



TC03669

Appeal number TC/2013/09227

*Value added tax – default surcharge – one day late payment –
proportionality of penalty – Total Technology decision – appeal dismissed*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

BRUCE & CO BUILDING CONTRACTORS (SUSSEX) 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

Mr H W Allen, Managing Director, for the taxpayer company

Ms Rita Pavely of HM Revenue and Customs for the Crown

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DECISION

Introduction

1 This appeal concerns a default surcharge of £927.09 for the period 08/12.

5 *Facts*

2 The surcharge history of the appellant shows that defaults occurred in periods 02/11,
05/11, 02/12, as well as that under appeal in respect of 08/12. The first default
occasioned simply the issue of a surcharge liability notice commencing the surcharge
regime; the second and third defaults resulted in no monetary penalty, because the
10 amounts of the surcharges were each less than £400 and were not therefore collected.
The surcharge for period 08/12 is therefore the first to impact financially on the
company, but in each of the first three cases the company would have been notified of
the defaults and their significance in the surcharge system, namely that the
progressive increase in the penalties from 2% to 5% to 10% was in principle
15 operating.

3 The due date for the payment in respect of the 08/12 quarter was 30 September
2012, extended in the case of electronic payments by seven days to 7 October. In
2012, 7 October was a Sunday and the company did not have sufficient funds to make
payment in full on the preceding Friday, 5 October; first thing on Monday 8 October,
20 when he was sure that funds were available, Mr Allen called at the bank to authorise
payment and it was received by HMRC that day *via* the Faster Payments System
(which the company had been using at least since April that year).

4 Mr Allen also told us that he had not noticed that the extended due date fell on a
weekend and that payment one day later – effectively just 9.5 hours after the deadline
25 – would be seen as a default. The company now uses internet banking, which enables
payment to be made even on a non-working day. As well as these circumstances,
which Mr Allen said should be taken into account, he urged upon us that the penalty
of £927.09 was disproportionate in relation to the very short period indeed for which
the payment had been late. The company, as most businesses, had had a very
30 challenging time during the recession and could afford only one secretary/bookkeeper
for this kind of work, and Mr Allen had to deal with payment authorisations himself
personally. Mr Allen told us that his company's annual turnover was in the region of
£250,000, with a 10-15% net profit.

5 Ms Pavely drew our attention to the reference at 21.3.1 in Notice 700, the VAT
35 Guide which is given to all taxpayers, to the requirement that electronic payments
falling due on a bank holiday or a weekend must clear HMRC's account beforehand –
unless the Faster Payments System is used which can enable payments to be made
during a weekend. The same is stated clearly at HMRC's website, which is referred
to in the automated responses to the online filings which the company was making.

40 6 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

7 The Value Added Tax Act 1994 provides:-

59 The default surcharge

5 (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

10 (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.

15 (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—

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

25 (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.

30 (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—

35 (a) is in default in respect of a prescribed accounting period ending within the surcharge period specified in (or extended by) that notice, and

40 (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.

45 (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;

50 (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.

5 (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

8 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;
10 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,

15 9 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] -

20 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
25 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.

30 10 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
35 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
45 depending on the right engaged).

11 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 *Energysys*.

12 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, contrasting with the 14-15% which is likely to be the highest which can be claimed in the present case. In regard to the claim of the lack of proportionality in the surcharge, therefore, it is clear that this case is a long way off the percentage which the penalty bore to the profits in *Total Technology* and in which the taxpayer was, even so, unsuccessful.

13 In so far as the immediate shortage of funds on Friday 5 October was concerned, it is clear from section 71 cited above that we are prohibited from taking it into account, and no overwhelming or exceptional event was suggested as having led to that position. The company was indeed already using the Faster Payments System which allows transfers to be made outside banking hours and, if the funds had been available on 7 October, the payment could have been made just in time rather than as it was just out of time. In the outcome, no reasonable excuse within the meaning of the legislation has been established: given the very limited powers which parliament has allowed to the tribunal, we regret that the appeal cannot succeed.

14 It must be recorded that Mr Allen made complaint additionally on two counts. The first was that his company's name had been misspelt on the publically displayed hearing list (by substituting 'Essex' for 'Sussex') and, more importantly, that the tribunal administration appeared to have lost his original appeal. This latter situation resulted in HMRC seeking to enforce the penalty and denying that an appeal had been made; and Mr Allen told us that it was ten months before any action was taken on his appeal.

15 The error in the hearing list is incontestable and we must apologise on behalf of the tribunal for it occurring. We were not in a position to go into the second complaint at the hearing, and it is for the tribunal administration itself to respond to it: if Mr Allen wishes to take it further, he should contact the Registrar at the Birmingham address which he will already be in possession of.

16 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.

15 **MALACHY CORNWELL-KELLY**
TRIBUNAL JUDGE

RELEASE DATE: 30 May 2014