TC03668

Appeal number TC/2014/01775

Value added tax – default surcharge – proportionality of penalty – Total Technology decision – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

K B EDITORIAL LTD

Appellant

- and -

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

TRIBUNAL: JUDGE MALACHY CORNWELL-KELLY
MR MICHAEL SHARP FCA

Sitting in public at Ashford House, County Shopping Centre, Ashford on 22 May 2014

The taxpayer company was not represented

Ms Rita Pavely of HM Revenue and Customs for the Crown

DECISION

Introduction

1 This appeal concerns a default surcharge of £377.00 for the period 11/13. We received a telephone message that Ms Kathryn Brown – who we understand to be the Managing Director of the appellant company – would not be present for the hearing but that she was "willing for the appeal to go ahead in her absence". We considered therefore that in the interests of justice it would be appropriate to proceed to determine the appeal as provided for in Rule 33.

Facts

2 The surcharge history of the appellant shows that defaults occurred in periods 08/12, 05/13 and 08/13, as well as that under appeal in respect of 11/13. The first default occasioned simply the issue of a surcharge liability notice commencing the surcharge regime; the second and third defaults resulted in penalties at 2% and 5% respectively, but they made no financial impact on the appellant because, being for less than £400, the penalties incurred were not collected. Nevertheless, the company would have been informed of the penalties and that the progressive nature of the surcharge regime was in course. The default under appeal is therefore at 10% of the tax paid late.

3 The due date for the payment in respect of the 11/13 quarter was 31 December 2013, extended in the case of electronic payments by seven days to 7 January 2014. The return for the quarter was made electronically on 7 January but the tax itself was not paid until 10 January. Ms Brown described this in her notice of appeal as "being slightly disorganised" and pointed out that this was at the busiest time of year. The penalty involved for this very short delay was, Ms Brown claimed, out of proportion to its extent – three days.

4 In her appeal notice, Ms Brown describes herself as "a busy mum of two trying to make a living", and in a previous letter to HMRC said that-

> I think it is absolutely outrageous that a person who is in no way trying to avoid payments is presented with such a fine when more and more people are avoiding both tax and VAT by dealing in cash. Not to mention the big corporations who seem to get away with murder.
>
> I am a one person operation, a busy working mum, who tries her best to be organised and efficient. The idea that you can fine me in this way is beyond infuriating.

5 On the issue of the proportionality of the penalty to the default, Ms Pavely relied on the decision of the Upper Tribunal in *Total Technology* as to the First-tier Tribunal's powers, which we cite below.

Legislation

6 The Value Added Tax Act 1994 provides:-

> 59 *The default surcharge*
> (1) Subject to subsection (1A) below 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.

(1A) A person shall not be regarded for the purposes of this section as being in default in respect of any prescribed accounting period if that period is one in respect of which he is required by virtue of any order under section 28 to make any payment on account of VAT.

(2) Subject to subsections (9) and (10) below, subsection (4) below applies in any case where—

(a) a taxable person is in default in respect of a prescribed accounting period; and

(b) the Commissioners serve notice on the taxable person (a "surcharge liability notice") specifying as a surcharge period for the purposes of this section a period ending on the first anniversary of the last day of the period referred to in paragraph (a) above and beginning, subject to subsection (3) below, on the date of the notice.

(3) If a surcharge liability notice is served by reason of a default in respect of a prescribed accounting period and that period ends at or before the expiry of an existing surcharge period already notified to the taxable person concerned, the surcharge period specified in that notice shall be expressed as a continuation of the existing surcharge period and, accordingly, for the purposes of this section, that existing period and its extension shall be regarded as a single surcharge 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) Subject to subsections (7) to (10) below, the specified percentage referred to in subsection (4) above shall be determined in relation to a prescribed accounting period by reference to the number of such periods in respect of which the taxable person is in default during the surcharge period and for which he has outstanding VAT, so that—

(a) in relation to the first such prescribed accounting period, the specified percentage is 2 per cent;

(b) in relation to the second such period, the specified percentage is 5 per cent;

(c) in relation to the third such period, the specified percentage is 10 per cent; and

(d) in relation to each such period after the third, the specified percentage is 15 per cent.

(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.

(7) If a person who, apart from this subsection, would be liable to a surcharge under subsection (4) above 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,

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 (and, accordingly, any surcharge liability notice the service of which depended upon that default shall be deemed not to have been served).

(8) For the purposes of subsection (7) above, a default is material to a surcharge if—

(a) it is the default which, by virtue of subsection (4) above, gives rise to the surcharge; or

(b) it is a default which was taken into account in the service of the surcharge liability notice upon which the surcharge depends and the person concerned has not previously been liable to a surcharge in respect of a prescribed accounting period ending within the surcharge period specified in or extended by that notice.

(9) In any case where—

(a) the conduct by virtue of which a person is in default in respect of a prescribed accounting period is also conduct falling within section 69(1), and

(b) by reason of that conduct, the person concerned is assessed to a penalty under that section,

the default shall be left out of account for the purposes of subsections (2) to (5) above.

(10) If the Commissioners, after consultation with the Treasury, so direct, a default in respect of a prescribed accounting period specified in the direction shall be left out of account for the purposes of subsections (2) to (5) above.

(11) For the purposes of this section references to a thing's being done by any day include references to its being done on that day.

71 *Construction of sections 59 to 70*

(1) For the purpose of any provision of sections 59 to 70 which refers to a reasonable excuse for any conduct—

(a) an insufficiency of funds to pay any VAT due is not a reasonable excuse; and

(b) where reliance is placed on any other person to perform any task, neither the fact of that reliance nor any dilatoriness or inaccuracy on the part of the person relied upon is a reasonable excuse.

(2) In relation to a prescribed accounting period, any reference in sections 59 to 69 to credit for input tax includes a reference to any sum which, in a return for that period, is claimed as a deduction from VAT due.

Conclusions

7 It is well established that if a surcharge complies with the statutory requirements in the circumstances of the case, it must be upheld and any indulgence or mitigation is a matter for the commissioners alone or, in exceptional cases, for judicial review; parliament has given the tribunal no power to reduce or mitigate default surcharges. That said, the decision of the Upper Tribunal in *Total Technology (Engineering) Limited v. RCC* [2012] UKUT 418 (TCC) does acknowledge that the tribunal at this level may strike down penalties if they are clearly out of all proportion to a default,

8 The decision in *Total Technology* was an exhaustive review of the law on this subject, and a case in which the appeal failed. In the context of the approach to be taken to the principle of proportionality in connection with the default surcharge regime, the Upper Tribunal observed at [97] -

> At the individual level, however, the question is whether the actual penalty is disproportionate in all of the circumstances and not whether there is a power to mitigate. The relevance of a power to mitigate is that an unreasonable penalty can be reduced and the question of proportionality of the penalty then falls to be answered by reference to the penalty as mitigated. Accordingly, we do not consider that the absence of a power to mitigate a penalty renders the regime non-compliant with the principle of proportionality. It is the level of the penalty, if anything, which will bring about that result.

9 At [99] the parameters of the first-tier tribunal's discretion in the matter are set out –

> In our judgment, there is nothing in the VAT default surcharge which leads us to the conclusion that its architecture is fatally flawed. There are, however, some aspects of it which may lead to the conclusion that, on the facts of a particular case, the penalty is disproportionate. But in assessing whether the penalty in any particular case is disproportionate, the tribunal must be astute not to substitute its own view of what is fair for the penalty which Parliament has imposed. It is right that the tribunal should show the greatest deference to the will of Parliament when considering a penalty regime just as it does in relation to legislation in the fields of social and economic policy which impact upon an individual's Convention rights. The freedom which Parliament has in establishing the appropriate penalties is not, we think, necessarily exactly the same as the freedom which it has in accordance with its margin of appreciation in relation to Convention rights (and even there, as we have explained, the margin of appreciation will vary depending on the right engaged).

10 In regard to the circumstances of the case then under appeal, the Upper Tribunal noted at [101] and [102] –

> Nor, on the facts of the present case, do we consider that the penalty imposed on the Company is disproportionate in the sense that its imposition is a breach of EU law and in particular of the principle of proportionality.
>
> The Company's essential complaint is that the amount of the penalty is unfair. It is unfair because of the following factors:
>
> a. the payment was only one day late;
>
> b. the previous defaults had been due to errors which were innocent, even if the Company could not establish a reasonable excuse for them;

> c. the Company had an excellent compliance record prior to the first of the defaults leading to the penalty;
> d. the amount of the penalty represents an unreasonable proportion of the Company's profits.
>
> Each of those factors falls within one of the heads of complaint which we have addressed. None of those complaints results in the default surcharge being non-compliant with the principle of proportionality; nor, in our view, do they have that result even if taken collectively. At the level of the Company, the amount of the penalty has been arrived at by applying a rational scheme of calculation which involves no breach of the principle of proportionality. That amount cannot, even if looked at in isolation, be said to be disproportionate in the sense of giving rise to a breach of the principle of proportionality. And even if the penalty is more than would be imposed if it were a matter for the decision of a tribunal, the amount of the penalty does not approach the sort of level which Judge Bishopp described as unimaginable in *Enersys*.

11 In *Total Technology*, the penalty being appealed was £4,260.26; annual profits were "around £50,000", which suggests quarterly profits of £12,500 making the surcharge in that case 34% of the quarterly profit – and still that appeal was unsuccessful. Since Ms Brown was not present at the hearing of this appeal, we did not have the opportunity to enquire the turnover of the business or its level of profit, and we cannot therefore reach any conclusion on whether the proportion which the penalty bears to, for example, a quarter's profits, takes us anywhere near the extremely limited discretion which we have.

12 It must be said that experience is that it is very unusual for such a situation to arise, but in any event there is not the evidence in this case upon which any conclusion can be reached impugning the penalty on the ground of disproportionality. If, having regard to the figures we have mentioned, Ms Brown considers that she can establish that her company would be able to take advantage of the limited latitude allowed by the Upper Tribunal's decision in *Total Technology* she should submit it to HMRC in writing.

13 That this was the "busiest time of year" does not in itself establish any exceptional circumstance that could give rise to a reasonable excuse within the meaning of the legislation, because it is a factor common to any business around Christmas. In the outcome, therefore, no reasonable excuse within the meaning of the legislation has been established and, given the very limited powers which parliament has allowed to the tribunal, we regret that the appeal cannot succeed.

Appeal rights

14 The appellant, not having been present or represented at the hearing of this appeal, is entitled pursuant to Rule 38 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 to make an application in writing to be received by the tribunal no later than 28 days after this Decision is sent to it for the Decision to be set aside and remade.

15 This document contains the 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 no 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.

MALACHY CORNWELL-KELLY
TRIBUNAL JUDGE

RELEASE DATE: 30 May 2014