



**TC03401**

**Appeal number: TC/2013/06806**

*VAT default surcharge - VAT paid late - Appellant mistakenly believed VAT was in credit and deducted 'credit' from VAT payment - whether reasonable excuse - no - insufficiency of funds - whether reasonable excuse - no - Appeal dismissed*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**TEMPS LIMITED**

**Appellant**

**- and -**

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

**TRIBUNAL:    JUDGE MICHAEL S CONNELL  
                  MR JOHN WILSON**

**Sitting in public at Alexandra House, The Parsonage Manchester on 7 January  
2014**

**The Appellant did not attend and was not represented**

**Ms Helen Roberts officer of HM Revenue and Customs, for the Respondents**

## DECISION

### The Appeal

1. Temps Limited (“the Appellant”) appeals against VAT default surcharges of £1,468.49 and £220.27, for its failure to submit, in respect of its VAT periods ended 01/13 and 04/13 respectively, by the due date, payment of the VAT due. The surcharges were calculated at 10% and 15% respectively of the amounts paid late.
2. The point at issue is whether or not the Appellant has a reasonable excuse for making late payment.
3. The Appellant did not attend the hearing and was not represented. However the Tribunal was satisfied that the Appellant had been notified of the date time and venue of the hearing and that it was in the interests of justice to proceed.

### Background

4. The Appellant had previously defaulted on a VAT payment in period 10/11 when a VAT surcharge liability notice was issued and had defaulted again in respect of periods 01/12 and 04/12.
5. Section 59 Value Added Tax Act 1994 (“VATA”) sets out the provisions in relation to the default surcharge regime. Section 59 of the VATA requires a VAT return and payment of VAT due on or before the end of the month following the relevant calendar quarter. [Reg 25(1) and Reg 40(1) VAT Regulations 1995].
6. The Appellant paid VAT on a quarterly basis and usually paid its VAT by the Faster Payment System (FPS). HMRC may allow additional time for payment when made by electronic means and pursuant to Regulation 40 (4) of the VAT Regulations 1995 allows an additional seven days after the end of the calendar month when payment would normally fall due (together with a further three days when the VAT is collected by direct debit). Limitations apply if the due date falls on a weekend or a bank holiday in which event the due date defaults to the last previous working day.
7. The Appellant submitted its 01/13 VAT return electronically on 7 March 2013. Payment was made in four instalments on 7 March 2013, 8 March 2013, 13 March 2013 and 3 April 2013 all by FPS. The VAT payment was therefore late.
8. The Appellant submitted its 04/13 VAT return electronically on 7 June 2013. Payment was made in two instalments on 7 June 2013 and 21 June 2013, each by FPS. The VAT payment was therefore again late.
9. Under s 59(1) a taxable person is regarded as being in default if he fails to make his return for a VAT quarterly period by the due date or if he makes his return by that due date but does not pay by that due date the amount of VAT shown on the return. The Commissioners may then serve a surcharge liability notice on the defaulting taxable person, which brings him within the default surcharge regime so that any

subsequent defaults within a specified period result in assessment to default surcharges at the prescribed percentage rates. The specified percentage rates are determined by reference to the number of periods in respect of which the taxable person is in default during the surcharge liability period. In relation to the first default the specified percentage is 2%. The percentage ascends to 5%, 10% and 15% for the second, third and fourth default.

10. A surcharge liability notice was issued for period 01/13 of £1,468.49 on 15 March 2013 and for period 04/13 of £440.54 (later reduced to £220.27) on 14 June 2013.

10 11. HMRC contend that the Appellant should have been aware of the potential financial consequences of a default, having been in the default surcharge regime from 16 December 2011 and having defaulted on two further occasions prior to the first default under appeal.

15 12. A taxable person who is otherwise liable to a default surcharge may nevertheless escape that liability if he can establish that he has a reasonable excuse for the late payment which gave rise to the default surcharge(s). Section 59 (7) VATA 1994 sets out the relevant provisions : -

20 ‘(7) If a person who apart from this sub-section would be liable to a surcharge under sub-section (4) above satisfies the Commissioners or, on appeal, a Tribunal that in the case of a default which is material to the surcharge –

25 (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

30 (b) there is a reasonable excuse for the return or VAT not having been so despatched then he shall not be liable to the surcharge and for the purposes of the preceding provisions of this section he shall be treated as not having been in default in respect of the prescribed accounting period in question ..’

13. The initial onus of proof rests with HMRC to show that a surcharge has been correctly imposed. If so established, the onus then rests with the Appellant to demonstrate that there was a reasonable excuse for late payment of the tax. The standard of proof is the ordinary civil standard on a balance of probabilities.

35 14. Section 59(7) must be applied subject to the limitation contained in s 71(1) VATA 1994 which provides as follows : -

‘(1) For the purposes of any provision of section 59 which refers to a reasonable excuse for any conduct -

40 (a) any insufficiency of funds to pay any VAT due is not a reasonable excuse.’

15. Although an insufficiency of funds to pay any VAT due is not a reasonable excuse, case law has established the principle that the underlying cause of any insufficiency of funds may constitute a reasonable excuse.

#### Appellant's Case

5 16. In its appeal letter dated 25 June 2013, the Appellant refers to the first default under appeal in respect of the VAT quarter ended 01/13:

10 *"We made payments of £52,000 on 07/03/13, £4,000 a day later on 08/03/13, £4,000 the following week on 13/03/13 and the balance of £6684.91 on 03/04/2013. Whilst we appreciate that part of this payment was late we feel strongly that HMRC's attitude to charge a surcharge is extremely harsh when we have made every effort to pay the VAT due. We continue to operate under very difficult trading conditions and had hoped that HMRC would take a more compassionate view towards these late payments, bearing in mind our determination to pay them as quickly as possible.*

15 *We would like to ask HMRC to rethink their position in relation to charging £1468.49 for late payments of £4,000 by 1 day, £4,000 by a week and the balance of £6,684.91 by 4 weeks."*

17. In relation to the second default under appeal in respect of the VAT quarter ended 04/13 the Appellant said in its notice of appeal:

20 *"We made a payment of £59,081.66 (which was made up of £60,550.15 due less a balance of £1,468.49 as per on line VAT a/c.) Subsequently, following a conversation with someone from your office we were told that what we thought was a credit on our account (a balance), wasn't in fact a credit, but a deficit (i.e. the fine from the previous VAT return), and as we had taken it as a credit*  
25 *we were in fact in arrears by £2,936.98 and a new fine had been imposed of £440.54 (which was 15% of the outstanding amount of £2,936.98.) Again we think this is extremely harsh".*

18. The Appellant added that HMRC's website which portrays VAT owed by a customer is :

30 *"extremely misleading and ambiguous. HMRC debt collection accepted our explanation and halved the surcharge of £440.54 for the period 04/13, as though we had paid the VAT on time, but could not remove the surcharge completely. If HMRC can accept they made a genuine mistake and halve the surcharge, why is it that they cannot remove the surcharge completely."*

35 19. The Appellant points out that the balance of VAT due of £2,936.98 was paid on 21 June 2013, as soon as it was realised a mistake had been made.

20. The Appellant also refers to the economic environment and their determination to meet their obligations despite difficult trading conditions experienced by both themselves and their customers. The Appellant says that the company has been in

existence for fifteen years and has only encountered difficulties in paying VAT on time since the onset of the recession.

### HMRC's Case

5 21. Ms Roberts for HMRC said that the potential financial consequences attached to the risk of a default would have been known to the Appellant after issue of the Surcharge Liability Notice for period 10/11 and subsequent surcharge default extension notices. The information contained on the reverse of each Notice states:

10 'Please remember your VAT returns and any tax due must reach HMRC by the due date. If you expect to have any difficulties contact either your local VAT office, listed under HM Revenue & Customs in the phone book as soon as possible, or the National Advice Service on 0845 010 9000.'

22. The requirements for submitting timely electronic payments can also be found -

- 15
- In notice 700 "the VAT guide" paragraph 21.3.1 which is issued to every trader upon registration.
  - On the actual website [www.hmrc.gov.uk](http://www.hmrc.gov.uk)
  - On the E-VAT return acknowledgement.

20 23. Also, the reverse of each default notice details how surcharges are calculated and the percentages used in determining any financial surcharge in accordance with the VAT Act 1994 s 59(5).

24. Therefore, HMRC say that the surcharge has been correctly issued in accordance with the VAT Act 1994 s 59(4).

25 25. With regard to the Appellant's grounds of appeal and in so far as the Appellant refers to difficult economic times, it is specifically stated in s 71(1) VATA 1994 that any insufficiency of funds to pay any VAT is not reasonable excuse.

26. HMRC may allow additional time for payment if requested. Any request must be made prior to the date on which the VAT falls due. The Appellant did not make any request for a time to pay arrangement.

30 27. HMRC contend that anyone giving their affairs due diligence should be aware of the time a payment takes to clear, and of any conditions their bank operates under regarding faster payment. The consequences of further failures had been fully spelt out and the company should have ensured that payment was made on time.

28. VAT is never the property of the company, the money belongs to the Crown and must be paid over as the law requires.

29. For a reasonable excuse to exist there must be something such as an unforeseeable or inescapable event outside their control so that despite the exercise of reasonable forethought and due diligence a default could not be avoided.

5 30. The Appellant has not given any specific reason for the 01/13 default other than  
implying that they were suffering general financial difficulties. Section 71(1)(a)  
VATA specifically excludes insufficiency of funds from being a reasonable excuse. A  
specific underlying reason behind the insufficiency of funds that could not be avoided  
even using foresight and due diligence may exceptionally amount to a reasonable  
10 excuse, but general economic trading conditions face all traders and are encountered  
in the normal course of business. All traders have to manage cash flow and deal with  
the economy in good times and bad. The ebb and flow of the economy is part of  
normal business trading and a normal risk of doing business. It is expected that a  
prudent business person will take steps to manage his business to ensure his  
obligations are met.

15 31. The Appellant also refers to the surcharge as being harsh. The question of  
fairness was addressed in the Upper Tribunal decision of *Hok* where it was  
commented that:

20 "It follows that in purporting to discharge penalties on the ground that their imposition  
was unfair, the Tribunal was acting in excess of jurisdiction, and its decision must be  
quashed."

The VAT default surcharge regime and penalties imposed for late payment are laid  
down in legislation and the First-tier Tribunal does not have jurisdiction to consider  
issues of fairness.

25 32. The Appellant says that it hoped that HMRC would take a more compassionate  
view towards these late payments bearing in mind their determination to pay them as  
quickly as possible.

30 33. Section 108 Finance Act 2009 was introduced specifically to help businesses  
having difficulty in paying their VAT, but the business needs to ask for time to pay.  
Surcharges are not imposed if deferred payment plans are requested and agreed before  
the due date and the plan is adhered to. There is no evidence of a time to pay  
agreement being requested by the Appellant.

34. Ms Roberts said that the VAT belonged to HMRC and should not be treated as  
part of a tax payers cash flow. She referred to the majority judgement of Lord Justice  
Nolan in *Stepto* where he said:

35 "That is because the scheme of collection which I have outlined involves at the outset  
the trader receiving (or at least being entitled to receive) from his customers the amount  
of tax which he must subsequently pay over to the commissioners. There is nothing in  
law to prevent him from mixing this money with the rest of the funds of his business  
and using it for normal business expenses (including the payment of input tax), and no  
40 doubt he has every commercial incentive to do so. The tax which he has collected  
represents, in substance, an interest-free loan from the commissioners. But by using it

5 in his business he puts it at risk. If by doing so he loses it, and so cannot hand it over to the commissioners when the date of payment arrives, he will normally be hard put to it to invoke s 19(6)(b). In other words he will be hard put to it to persuade the commissioners or the tribunal that he had a reasonable excuse for venturing and thus losing money destined for the Exchequer of which he was the temporary custodian.”

10 35. HMRC say that with regard to the second default under appeal, what happened was unfortunate and may at best be classed as a genuine error. However this does not equate to a reasonable excuse. VAT Public Notice 700/50 advises what factors will be taken into account when considering reasonable excuse and states that “Genuine mistakes, honesty and acting in good faith are not reasonable excuses”.

15 36. Legislation does not differentiate between a payment which is one day late or ten days or more late. The legislation is clear as to its intention and when a VAT payment is late statute provides for how the surcharge is to be calculated by reference to a percentage of unpaid VAT by the due date. HMRC submit that in their view neither HMRC nor the Tribunal have jurisdiction to mitigate a surcharge which has been properly calculated.

20 37. HMRC submit that the Appellant failed to make payments of VAT by the due date and their failure resulted in a surcharge being imposed. The Appellant has not discharged the onus on it to demonstrate that there was an acceptable reasonable excuse for its failure to pay the VAT by the due date.

### Conclusion

38. The Appellant was clearly aware of the due date for payments of its VAT and the potential consequences of late payment.

25 39. The Appellant’s first ground of appeal in essence is that it was suffering cash flow shortages at the time of the default.

30 40. To elaborate on HMRC’s submissions, in *Customs & Excise Commissioners –v- Steptoe [1992] STC 757* the tax-payer argued that although the proximate cause of his default was insufficiency of funds, the underlying cause of that insufficiency, namely the unexpected failure by a major customer to pay him on time, amounted to a reasonable excuse. The Court determined on a majority that the statutory exclusion of insufficiency of funds as an excuse did not preclude consideration of the underlying cause of insufficiency and that a trader might have a reasonable excuse if it were caused by an unforeseeable or inescapable event or when, despite the exercise of reasonable forethought and due diligence, it could not have been avoided. The Court  
35 nevertheless made it clear that the test had to be applied strictly.

40 41. To decide whether a reasonable excuse exists where insufficiency of funds causes the failure the Tribunal must take for comparison a person in a similar situation to that of the actual tax-payer who is relying on the reasonable excuse defence. The Tribunal should then ask itself, with that comparable person in mind, whether notwithstanding that person’s exercise of reasonable foresight, due diligence and a proper regard for the fact that the tax would become payable on the particular dates,

those factors would not have avoided the insufficiency of funds which led to the failures. There is no evidence that the Appellant did so. Furthermore the Appellant could have requested a time to pay arrangement but did not do so

5 42. The Appellant's second ground of appeal is that there was a genuine mistake and no intention to pay VAT late. That is accepted by the Tribunal, but it is not a valid ground of appeal. HMRC agreed to halve the penalty previously imposed and the reduced penalty remains payable.

10 43. The burden of proof is on the Appellant to show that the underlying cause of its failure to meet its VAT payment obligations was due to unforeseen circumstances or events beyond its control. In the Tribunal's view, for the reasons argued by HMRC and given above, that burden has not been discharged and there was no reasonable excuse for the Appellant's late payment of VAT for the 01/13 and 04/13 VAT periods.

44. The appeal is accordingly dismissed and the surcharge upheld.

15 45. 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  
20 "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

**MICHAEL S CONNELL**

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**TRIBUNAL JUDGE**

**RELEASE DATE: 10 March 2014**