[2018] UKFTT 0068 (TC)

TC06333

Appeal number: TC/2017/02363

VALUE ADDED TAX- default surcharge – interaction with payments wrongfully deducted under the Construction Industry Scheme by a major customer – reasonable excuse – no – appeal - dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

SDL INTERIORS LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE NIGEL POPPLEWELL
WILL SILSBY

Sitting in public at Cardiff on 4 December 2017

Mr Phillip Pook, Director of the appellant for the appellant

Miss Rhianon Lewis, Officer HMRC for the respondents

DECISION

INTRODUCTION

1. This is a VAT case. It concerns the default surcharge. The respondents (or "HRMC") have assessed the appellant to default surcharges for late payment of VAT for four VAT periods (the "Default Periods"), details of which are set out below.

Period	Amount
12/13	£2068.95
03/14	£2693.85
06/14	£2100.18
09/14	£3181.92

2. There is little or no dispute about the relevant law. The main issue in this appeal is whether the appellant has a reasonable excuse for the late payments.

3. The appellant and respondents agree that the appellant's most significant customer during the Default Periods had wrongly deducted tax under the Construction Industry Scheme ("CIS") on materials. This tax had been "deposited" with the respondents. The basis of the appellant's case is that it has a reasonable excuse because:

(1) This wrongfully deducted tax was sitting with HMRC during the Default Periods, and it more than covered the VAT due during those periods. So the appellant owed the respondents no VAT for the Default Periods; and/or

(2) The wrongfully deducted CIS tax caused cash flow difficulties which meant that the appellant could not meet its obligations to pay the VAT during the Default Periods.

4. For the reasons given below we have decided to dismiss the Appeal.

SUMMARY OF THE LAW

VAT and the default surcharge regime

5. The appellant paid VAT on a quarterly basis. Section 59 of the VAT Act 1994 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. 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 (2), 40(2)]. Under that discretion, HMRC allow a further seven days for filing and payment.

7. Section 59 Value Added Tax Act 1994 ("VATA 1994") sets out the provisions in relation to the default surcharge regime. 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. HMRC 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 chargeable default the specified percentage is 2%. The percentage ascends to 5%, 10% and 15% for the second, third and fourth default.

8. 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: -

> "(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 -
>
> (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 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 .."

9. It is s 59(7)(b) on which the appellant seeks to rely. The burden falls on the appellant to establish that it has a reasonable excuse for the late payment in question.

10. 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 -
>
> (a) any insufficiency of funds to pay any VAT due is not a reasonable excuse.'

11. The test we adopt in determining whether the appellant has a reasonable excuse is that set out in *The Clean Car Co Ltd v C&E Commissioners* [1991] VATTR 234, in which Judge Medd QC said:

> "The test of whether or not there is a reasonable excuse is an objective one. In my judgment it is an objective test in this sense. One must ask oneself: was what the taxpayer did a reasonable thing for a responsible trader conscious of and intending to comply with his obligations regarding tax, but having the experience and other relevant attributes of the taxpayer and placed in the situation that the taxpayer found himself at the relevant time, a reasonable thing to do?"

12. Although an insufficiency of funds to pay any VAT due is not a reasonable excuse, case law, most importantly the case of *C&E Commissioners v Steptoe* [1992] STC 757 ("*Steptoe*") has established the principle that the underlying cause of any insufficiency of funds may constitute a reasonable excuse. In *Jonathan Skuce v HMRC* [2018] UKFTT 003 ("*Skuce*") Judge Poon summarised the relevant case law as follows:

> "57. Section 71(1)(a) specifically precludes an insufficiency of funds from being a reasonable excuse. This statutory exclusion is qualified, to a limited extent, by case law authority such as *Steptoe*, which establishes the principle that there is a distinction between the direct or proximate cause and the underlying cause for the shortage of funds.
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> 58. In *Steptoe*, the taxpayer was an electrical contractor with 95% of his work being done for a Local Council, which was 'virtually his only customer', and 'an extremely slow payer'. The tribunal of first instance described the council as having 'never paid the amount owing on an invoice less than six weeks after it was delivered and usually it was paid upwards of two months late'.
>
> 59. The taxpayer in *Steptoe* was not on cash accounting, and was late in paying his VAT for two periods (11/86 and 08/87) and then continued to be in default for the four successive periods of 11/87, 02/88, 05/88 and 11/88. The payments were late by about two months, and the taxpayer pleaded cash flow difficulties as his reasonable excuse. The Commissioners rejected the taxpayer's grounds for reasonable excuse, but the VAT tribunal (as it was then) allowed the taxpayer's appeal on the ground of the Council's pattern of paying late. The Commissioners appealed to the High Court, and Kennedy J confirmed the tribunal's decision. The Commissioners' appeal to the Court of Appeal was dismissed by a majority (Lord Donaldson MR and Nolan LJ, Scott LJ dissenting).
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> 60. The reasoning of the majority in *Steptoe*, according to Lord Donaldson, as regards the legislative intention of the predecessor provision of s 71(1)(a), 'is that insufficiency of funds can never of itself constitute a reasonable excuse, but that the cause of that insufficiency, ie the underlying cause of the default, might do so'.

61. That said, Lord Donaldson states that 'there must be limits to what could be regarded as a reasonable excuse'. As to what those limits could be, Lord Donaldson agrees with Nolan LJ's reasoning in this respect:

> 'Nolan LJ, as I read his judgment in *Customs and Excise Comrs v Salevon Ltd* [1989] STC 907, is saying that if the exercise of reasonable foresight and of due diligence and a proper regard for the fact that the tax would become due on a particular date would not have avoided the insufficiency of funds which led to the default, then the taxpayer may well have a reasonable excuse for non-payment, but that excuse will be exhausted by the date on which such foresight, diligence and regard would have overcome the insufficiency of funds.'

62. In contrast, Scott LJ's opinion that the underlying cause of the insufficiency of funds must be an 'unforeseeable or inescapable event' is considered as 'too narrow' by Lord Donaldson for the following reasons:

> '(a) it gives insufficient weight to the concept of reasonableness and
>
> (b) it treats foreseeability as relevant in its own right, whereas I think that 'foreseeability' or as I would say 'reasonable foreseeability' is only relevant in the context of whether the cash flow problem was 'inescapable', or as I would say, 'reasonably avoidable'. It is more difficult to escape from the unforeseeable than from the foreseeable.'

63. According to Lord Donaldson therefore, the appropriate test concerning whether an insufficiency of funds amounts to a reasonable excuse is to examine if the underlying cause of the insufficiency is 'reasonably avoidable'. It is important to distinguish what is foreseeable from what is avoidable. The foreseeability of the insufficiency has no relevance in its own right, and foreseeability is only relevant in assessing whether the shortage of funds could have been avoided. Shortly stated, what is unforeseen cannot be avoided; only the foreseeable is avoidable".

13. Although not binding on us, we consider this summary to be an accurate synopsis of the legal position and we gratefully adopt it for the purposes of this Decision.

The construction industry scheme

14. The provisions that allow HMRC to offset CIS deductions against a company's tax liabilities are in the Finance Act 2004 and the Income Tax (Construction Industry Scheme) Regulations 2005. Regulation 56(5) stipulates that HMRC shall not repay any sum deducted under FA 2004 s 61 to a company sub-contractor until:

> "The tax year in which the deduction was made, has ended and the qualifying sub-contractor has delivered the return required by regulation 73 of the PAYE Regulations (annual return of relevant payments liable to deductions of tax)."

15. Regulation 56(2) stipulates the order in which any CIS credits should be discharged and Regulation 56(3) states any sum deducted as is not required to discharge the sub-contractor's liabilities specified in paragraph (2) shall be repaid to the qualifying sub-contractor.

16. Where the sub-contractor is a company, the legislation states at FA 2004 s 62(3) that deductions are first to be treated as paid on account of any "relevant liabilities" of the sub-contractor. "Relevant liabilities" in this context means the company's obligations to pay over to HMRC any PAYE, NICs, and CIS deductions. Any excess deductions determined at the end of the tax year when the company has submitted its employer's annual return on form P35 for non-Real Time Information ("RTI") years, or Employer Payment Summary returns for RTI years, can be set against corporation tax liabilities or repaid.

17. For RTI years, the company will complete monthly Employer Payment Summary returns showing cumulative CIS deductions taken from its own income during the tax year. These amounts are off-set against the PAYE and other deductions it is due to pay for the tax year. Any excess of CIS deductions taken from the company's own income is carried forwarded month by month until all of the CIS deductions for the tax year are used, or the end of the tax year is reached.

18. Repayment and off-set claims for limited company subcontractors can only be dealt with when the company has filed its final Employer Payment Summary and all associated Full Payment Submissions for the tax year. If HMRC cannot agree the company's whole claim, they will ask the company for their payment and deduction statements and supporting evidence of receipt. HMRC can still consider a part repayment/off-set for the deductions they can agree. Where there is a mis-match, HMRC will need to take up the discrepancy with the company.

19. It is not until the end of the tax year that excess CIS deductions which cannot be set-off and are still available may be refunded or set against other liabilities.

FINDINGS OF FACT

20. We were provided with a bundle of documents. Mr Pook gave oral evidence on behalf of the appellant. He gave his evidence clearly and, save as regards one element of his evidence which we deal with at [29] to [31] below, we found him to be a cogent and reliable witness.

21. It was apparent at the hearing that evidence which could be relevant to our decision was not available, most importantly the timing of the over deduction by Lagan Construction (“Lagans”), and the appellant's bank statements covering the payment dates for the Default Periods. Following a direction to this effect, the appellant provided these to us.

22. From this evidence, we make the following findings of fact:

(1) The appellant has been registered for VAT trading as an interior building services company since January 2007 with VAT registration number 885 5362 82.

(2) The appellant has been in the default surcharge regime from periods 03/12 onwards. The surcharge liability notices for the Default Periods were numerically correct and properly served on the appellant.

(3) From the period 06/12, the appellant's usual method of payment has been the "Faster Payment Service".

(4) For each of the Default Periods, the VAT returns were submitted and received on time. However, for each of those periods, payment of the VAT itself was late. For period 12/13, payment of £13,793 was due on 31/01/14 but was not made until 13/02/14. For period 03/14, the amount due was £17,959.05, the due date was 30/04/14 but payment was not made until 15/05/14. For period 06/14, the amount due was £14,001.22, the due date was 31/07/14 but payment was not made until 14/08/14; and for period 09/14, the amount due was £21,212.86, the due date was 31/10/14 but payment was not made until 21/11/14. These due dates are extended where payment is made electronically until seven days after the statutory due date. But in all the Default Periods, notwithstanding this extension, payments were still made after their respective due dates.

(5) The appellant's record of late payments prior to and during the Default Periods is set out below:

Period	**Amount in £ (rounded)**	**Dates Late (after the 7 days grace allowed for electronic payments)**
06/12	7,340	10
09/12	6,352	15
12/12	On time	
03/13	21,827	11
06/13	10,108	Difficult to tell but could be 42 days
09/13	12,736	11
12/13	13,793	6
03/14	17,959	8
06/14	14,001	7
09/14	21,212	14

(6) The appellant's most significant customer, by a country mile, during the Default Periods, was Lagans. Lagans and the appellant are subject to the provisions of the CIS which required Lagans, in the absence of a gross payment certificate which benefited the appellant, to deduct an amount equivalent to 20% of the payments it made to the appellant, from those payments. However, Lagans was only required to make these CIS deductions on the labour element of the services supplied by the appellant. It is not required by the CIS regime to make CIS deductions from the materials element of the payments.

(7) However, Lagans wrongfully (as accepted by both parties) made CIS deductions from the material's elements of those payments.

(8) Whilst it is not wholly clear when this over deduction was made, it seems to have been made from the payment due in respect of the October 2013 valuation and payment. A table of the deductions made by Lagans for the relevant period is set out below.

SDL Interior's valuation	Gross Labour Content	Monthly Labour Content	20% Deduction	Lagan Deduction
Sep-13	96739.63	96739.63	19347.93	
Oct-13	130031.98	33292.35	6658.47	58438.36
Nov-13	167524.46	37492.48	7498.50	
Dec-13	178890.89	11366.43	2273.29	
Jan-14	187483.19	8592.30	1718.46	
Feb-14	196343.19	8860.00	1772.00	
Mar-14				
Apr-14	220963.69	24620.50	4924.10	
			44192.75	58438.36

(9) The reason for the over deduction was that Lagans had assumed that the entirety of the relevant invoice was attributable exclusively to labour, when a good proportion of it was attributable to materials for which no deduction should have been made.

(10) On 19 November 2013 Mr Pook emailed Lagans pointing out the over deduction to them. At that stage he said the over deduction was

£52,373.25, and he asked Lagans to add that on to the payment due on 5 December 2013.

(11) Initially it seemed that Lagans were prepared to do that, but by 2 December 2013, they emailed the appellant to say that the amount "over taxed" in previous payments could not be rectified and SDL would have to reclaim it from HMRC.

(12) Following further email exchanges, on 9 December 2013 Mr Pook emailed Lagans to say:

> "Following my meeting on site last Thursday where as I was told by Mr Fergal Delaney that nothing could be done about the tax that had already been paid to HMRC, however my Company Secretary has since spoken to Revenue & Customs to ask their advice. She was informed by HMRC that it is possible for you to contact them and amend your submitted return accordingly, at which point you are then able to refund us the over subscription that you submitted. This will mean that any money you have already paid to HMRC, your account will be in credit and this can be offset against further amounts due.
>
> The only way that we would get reimbursements is by waiting until the end of the financial year, and after our accounts have been submitted and signed off. This we are not prepared to undertake, as this is clearly an error on behalf of Lagan account department, and according to HMRC it is your responsibility to correct the errors both prior and going forward".

(13) In December 2013, there were further email exchanges between Mr Pook and Lagans in which Lagans agreed to make no deductions for October and November (and indeed for further periods) to try and reduce the over taxation issue. As can be seen from the table at [22(8)], they made no further deductions until after April 2014.

(14) At that time Mr Pook was the finance director of the appellant.

(15) The mechanism of invoicing in the construction industry is less straightforward than it is in other industries. The sub-contractor values the work that he has undertaken for a contractor on a monthly basis, and does so on the 20th of each month. It values the work done between the 1st of the month until the 20th on an actual basis, and estimates the work that it will do between the 20th of the month and the end of that month.

(16) The contractor then has to certify that work by the 7th day of the following month. That certification indicates the amount that the contractor intends to pay to the subcontractor and identifies the CIS deductions that it is intending to make.

(17) Payment itself, however, is not then made until a month or so later.

(18) There is a mechanism to deal with disputes regarding the valuations but, we were told by Mr Pook that it is seldom used and the contractor has the commercial whip hand. At the end of the project there is a wash-up and, theoretically at least, the sub-contractor should have charged (and be paid for) for all the work that it has done. However, as Mr Pook says and as we accept, the sub-contractor often has to cut a commercial deal with the contractor at that time. So it may well be that the sub-contractor does not ever get fully remunerated for the entirety of the work that it has undertaken.

(19) What is clear, however, is that on the 7th day of the month when the certification has been given, the sub-contractor is clear about the amount that he will ultimately be paid by the contractor for the relevant period: and also clear of the amount that will be deducted under the CIS scheme from that payment.

(20) The appellant set off the Lagans over deduction against its in-year PAYE liabilities, but the over deduction far outweighed those PAYE liabilities.

(21) For the Default Periods, full credit had not been given for the overpaid CIS deductions against the PAYE liabilities. The responsibility for submitting VAT returns at the appellant fell to Rachel Limbrick who was responsible for VAT compliance generally.

(22) For the Default Periods, the appellant banked with Lloyds Bank, and its statements show that for the periods in which payments should have been made for the Default Periods, the appellant's overdraft limited was £25,000.

(23) Following imposition of the default surcharges (all of which were at the rate of 15%), the appellant requested a discussion with HMRC regarding the surcharges and sought a review. The respondents carried out such a review and informed the appellant in a letter dated 17 February 2017 that the surcharges were upheld.

(24) The appellant presented an appeal to the Tribunal on 14 March 2017.

BURDEN AND STANDARD OF PROOF

23. 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.

DISCUSSION

Appellant's grounds of appeal

24. The appellant puts forward two grounds of appeal.

> (1) HMRC was in possession of its money (namely the over deduction) and this was, or should have been, standing to the appellant's credit with HMRC. As such it owed no money to HMRC on the due dates for payment.
>
> (2) The over deduction had caused cash flow issues which meant that on each due payment date it was very difficult for the appellant to find the cash to pay the VAT due.

Respondents' submissions

25. HMRC submits as follows:

> (1) The appellant has been in the default surcharge regime since 03/12 and was well aware of the financial consequences of not paying VAT on time.
>
> (2) The surcharge liability notices sent to the appellant would have further alerted it to the importance of submitting its returns and VAT on time, and contained advice that taxpayers who could not pay the full amount of tax due on time should pay as much as possible to reduce or prevent a surcharge.
>
> (3) There is no evidence of the appellant contacting HMRC to indicate that it was likely to be unable to pay its VAT on time, nor seeking any Time to Pay arrangements for the Default Periods.
>
> (4) The appellant's bank statements show that it did not have an insufficiency of funds on the due dates for payment which prevented it paying the VAT on time.
>
> (5) The real reason the appellant paid VAT late was because it had made a business decision to keep the overdraft facility for other reasons.
>
> (6) The respondents have not visited a surcharge on the appellant for the period 09/13 as the over deduction occurred shortly before the due date for payment of VAT for that period.
>
> (7) By the time payment was due for period 12/13, and for future periods, any reasonable excuse for non-payment based on the over deduction had expired.
>
> (8) VAT collected by the appellant from payments made to it does not belong to it and should have been accounted for to HMRC rather than used

to pay other creditors. The appellant's conscious decision to pay other creditors is not a reasonable excuse.

Discussion

26. The appellant's first ground of appeal is that it thought that HMRC were sitting on the over deduction which was money due to it, and therefore on the due dates for payment of the VAT, there was nothing that he actually owed them on those dates.

27. We can see no reason why, in principle, an honestly held and reasonable belief by a taxpayer that it owes no money to HMRC, since HMRC are in possession of "its" money cannot be a reasonable excuse.

28. But we do not think that this comprises a reasonable excuse for this appellant in its circumstances.

29. Mr Pook has given slightly conflicting evidence concerning his knowledge of the basis on which over deductions made by a contractor can be put to the benefit of the sub-contractor. On two occasions in his evidence he indicated that he knew that CIS repayments due to a taxpayer could only be used against in year PAYE liabilities, and it was only at the end of the year, and in the following tax year, that they could be reclaimed or set off against other tax (including VAT liabilities). However, towards the end of his evidence he said on one occasion that he did not realise that CIS deductions could be used only against in year PAYE, but he thought they could be made against other tax liabilities in that year.

30. It is our view that Mr Pook's understanding of the way in which CIS repayments could be used is that they could be used only against in year PAYE.

31. We say this for a number of reasons:

(1) The appellant is a gross payee and as such would have been recovering or seeking credit for CIS payments for many years. We do not know when it entered the CIS, but we suspect it was in or around January 2007 given that it was then that it was registered for VAT. By 2013 the appellant would have had a lengthy track record and we strongly suspect, a considerable insight, into the way in which CIS deductions could be credited or used by it.

(2) It is absolutely clear that, in common with many other small businesses, Mr Pook was very concerned about the appellant's cash flow, and in particularly the cash that it was due from its most significant customer, Lagans. Indeed, when the problem of the over deduction by Lagans emerged, it was Mr Pook, as finance director of the appellant, who conducted the email discussions (and perhaps telephone discussions too) with Lagans with a view to persuading Lagans to pay the over deducted tax to the appellant with the December payment. An important factor in the appellants' cash flow was the use to which CIS deductions could be put. We think it is likely that Mr Pook would have known about the basis

on which HMRC would give credit or repayment for CIS deductions given his concern about cash flow.

(3) Furthermore, it was clear from the evidence of the email of the 9 December mentioned above, that Mr Pook knew that HMRC was not prepared to give credit or repayment for the over deduction until the next tax year.

(4) In his evidence, when questioned by the judge as to why, if he genuinely thought that HMRC was sitting on the appellant's money (and thus no further payments were due), the appellant in fact paid the VAT but did so late, Mr Pook responded that it was Rachel Limbrick, the company secretary, who was responsible for making payments, and that, had he known that she had been continuing to make payments of VAT, he would have asked her why she had done so given that HMRC was sitting on its money. We find this an unconvincing answer. As we have said, it is our view that Mr Pook knew (and certainly should have known) about the financial position of the appellant both generally and in respect of this Lagan over deduction. If he had genuinely thought, as he now asserts, that the appellant owed no money to HMRC, it would have been entirely consistent for him to have paid nothing at all to HMRC for the relevant periods. It is our view that if cash flow was, as it clearly was, as important to the appellant as Mr Pook has made out, and given his position as finance director and his involvement with Lagans concerning the over deduction, it is inconceivable to us that he would not have had considerable input into the payments that were made by the appellant to its creditors (including HMRC). If, therefore, he did have an honestly held belief that HMRC was sitting on the appellant's money and thus the appellant owed nothing to HMRC, we would have thought that he would have stopped paying HMRC the VAT due for the Default Periods (and indeed for later periods) until the credit had unwound itself.

32. On the basis of the foregoing, we therefore do not accept the appellant's first ground of appeal.

33. Turning now to the second ground. This is essentially that the appellant had a cash flow issue and could not find the money on the due dates to pay the VAT, as a result of the over deduction made by Lagans in October 2013.

34. An insufficiency of funds cannot be a reasonable excuse by virtue of Section 71(1) of VATA 1994.

35. But, as set out in *Steptoe* and as interpreted in *Skuce* it is clear that a shortage of funds might comprise a reasonable excuse, especially where a significant customer defaults in payment.

36. Following *Steptoe* and *Skuce*, we believe that the tests we should apply when deciding whether an insufficiency of funds may give a rise to reasonable excuse is as follows:

(a) If the insufficiency of funds was unforeseeable, then the taxpayer has a reasonable excuse.

(b) Even if the insufficiency of funds was foreseeable, the taxpayer may still have a reasonable excuse if that insufficiency was not reasonably avoidable.

(c) However, that reasonable excuse does not last for ever. It will cease when a previously unforeseeable shortage becomes foreseeable, and where a previously foreseeable shortage, (which is a reasonable excuse by dint of the fact that it was not reasonably avoidable), becomes reasonably avoidable.

37. Applying the first of these principles, it is our view that the shortage of funds was foreseeable.

38. We would note that it is to HMRC's credit that they have accepted that might not have been the case for the period 09/13 for which payment would have been due at the beginning of December 2013 (say 7 December 2013). This is on the basis that the over deduction occurred shortly before that date.

39. It was apparent to the appellant that probably by 9 December 2013 and certainly by 17 December 2013 that Lagans were not going to add the over deduction to the December payment and that the over deduction could only be dealt with in two ways. Firstly by Lagans reducing the CIS deductions for labour in future periods (which they then did as illustrated by the table at 22(8)); and secondly by the appellant making an in year deduction against its PAYE liabilities, and a claim in the following tax year for repayment of tax paid in the previous tax year, or credit against tax due in that following tax year.

40. We remind ourselves of the due dates for payment for each of the Default Periods. They were 7 February 2014, 7 May 2014, 7 August 2014 and 7 November 2014. So between 17 December 2013 and the date for payment for the first of these periods, there was a period of some 7 weeks. For subsequent Default Periods, the intervening periods were considerably longer (a period of nearly 11 months in the case of the payment due on 7 November 2014).

41. It is our view that given these intervening periods, the insufficiency of funds caused by the Lagans over deduction was entirely foreseeable as at the due dates for payment. And as such, we agree with HMRC that the appellant should have put in place financial contingency plans to enable it to pay the VAT on their respective due dates.

42. Furthermore, as set out at [22(5)] the appellant's pattern of late payments does not appear to have changed materially between the period before the over deduction and for the Default Periods.

43. Although the amounts of VAT payable in the Default Periods were generally larger than those preceding the Default Periods, the pattern of late payment (namely being between 6 - 14 days late) does not appear to have been affected by the Lagans over deduction.

44. This strongly suggests to us that the Lagans over deduction was not the proximate cause of the late payments during the Default Periods.

45. However, even if the shortage of funds was foreseeable, the appellant may still have a reasonable excuse if it can show that the insufficiency of funds was not reasonably avoidable. We do not think this is the case.

46. Firstly, in respect of those three Default Periods for which payment was due after the end of the 2013/2014 tax year (i.e. after 1 April 2014), the appellant could have made a timely application for credit of the Lagans over deduction against payments of VAT due on 7/5/14, 7/8/14 and 7/11/14.

47. We have found that the appellant, through the agency of Mr Pook, was aware of the ability to obtain credit or repayment for overpaid CIS tax in the following tax year. There is no evidence before us that the appellant made any effort to seek this credit or repayment and this has come as something of a surprise to us given Mr Pook's wholly justifiable insistence that cash flow was very important to the appellant. It is our view that the failure to make such a timely application for credit or repayment (something which was entirely in the hands of the appellant) is not something that a responsible taxpayer conscious of and intending to comply with its obligations regarding tax, would have done. This is especially in light of the experience of the appellant of the repayment and credit arrangements around the CIS deduction of which we think it was entirely aware since it had entered the CIS regime in 2007.

48. Secondly, an examination of the bank accounts shows that for the first Default Period, the payment of £13,793 for which was due on 7 February 2014 could have been paid at any time between 3 February 2014 and 7 February 2014 without breaching the overdraft limit.

49. Indeed, the appellant did not pay the VAT until 13 February 2014 notwithstanding that it could easily have done so any time on or after 7 February 2014 and been within its overdraft headroom.

50. It is our view as regards this period that the appellant made a conscious decision, as suggested by HMRC, to pay other creditors in preference to HMRC. Indeed, in his letter to the respondent's solicitors' office on 7 June 2017 (indeed to Miss Lewis) the appellant indicated that:

> "Most quarters had the VAT been paid on the date required the business account would have been taken up to its full overdraft limit or on one occasion over it. Leaving no money to keep labour on site or suppliers fluid with materials required. The business made a decision to hold payment until a definite receipt of funds had hit our account at which point it made payment immediately."

51. This "payment immediately" point is clearly wrong since in this period the appellant could have paid both on time and immediately after its due date. Payment was not actually made until 6 days after the due date.

52. For the payment due on 7 May 2014, it is clear from the bank statements that it would have been impossible for the appellant to have paid the VAT due of £17,959.05 at any time between 1 May and the date on which payment was actually made (15 May) without going over the appellant's overdraft limit.

53. So for this period, Mr Pook is right in that payment was made as soon as the overdraft headroom became available. But, as we say, by that time the knowledge of the over deduction had, in our view, become stale. Mr Pook knew about the over deduction and the fact that he could not get credit for it from HMRC until the following tax year in mid December 2013, some 4½ months prior to the payment date of the £17,959.05. A responsible taxpayer conscious of its obligations towards tax would have put in place some financial contingency plans to cover the payment date for this period. It would also have made a timely application for credit against VAT liabilities arising in the new tax year.

54. The staleness point is even more acute for payments due on 7 August 2014 and 7 November 2014. Even if (which we do not think is the case) the insufficiency of funds was not reasonably avoidable for the two earlier periods, in our view the position in respect of these two periods the shortage of funds had become reasonably avoidable because the appellant could and should have made a timely application for credit or repayment against the payments due in this tax year.

55. For the payment due on 7 August 2014 of £14,001.22, the appellant's bank account shows that such payment could have been made within its headroom at any time between 1 August 2014 and the due date of 7 August 2014. It could then have been made before it was ultimately paid on 14 August 2014. So again, Mr Pook's assertion that it either had insufficient money in its bank account to pay or that payment was made as soon as it did have money in its bank account (and thus justifying in this case payment on the 14 August rather than the 7 August) is incorrect. Payment could well have been made on the due date.

56. Finally, for the period for which payment should have been made on 7 November 2014 (the amount being £21,212.26), the appellant's bank statements show that payment of that amount could have been made at any time from 3 November to 5 November without breaching its overdraft (notwithstanding that on the due date, payment would have breached the overdraft). Payment was in fact made on 21 November 2014 when the appellant had £55,786 in its account, but it could have been made one week earlier on the 14 November 2014 when the appellant had £33,114.72

standing to its credit in its bank account. So again, Mr Pook's assertion that payment was made as soon as possible after the overdraft limit would not be breached, is incorrect.

57. Finally, it is worth observing that the appellant did benefit from a cash flow advantage as a result of Lagans not deducting any CIS tax from subsequent (i.e. after October 2013) related payments even from the labour element (which was probably incorrect as a matter of law). So the financial impact of the initial over deduction was ameliorated by this approach by Lagans and by January 2014, some £10k or so of CIS tax which should have been deducted, had not done been so. By the time that April 2014 was reached (as seen in the table at [22(8)], the amount of over deduction had reduced to £14,245.61.

58. So it was not all downside for the appellant.

59. Drawing these threads together, it is our view:

> (1) For each of the Default Periods, the impact on the appellant's cash flow and any sufficiency of funds caused by the Lagan over deduction, was foreseeable.
>
> (2) For each of these periods, any insufficiency of funds caused by that over deduction could reasonably have been avoided by the appellant putting in short term financial contingency plans; for paying within its overdraft limit; for discussing and perhaps reaching a time to pay agreement with HMRC; and by seeking credit or repayment for the over deduction against tax due in the tax year 2014/2015.

60. As we have said above, there is no difference in the pattern of late payments before and after the Lagan's over deduction, and it is our view, like that of HMRC and as admitted by Mr Pook in his letter to Miss Lewis of 7 June 2017 that the business had made a conscious decision to pay HMRC after it had paid other, in its view more important, creditors. The appellant had been in the default surcharge regime since 2012 and well knew the consequences of such failure. We suspect that those consequences were simply factored in to a commercial decision taken by the appellant to favour other creditors above HMRC. Accordingly, we do not believe that the appellant has a reasonable excuse for late payment of its VAT for any of the Default Periods.

DECISION

61. For the foregoing reasons we dismiss the appeal.

APPEAL RIGHTS

62. 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.

NIGEL POPPLEWELL
TRIBUNAL JUDGE

RELEASE DATE: 10 FEBRUARY 2018