



TC04250

Appeal number: TC/2014/01600

VAT – default surcharge – whether Tribunal has jurisdiction to consider an appeal against a surcharge not actually collected due to HMRC administrative practice of not enforcing surcharges of less than £400 imposed at 2% or 5% rate – practical implications in similar appeals considered – whether reasonable excuse for default in this case – appeal dismissed, even though no surcharge actually imposed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

WORKSTATION FARNHAM LTD

Appellant

-and-

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

Respondents

TRIBUNAL: JUDGE KEVIN POOLE

The Tribunal determined the appeal on 7 November 2014 without a hearing under the provisions of Rule 26 of the Tribunal Procedure (First-tier Tribunal)(Tax Chamber) Rules 2009 (default paper cases) having first read the Notice of Appeal dated 30 April 2014 (with enclosures), HMRC's Statement of Case received on 18 June 2014 (with enclosures) and HMRC's response dated 9 October 2014 to the Tribunal's request for representations from the parties dated 23 September 2014.

DECISION

Introduction

1. This appeal started life as a straightforward appeal against a default surcharge of £752.32 imposed (at the 10% rate for a fourth default) for late payment of VAT in respect of VAT accounting period 11/13.
2. Upon HMRC deciding to cancel the surcharge liability notice issued in respect of the first default in the current cycle, the result was that the default for period 11/13 became subject to default surcharge at the rate applicable to a third default (i.e. 5%); as this meant the size of the surcharge reduced to £376.16, HMRC confirmed they would not be seeking to collect it, under their general administrative practice of not enforcing default surcharges of less than £400 arising at the 2% or 5% rates for second and third defaults.
3. The preliminary question that then arose was whether the appeal should continue in relation to what had now been “downgraded” from a £752.32 default surcharge at the 10% rate to a surcharge liability notice extension without any financial penalty attached for period 11/13.
4. This decision considers the detailed law applicable to such issues, and discusses some practical implications in relation to other similar appeals.

The facts

5. The facts are not complex, though they are a little convoluted.
6. The Appellant was late in paying its VAT for various periods, with the consequences (in terms of surcharge liability notices and a default surcharge) as set out in the table below:

Default number	VAT period	Amount paid late	Consequence
1	05/12	£6,359.55	Surcharge liability notice issued
2	05/13	£5,108.81	Surcharge liability notice extension issued (surcharge at 2% rate would have been £102.17, below £400, so not imposed)
3	08/13	£3,895.81	Surcharge liability notice extension issued (surcharge at 5% rate would have been £194.79, below £400, so not imposed)
4	11/13	£7,523.21	Surcharge of £752.32 issued at 10% rate

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7. The Appellant wrote to HMRC on 31 January 2014, asking for a review of the surcharge. They confirmed its imposition in a letter dated 24 February 2014 and advised the Appellant on his right to appeal to the Tribunal.

8. The Appellant did so. He wrote to the Tribunal on 11 March 2014 (received on 13 March 2014), asking the Tribunal to “review the case”. Unfortunately, he did not use the Tribunal’s notice of appeal form and his letter did not contain all the necessary details to comply with the Tribunal’s procedure rules so the papers were returned. They were resubmitted, together with a notice of appeal form, and received by the Tribunal on 2 May 2014. To the extent necessary, I direct that the appropriate time limit for submission of the notice of appeal be extended such that the appeal received on 2 May 2014 shall be deemed received in time.

9. The grounds of appeal stated by the Appellant were essentially:

(1) it was thought payments had always been made on the 10th of the month, which was considered to be the due date;

(2) the Appellant did not believe it had received the earlier warnings, and it had been given (and kept to) a payment plan; and

(3) the funds were not available to pay the surcharge;

10. The appeal papers were forwarded to HMRC on 9 May 2014, and they were requested to deliver their statement of case within 42 days. The appeal was allocated to the “default paper” category.

11. In HMRC’s statement of case, which was received on 19 June 2014, they said it had been established that there was indeed a “time to pay” arrangement in place in relation to period 05/12, which was therefore removed from the schedule of defaults. In consequence of this, the default for period 11/13 now became the third (rather than the fourth) default in the cycle, with an applicable default surcharge rate of 5% rather than 10%. This reduced the size of the surcharge from £752.32 to £376.16 which was below the £400 level which HMRC did not collect. The default surcharge was therefore removed altogether and HMRC were not seeking to impose any financial penalty on the Appellant for the 11/13 default (though it would still count as a default, which would continue the present cycle of defaults and therefore render the Appellant liable to a default surcharge at the 10% rate if it defaulted again in respect of any period up to and including 11/14).

12. In the light of the particular circumstances of the case, the matter was referred to me for consideration – in particular as to whether it was appropriate for the appeal still to be determined, bearing in mind there was no extant default surcharge.

13. I considered it appropriate to outline my thoughts on that issue to the parties and offer them the opportunity to make representations before I reached a view on it.

14. HMRC have responded, by representations dated 9 October 2014.

The law

Introduction

15. My concern in the present case is a somewhat technical one, but it has a number of practical implications.

5 16. The broad scheme of the VAT default surcharge appeals legislation is that no appeal is to be brought in relation to any alleged defaults until an actual surcharge liability is triggered. When that occurs, an appeal is made against the imposition of the surcharge and in the context of that appeal, the Tribunal is required to consider not only the default which actually triggered the surcharge, but also any other default
10 which is “material” to it. Defaults considered to be “material” for this purpose are effectively those which have contributed to the imposition of the surcharge, but only if they have not already given rise to a surcharge for a period earlier than the one under appeal.

Examples

15 17. Let us consider an example of a trader (X) who has, let us assume, a VAT liability of £30,000 per quarter and who consistently pays all his VAT late. When he does so for the first time (say, for period 03/13), he will receive a surcharge liability notice. No right of appeal to the Tribunal arises in relation to that notice. When he defaults again in relation to the following period (06/13), he will be subject to a 2%
20 default surcharge of £600, against which he can appeal. In the context of that appeal, the Tribunal can consider not only the circumstances surrounding the 06/13 default, but also those surrounding the 03/13 default.

18. Now let us assume the Tribunal confirms the 06/13 surcharge (having found no reasonable excuse to exist for either the 03/13 or 06/13 default). Then X defaults
25 again in relation to period 09/13. A 5% surcharge of £1,500 is imposed by HMRC. If X wishes to appeal against that surcharge, the Tribunal may not reconsider the question of “reasonable excuse” in relation to the 03/13 and 06/13 surcharges.

19. Now let us assume the Tribunal finds a reasonable excuse to exist for the
30 09/13 default. The 5% surcharge is removed, along with the surcharge liability notice extension. But X defaults again in relation to period 12/13, so a further surcharge at the 5% rate is imposed (of £1,500). This time, X decides not to appeal the surcharge.

20. He then defaults again in relation to period 03/14. A surcharge at the 10% rate
35 is imposed for this fourth default in the cycle (£3,000). X appeals, and wishes also to assert a reasonable excuse in relation to one or more of the earlier defaults. He cannot do so (even in relation to period 12/13, which he has not previously appealed), because all of the earlier defaults have already given rise to earlier surcharges. If he wishes to maintain an appeal against the validity of the surcharge liability notice extension for period 12/13, he can only do so in the context of an appeal against the default surcharge actually imposed by that notice. He would therefore need to apply
40 to make a late appeal against the 12/13 surcharge which, if permission were granted,

would (if possible) be heard at the same time as his appeal against the 03/14 surcharge.

The legislation

21. The legislation which sets this out is in subsections 59(7) and (8) of the Value
5 Added Tax Act 1994 (“VATA”), which provide as follows:

“(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 –

10 (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

15 (b) there is a reasonable excuse for the return or the 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).

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

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

30 (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.”

22. It can readily be seen that these provisions refer to the taxpayer being “liable to a surcharge”, rather than being “required to pay a surcharge” (the relevant words have been italicised above).

35 *Interaction with administrative non-collection of small surcharges*

23. The difficulty in the present appeal is that these provisions sit rather uneasily with HMRC’s practice of not imposing default surcharges of less than £400 where the applicable surcharge rate is 2% or 5%. Under the terms of the provision which actually imposes the default surcharge (subsection 59(4) VATA), a taxpayer is made

“liable to a surcharge” calculated in accordance with subsections 59(4) and (5) VATA. Thus, even though HMRC do not seek to collect the smaller surcharges, the taxpayer is still technically “liable” to them. Of course, if they have not been imposed, then the taxpayer will not have any reason to appeal against them; but strictly speaking he should, just in case he becomes liable to a later surcharge in the same cycle of defaults. This is because, in relation to any such later surcharge, the earlier default will not be “material to the surcharge”, because the taxpayer will have “previously been liable to a surcharge” (even though no surcharge was actually imposed) in respect of the earlier prescribed accounting period.

10 Discussion and decision

The general issue

24. Applying the law to the facts of the present appeal, therefore, even though the Appellant is ultimately not being charged with a default surcharge for period 11/13, he is strictly liable to a surcharge for that period and therefore he can appeal against that liability. But if he is not being asked to pay a surcharge, why should he bother? Because if he does not do so, but commits a further default in the current cycle of defaults (leading to the imposition of a further surcharge) the Tribunal would have no jurisdiction, in the context of an appeal against the later surcharge, to consider whether there was in fact a reasonable excuse for the 11/13 default.

25. It is also worth observing that, in the context of the present appeal, the Tribunal has no jurisdiction to consider whether the 05/13 or 08/13 defaults should be expunged on the basis of a reasonable excuse, as neither of those defaults is “material to” the 11/13 surcharge (because the Appellant has “previously been liable to a surcharge in respect of a prescribed accounting period ending within the surcharge period specified in or extended by” the surcharge liability notices for those earlier periods, even though HMRC have chosen not to collect the default surcharges that were strictly due for them).

26. Thus HMRC’s administrative relaxation (in not collecting small surcharges) has the (presumably unintended) effect of preventing a taxpayer from arguing that a reasonable excuse exists for the earlier relevant default(s) when appealing a later default surcharge. Until the legislation is changed to correct this deficiency, the only safe course for taxpayers who receive surcharge liability extension notices which have benefited from the £400 administrative relaxation is to appeal against their issue where the taxpayer considers there is a reasonable excuse for the default, even though there is no immediate financial penalty at stake.

27. It is to be expected that unless and until the law is changed, the Tribunal is likely to be sympathetic to applications for late appeals in relation to earlier surcharge liability notices where the taxpayer is prevented by this legislative bear trap from raising any “reasonable excuse” argument in relation to those earlier defaults in the context of a later default surcharge appeal. That cannot be guaranteed, however, and in any event will add a wholly unwelcome and entirely unnecessary extra complication to many such appeals.

The specifics of this case

28. The only default that I have power to consider, from the point of view of “reasonable excuse”, is that relating to period 11/13.

29. Addressing the grounds of appeal actually raised by the Appellant (see [9] above):

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(1) I do not consider that the Appellant’s misunderstanding of the due date for payment can give rise to a reasonable excuse. There is nothing to suggest that HMRC have misled him (except perhaps the Appellant’s assertion that it has not received any of the earlier surcharge liability notices, as to which see below), and taxpayers have a general responsibility to inform themselves about due dates for payment – which is also amply explained in HMRC’s publications on the point.

(2) HMRC have accepted that the Appellant was given (and kept to) a time to pay arrangement for period 05/12, hence they have cancelled the surcharge liability notice for that period. As to the alleged non-receipt by the Appellant of the notices, I accept HMRC’s submission that the burden lies on the Appellant to satisfy the Tribunal that it was not served with the notices (under section 98 VATA and section 7 Interpretation Act 1978). I do not consider it has discharged that burden. Its entire approach to the discharge of its VAT liabilities and to the conduct of this appeal displays a degree of disorganisation and I do not feel able to accept the Appellant’s letter (which states that the writer has “no recollection of this” before going on to assert that he was never notified by HMRC of any non-payment) as sufficient evidence to persuade me.

(3) An insufficiency of funds cannot give rise to a reasonable excuse for non-payment (see section 71 VATA); the underlying cause of such an insufficiency is capable of doing so, but there is no evidence before me to support the existence of any such circumstances. In any event, the stated ground of appeal is not that the Appellant had insufficient funds to pay the VAT, but that it has insufficient funds to pay the surcharge.

Decision

30. I therefore find there to have been no reasonable excuse for the Appellant’s late payment of its VAT for the period 11/13 and the Appellant was therefore liable to a surcharge of £376.16 in respect of that default (even though HMRC, under their usual administrative practice, did not seek to enforce payment of that liability).

31. I must therefore DISMISS the appeal.

32. 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.

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**KEVIN POOLE
TRIBUNAL JUDGE**

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RELEASE DATE: 12 November 2014