertheless, we find that the directors genuinely believed that informing HMRC that a payment would be late was sufficient to prevent a penalty accruing. For example Mr Primarolo's letter of 26 October 2011 to HMRC says:

> "the payment plan was at one point renegotiated to include month 8 of the tax year 2010-11 with [name of officer] on 24 December 2010 at which point I informed her that I would be late in paying the remaining months for 2010-11 (so how you can charge me a penalty for this month and the subsequent months is quite frankly beyond belief."

In oral evidence before the Tribunal Mr Severn said that "As far as I was aware as long as if I rang up then that was enough".

80. We have considered whether the directors' belief that, for the penalty to be removed, they simply needed to tell HMRC in advance that payment of the PAYE will be late, constitutes a reasonable excuse.

81. The company has not explicitly provided any basis for their belief – such as written guidance from HMRC or statements in their many phone conversations. Nothing in the Action History notes to indicate that HMRC had at any time indicated to the company that the various payment arrangements would prevent a penalty accruing. In the absence of any reason for this belief, it cannot constitute a reasonable excuse.

82. However, it is clear that in past years the directors had simply called HMRC and no penalties had accrued. We therefore infer that it was this past practice on which they were relying.

83. Assuming this inference is correct, this would mean that directors' belief rested on their failure to realise that the law had changed, and that from April 2010 penalties would be charged for late paid monthly PAYE. However, we note that:

(1) It is well established principle of English law that ignorance of the law cannot constitute a reasonable excuse.

(2) HMRC has no statutory duty to inform employers of the change in the law; the onus is on taxpayers to be aware of changes to the law.

(3) Even though there was no statutory obligation on HMRC to inform the company of the change to the law, it issued a letter to the company on 28 May 2010 warning that the payment for Month 1 was late and that further late payments risked penalties.

(4) HMRC twice explicitly referred to the risk of penalties[4], although we did note that references to distraint and enforcement proceedings are more frequent than references to penalties.

84. We thus find, first, that the company's belief that a unilateral statement that PAYE payments would be late will be sufficient to prevent a penalty from being charged, does not of itself constitute a reasonable excuse. On the assumption that this belief rested on the directors' failure to the law had changed, this also does not constitute a reasonable excuse – even though HMRC might have done more to draw the change in the law to the company's attention.

Overall conclusions on TTP

85. As a result of the foregoing, we find that there was no TTP agreement for any of the months of default. We also find that the company's mistaken belief that it was enough simply to inform HMRC about late payments, does not constitute a reasonable excuse.

Special circumstances

86. FA 2009, Sch 56, para 9 allows HMRC to reduce the penalty "if they think it right because of special circumstances/"

87. In *Clarks of Hove Ltd. v Bakers' Union* [1978] 1 WLR 1207, a decision of the Court of Appeal, "special circumstances" was said to mean "exceptional or out of the ordinary".

88. HMRC did not make any submissions to the Tribunal about special circumstances and there is nothing we could find in the papers provided to us, which indicated that the special circumstances provisions had been considered.

89. In *Algarve Granite v R&C Commrs* the Tribunal (Judge Brannan and Mr Howard) held that HMRC's failure to consider whether or not special circumstances exist meant that the decision is "flawed" in a judicial review sense. We do not repeat their careful analysis here, but gratefully rely upon it.

90. Because HMRC did not consider special circumstances, the Tribunal must consider whether the penalty should be reduced under FA 2009, Sch 56, para 9.

91. The first step is whether there are any "special circumstances" in the company's case. We have to set aside the shortage of funds, as "ability to pay" cannot constitute a

[4] On 7 June and 25 October 2010

special circumstance[5]. The only other reason for late payment given by the company is the mistaken belief that simply informing HMRC that they were going to pay late was sufficient to prevent a penalty arising. This, in our view, does not fall within the meaning of "special circumstances" – it is simply an erroneous understanding, probably based on a failure to realise that the law had changed.

92. Thus, although we have considered special circumstances, we have found that none apply to the company.

Proportionality

93. Mr Primarolo submitted in his letter of 10 October 2011 that the penalty charge was "completely exorbitant". We have taken this as a submission that the penalty was disproportionate.

94. Proportionality is an important constituent in both EU law and the Human Rights Convention. The company in this case is disputing a penalty for late submission of PAYE returns. This is a domestic legal question and does not engage EU law.

95. The Tribunal can thus only consider whether the penalty breaches the Convention, and in particular Article 1 Protocol 1 ("A1P1") of the Human Rights Convention, incorporated as Schedule 1 of the Human Rights Act 1988, which reads as follows:

> "**Protection of Property**
>
> Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and the general principles of international law.
>
> The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties

96. Whether or not a penalty is disproportionate has recently been considered by the Upper Tribunal in *Total Technology (Engineering) v R&C Commrs* [2012] UKUT 418(TC) ("*Total Technology*"). At [50] to [66] of their decision, the Upper Tribunal comprehensively reviewed the relevant case law on proportionality under human rights law. We gratefully adopt their analysis, which is not repeated here.

97. With reference to the second paragraph of A1P1 the Upper Tribunal said[6]:

> "A1P1 itself provides that the State may enforce such laws as *it* deems necessary. In those circumstances, it is not at all surprising that the State is entitled to a wide margin of appreciation, so wide as to allow

[5] FA 2009, Sch 56, para 9(2)(a)

[6] At [50(c)] of the decision; the emphasis given to "it" in the first sentence is that of the Upper Tribunal

> imposition of taxes, contributions or penalties unless the legislature's assessment of what is necessary is devoid of reasonable foundation."

98. The phrase "devoid of reasonable foundation" is derived from EU caselaw[7] and also emphasised in UK court judgments[8].

99. Other case law states that a penalty will disproportionate so as to be a breach of an individual's Convention rights, if it is "not merely harsh but plainly unfair, so that, however effectively that unfairness may assist in achieving the social goal, it simply cannot be permitted."[9] Both of these tests set a very high threshold before a penalty can be found by a court or tribunal to be disproportionate.

100. Applying these principles to the penalty charged on the company in this case, we find that:

(1) it was self-evidently introduced to encourage prompt payment of PAYE, which is a legitimate aim;

(2) it is proportionate to the size of the unpaid PAYE and to the number of defaults each year;

(3) there is no penalty for the first default, which helps to mitigate the harshness of the regime;

(4) there is further provision for the penalty to be reduced or eliminated by the reasonable excuse and/or special circumstances provisions.

101. In short, we find that although the penalty may be regarded as "harsh", it is within the state's margin of appreciation and does not meet the threshold of being "plainly unfair" or "without reasonable foundation".

Decision

102. We thus find that:

(1) the company does not have a TTP agreement for the months in question;

(2) neither its cashflow difficulties nor its belief that simply informing HMRC that payment would be late, constitutes a reasonable excuse for its defaults;

(3) there were no special circumstances; and

(4) the penalties were not disproportionate.

103. As a result we dismiss the appeal and confirm the penalties.

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[7] *Gasus Dosier- und Fördertechnik GmbH v. The Netherlands* (Application no. 15375/89) at [60]
[8] See for example *R (Federation of Tour Operators) v HM Treasury* [2008] STC 2524 at [32]
[9] *International Transport Roth GmbH v Home Secretary* [2003] QB 728 at [26]

Appeal rights

104. 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.

105. 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.

ANNE REDSTON
TRIBUNAL PRESIDING MEMBER

RELEASE DATE: 19 February 2013