



TC03910

Appeal number: TC/2014/01144

VAT default surcharge – payment made late – insufficiency of funds – whether reasonable excuse – no – whether penalty disproportionate – no – appeal dismissed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

DNA CONSULTANCY LTD

Appellant

- and -

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

TRIBUNAL: JUDGE MICHAEL S CONNELL

The Tribunal determined the appeal on 28 May 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 notification of Appeal dated 28 October 2013 and 26 February 2014 and HMRC's Statement of Case received on 18 March 2014, the Appellant submitting no response.

DECISION

The Appeal

5 1. DNA Consultancy Ltd ('the Appellant') appeals against a default surcharge of £1,009.75 imposed by HMRC on 12 July 2013, in respect of the VAT period ended 31 May 2013, for its failure to submit, by the due date, payment of VAT due. The surcharge was calculated at 10% of the VAT due of £10,097.57.

10 2. The point at issue is whether the Appellant has a reasonable excuse for making late payment.

Background

15 3. The Appellant has been in the VAT default surcharge regime from period 02/12 and prior to the surcharge period under appeal had defaulted in periods 11/12 and 02/13.

4. The Appellant was on a quarterly basis for VAT. Section 59 of the VAT Act 1994 requires VAT returns and payment of VAT to be made on or before the end of the month following each calendar quarter. [Reg. 25(1) and Reg 40(1) VAT Regulations 1995.]

20 5. HMRC have discretion to allow extra time for both filing and payment when these are carried out by electronic means. [VAT Regulations 1995 SI 1995/2518 regs. 25A (20), 40(2)]. Under that discretion, HMRC allow a further seven days for electronic filing and payment.

25 6. In respect of the default in period 05/13, as payment was made electronically the due date was 7 July 2013. The return was received on 10 July 2013 and the VAT payment in two instalments on 19 July 2013 and 23 August 2013.

30 7. 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. Section 59 (7) VATA 1994 sets out the relevant provisions : -

'(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 –

35 (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

40 (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.

8. Section 59(7) must be applied subject to the limitation contained in s 71(1)
5 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 -

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

10 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

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

Appellant’s contentions

10. The Appellant does not dispute that its VAT payments for the periods 05/13, was late.

20 11. The Appellant’s grounds of appeal are that it had cash flow problems. In its letter of appeal the Appellant says:

25 “As stated in my letter payment of £10,097.57 was due during July 2013. A part payment of £6,000 was made on 19 July 2013 with the outstanding payment of £4,097.57 made on the 23 August 2013. I accept that this is a late payment but the outstanding sum was just over £4,000 for less than 2 months. A surcharge of over £1,000 cannot reflect the amount of loss to the HMRC.

30 I also note that notices were sent to us, these did not reach us. We notified the VAT office of our change of address through the web site, post and forms. The process of change of address took some time to register.

35 The late payment was due to cash flow issues with our business. We are a small company of 2 full time and 1 part time staff. Approximately 70% of our work is carried out through sub consultancy arrangements with much larger organisations. The 30 day arrangements we have are with very few exceptions adhered to.”

HMRC’s contentions

40 12. The Period 05/13 had a due date of 7 July 2013 for electronic VAT Payments and returns. The VAT return was not received on time. The Appellant paid his VAT electronically. The tax due was £10,097.57. The first payment of £6,000 was twelve days late and payment of the balance outstanding of £4,097.57 was received by

HMRC on 23 August 2013, 47 days late. As the payment was received late the Surcharge was correctly imposed.

13. The potential financial consequences attached to the risk of default should have been known to the Appellant from the information printed on the 02/12 V160 Surcharge Liability Notice and subsequent V161 default notices

14. Included within the notes on the reverse of the Surcharge Liability Notice, is the following, standard, paragraph:

“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.”

15. The reverse of each 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).

16. The requirements for submitting timely electronic payments can in any event be found-

- 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
- On the E-VAT return acknowledgement.

17. The Surcharge has therefore been correctly issued in accordance with the VAT Act 1994 s 59(4), payment having been received by HMRC after the due date.

18. With regard to the Appellant's grounds of appeal, it is specifically stated in s 71(1) VATA 1994 that any insufficiency of funds to pay any VAT is not reasonable excuse.

19. 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 made no contact with HMRC prior to the due dates for payment and did not make any request for a time to pay arrangement

20. The Appellant says that the surcharge is unfair and does not reflect any loss to HMRC. The case of *Total Technology (Engineering) Limited v HMRC* was heard in the Upper Tribunal when it was held that:

- 1) There is nothing in the architecture of the default surcharge system which makes it fatally flawed.
- 2) The Tribunal found that the VAT default Surcharge regime does not breach EU law on the principle of proportionality.

3) In order to determine whether or not a penalty is disproportionate, the Upper Tier Tribunal addressed the following factors:

- (a) The number of days of the default
- (b) The absolute amount of the penalty
- 5 (c) The ‘inexact correlation of turnover and penalty’
- (d) The ‘absence of any power to mitigate’

The Upper Tribunal Chamber President, Mr. Justice Warren and Judge Colin Bishopp decided that none of these leads to the conclusion that the Default Surcharge regime infringes the principle of proportionality.

- 10 21. The default surcharge is calculated by reference to the number of previous defaults and the amount of VAT paid late in accordance with legislation. It is not intended to reflect any loss to HMRC.

Conclusion

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

23. The Appellant’s ground of appeal is that it was suffering cash flow shortages at the time of the default.

- 20 24. 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 nevertheless made it clear that the test had to be applied strictly.

- 25 25. 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.
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26. The Tribunal accepts that the underlying cause of the defaults may have been cash flow shortage. However the Appellant has not been able to provide any information to show that the cash flow shortage was entirely unforeseeable, outside the normal hazards of trading or due to events beyond its control.

27. The Appellant could have requested time to pay but did not do so.

28. Legislation lays down the surcharges to be applied in the event of VAT being paid late. Surcharges are therefore applied at a rate fixed by statute and determined by the number of defaults in any surcharge liability period.

29. The burden of proof is on the Appellant to show that he has a reasonable excuse for the late payment of VAT for the period 05/13. In the Tribunal's view, for the reasons given above, that burden has not been discharged.

30. The Appellant says that the surcharges are unfair and do not reflect any loss to HMRC. For the reasons submitted by HMRC and set out in paragraphs 20 and 21 above, this is not a ground of appeal which can be considered by the Tribunal.

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

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.

MICHAEL S CONNELL
TRIBUNAL JUDGE

RELEASE DATE: 11 August 2014