



[2020] UKFTT 0087 (TC)

TC07581

VAT - default surcharge – Section 59 Value Added Tax Act 1994 - whether HMRC should have issued the penalty – yes - whether the Appellant has a reasonable excuse for late payment of VAT - Yes - Appeal Allowed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

Appeal number: TC/2019/04833

BETWEEN

MIRENCLIFF LIMITED

Appellant

-and-

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

Respondents

**TRIBUNAL: PRESIDING MEMBER: MR G.
NOEL BARRETT
MEMBER: MRS H MYERSCOUGH**

**Sitting in public at Taylor House Roseberry Avenue London on 16th December
2019**

Appellant Mr John Cross Director of the Appellant Company

**Miss Laura Castle Presenting Officer for HM Revenue and Customs' Solicitor's
Office, for the Respondents**

DECISION

INTRODUCTION

1. This is an appeal by Mirencliff Limited (“the appellant”) against an assessment for default surcharges for late payment of VAT as follows: -

Quarter	VAT	Due Date	Rate of Surcharge	Amount of Surcharge
01/19	£27,362.65	28.02.19	5%	£1,368.13

2. The assessment resulted from the appellant’s third default in accounting for its liability to VAT on time. It followed a Surcharge Liability Notice (“SLN”) which was issued to the appellant on 15.12.17, after its first default, for late payment of its VAT in the sum of £57,914 for the quarter 10/17, by virtue of which, the appellant entered into the default surcharge regime.

3. The appellant defaulted a second time by making late payment of VAT in the sum of £47,480.92 for the quarter 04/18 when a penalty at the rate of 2% amounting to £949.61 was imposed.

4. The appellant defaulted for a third time by making late payment of VAT in the sum of £27,362.65 for the quarter 01/19 when a penalty at the rate of 5% amounting to £1,368.13 was imposed.

5. The appellant was on time in filing its VAT Returns on each of the 3 occasions.

6. The appellant paid the VAT due 1 day late on 3 March 2019.

7. The appellant appeals against this third surcharge, firstly on the basis that HMRC should not have raised the surcharge; and secondly, on the basis that it has a reasonable excuse for late payment

8. The appellant requested HMRC to review its decision to impose the penalty surcharge and HMRC issued its reply on 3 July 2019, confirming that the surcharge would be upheld.

10. The appellant then appealed to the Tribunal, his appeal being generated on 26 July 2019.

THE LAW

11. By section 59(1)(a) and (b) of the Value Added Tax Act 1994 (VATA) a person shall be regarded as being in default for that period:

“if by the last day on which a taxable person is required to furnish a return HMRC have not received that return, or have received that return but have not received the amount of VAT shown on the return”.

12. Under Regulations 25(1) and 40(1) VAT Regulations 1995, if the tax payer is on a quarterly basis for returns, (as the appellant was) the returns and their related tax payments are due on or before the end of the month next following each calendar quarter. Where however the taxpayer files his return or pays tax electronically HMRC allow a further seven days from the end of the month next following each calendar quarter for such electronic filing and payment.

13. On a first default occurring, HMRC serve a Surcharge Liability Notice (SLN) on the taxable person. On subsequent defaults HMRC serve a Surcharge Liability Notice Extension (SLNE). Although no surcharge is imposed on the SLN, if any further defaults are made by the taxable person before the expiry of the first anniversary of the last day of the period referred to in the SLN, then the taxable person becomes liable to a surcharge being the greater of the specified percentage or £30.

14. With each SLN and subsequent SLNEs, HMRC provide the taxable person with notes explaining what amounts to a default and the consequences which will flow from further defaults. Those notes also advise the taxable person to contact HMRC's local Debt Management Unit if they expect to have difficulty paying VAT on time.

15. The specified surcharge percentages are set out in Section 59(5) VAT as follows:

- (a) in relation to the first prescribed period the specified percentage is 2%.
- (b) in relation to the second such period the specified percentage is 5%.
- (c) in relation to the third such period the specified percentage is 10%.
- (d) in relation to such period after the third the specified percentage is 15%.

16. HMRC do not however issue a surcharge at the rate of 2% or 5% if it calculates it to be less than £400. Nevertheless, the percentage surcharge continues to increase in accordance with paragraph 13 above, for each subsequent default.

17. Section 59(7) VATA provides that a taxable person shall not be liable to the surcharge and shall not be treated as having been in default, if he satisfies the Tribunal there is a reasonable excuse for late filing of the VAT return or the late payment of the VAT thereon.

18. Section 71(1) VATA provides that:

- “(a) an insufficiency of funds to pay any VAT is not a reasonable excuse;
and
- (b) where reliance is placed on any 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”.

19. Section 108 Finance Act 2009, as summarised, provides that there is no liability to a default surcharge for a period where contact is made with HMRC by the Tax Payer prior to the due date in order to arrange Time to Pay and that Time to Pay is agreed by HMRC.

20. References to “taxable person” and “Tax Payer” within the legislation include companies as corporate personalities as well as individuals.

THE STANDARD AND BURDEN OF PROOF

21. The standard of proof is the ordinary civil standard being “on the balance of probabilities”.

22. The burden of proving that the penalty is due and has been correctly calculated, falls upon the respondents

23. The burden of establishing a reasonable excuse falls upon the appellant

THE EVIDENCE AND OUR FINDINGS OF FACT

24. It is fair to say that there has been a significant amount of confusion in the case, on the part of both HMRC and the appellant as to whether or not and indeed during which periods there was a valid time to pay agreement in place in respect of the appellants outstanding VAT.

25. In our view this confusion cannot be over-emphasised and is conveniently illustrated by the number of subsequent amendments and alterations made by HMRC to the defaults it had previously notified to the appellant as shown within the bundle of documents in the schedule of defaults and payments

26. Thus, after being notified of a default for the 07/18 quarter on the 14 September 2018 carrying a 5% penalty amounting to £3,009.34, that surcharge was subsequently removed by HMRC by letter dated 3 July 2019.

27. Subsequently, after being notified of a further default for the 10/18 quarter on the 14 December 2018 carrying a 10% penalty amounting to £4,925.04, that surcharge was also subsequently removed by HMRC by letter also dated 3 July 2019. For in excess of 8 months, during which the appellant was under enormous financial strain in regard to their cash flow, they were under the impression (incorrectly, as it subsequently transpired) that they owed HMRC over £8,000 of penalties.

28. Upon those penalties being removed by HMRC, the penalty now under appeal was reduced from being charged at 15% equating to £4,104.39 to being charged at 5% amounting to £1,368.13.

29. By way of background Mr Cross explained and again we accepted that he had previously managed and run the “The Boatyard” at Leigh on Sea himself for approximately 17 years. However approximately three years ago, in the certainty that the restaurant was running well financially and that the long-term and capable members of staff, he had employed, trained and worked with for a number of years and the person he was going to promote to be a trusted senior manager of the business, were all trustworthy and capable of running the restaurant without him, he decided as he was by then in his late seventies, to retire from actively running the restaurant.

30. Mr Cross explained that at first, he simply could not understand why the company was running out of money and was “overheating” on its overdraft facility. He confirmed that the company should have had over £200,000 in the bank. Once he had engaged his accountants to forensically check the company's accounting records, they had advised him, to his horror, that the appellant company had been the subject of a serious and major financial fraud and that his trusted manager and possibly other staff had been fraudulently “cancelling off” hundreds of electronically generated customer bills and replacing them, with bills for much smaller amounts. He explained that customers had paid the original much larger and correct bill for that which they had consumed, but only the amount on the much smaller “replacement” account was actually being banked. It had been possible by checking incoming supplies to assess/guestimate the approximate amount the company had lost, but it was impossible to accurately calculate the precise amount.

31. Mr Cross explained that the appellant company was at that time faced with huge sudden and unexpected cash flow difficulties, at a time when the main and most profitable summer season was drawing to a close such that it looked as though the company might well go into liquidation or that HMRC would seek to wind the company up, unless they could somehow buy time to trade out of the huge and unexpected loss.

32. Furthermore Mr Cross also had to cope with the deceit of knowing that his senior staff member who he had personally chosen and trusted to manage the restaurant after his retirement, and possibly some other more junior staff members were criminals and had stolen large sums of money from the company.

33. Whilst he immediately dismissed the employees and reported them to the Police. In the event, after investigating the matter the Police decided that there was not enough evidence to warrant successfully prosecuting any of the employees.

34. Mr Cross confirmed that he immediately notified HMRC that the appellant would not be able to pay the VAT due for the 10/17 quarter and requested a time to pay agreement. Even though HMRC agreed a time to pay agreement, this default put the appellant into the VAT default surcharge regime, albeit that there is no penalty to pay on a first default.

35. Mr Cross explained that over the next 14 months he had numerous telephone conversations with HMRC explaining to them what had happened, pre-warning them that the appellant would again be unable to meet its quarterly VAT payment and extending the time to pay agreement as further quarterly VAT payments became due. During this period the appellant received at least four letters from HMRC in regard to its time to pay agreement as further amounts were added to it and the repayments amounts were altered, the most recent of which was dated 5 February 2019.

36. Mr Cross says that despite all his efforts he could not have a meaningful conversation with anyone at HMRC

37. He said that he believed that the amended time to pay agreement included the 01/19 payment, the subject of this appeal.

38. He asserted that he had done everything in his power, not only to keep making the agreed repayments under the time to pay agreement, but to ensure that the subsequent defaults were included within it.

39. We found Mr Cross to be an entirely credible witness for whom we have some sympathy, we accept fully his recollection of the facts of this case.

40. HMRC were however able to show and we accepted that the 01/19 quarter VAT payment could not have been included in the time to pay agreement, or in the instalments set out in their letter issued on 5 February 2019, as the appellant did not submit its return for that quarter until 28 February 2019.

41. The appellants Bank Statement for January 2019, contained within the bundle of documents, still showed it to be some £30,000 overdrawn just over a year and a quarter after the fraud and the thefts from the appellant had been discovered. By that time the appellant had only had one summer season of trading to try to recoup around £200,000 of its previous losses.

THE APPLICABLE LAW

42. It has been established and accepted in case law for some time, that whilst an insufficiency of funds to pay VAT is not a reasonable excuse, the underlying cause of the insufficiency may be a reasonable excuse.

43. In *ETB (2014) Limited v HMRC* [2016] UKUT 0424 (TCC) at [11] the Upper Tribunal referred to the judgment of the Court of Appeal in *Customs and Excise v Steptoe* [1992] STC 757). In that case, the Court of Appeal held that although insufficiency of funds can never of itself constitute a reasonable excuse, the cause of that insufficiency – the underlying cause of the taxpayer's default – might do so. The Upper Tribunal then summarised (at [15]) the test which emerges from the judgment of the majority of the Court of Appeal in *Steptoe* as follows:

“In summary, the question to be asked when considering whether someone has a reasonable excuse for failing to pay an amount of tax on time because of a cash flow problem is whether the insufficiency of funds was reasonably avoidable. A cash flow problem would usually be regarded as reasonably avoidable if the person, having a proper regard for the fact that the tax was due on a particular date, could have avoided the insufficiency of funds by the exercise of reasonable foresight and due diligence. If the cash flow problem was reasonably avoidable then the mere fact that the taxpayer could not afford to pay the VAT at the proper time would not, without more, be a reasonable excuse. On the other hand, if such foresight, diligence and regard would not have avoided the insufficiency of funds then the taxpayer will usually be regarded as having a reasonable excuse for the VAT having been paid late until it would be reasonable to expect the taxpayer to have found alternative funding or taken other action to counteract the insufficiency.”

44. In *Christine Perrin v HMRC* [2018] UKUT 0156 (TCC) at [81] The Upper Tribunal provided guidance to the First Tier Tribunal as follows-

“When considering a “reasonable excuse” defence, therefore, in our view the FTT can usefully approach matters in the following way: (1) First, establish what facts the taxpayer asserts give rise to a reasonable excuse (this may include the belief, acts or omissions of the taxpayer or any other person, the taxpayer’s own experience or relevant attributes, the situation of the taxpayer at any relevant time and any other relevant external facts). (2) Second, decide which of those facts are proven. (3) Third, decide whether, viewed objectively, those proven facts do indeed amount to an objectively reasonable excuse for the default and the time when that objectively reasonable excuse ceased. In doing so, it should take into account the experience and other relevant attributes of the taxpayer and the situation in which the taxpayer found himself at the relevant time or times. It might assist the FTT, in this context, to ask itself the question “was what the taxpayer did (or omitted to do or believed) objectively reasonable for this taxpayer in those circumstances?” (4) Fourth, having decided when any reasonable excuse ceased, decide whether the taxpayer remedied the failure without unreasonable delay after that time (unless, exceptionally, the failure was remedied before the reasonable excuse ceased). In doing so, the FTT should again decide the matter objectively, but taking into account the experience and other relevant attributes of the taxpayer and the situation in which the taxpayer found himself at the relevant time or times.”

DECISION

45. Following this guidance, we have already set out the facts, and those which are proven.

46. In our view, the proven facts of this case, are sufficient to establish that the appellant does have an objectively reasonable excuse for their default. Taking into account the situation in which Mr Cross found the appellant to be in as a result of the fraud, Mr Cross's actions and attention to matters thereafter, and his experience and attributes, we believe that Mr Cross, on behalf of the appellant acted in an objectively reasonable way.

47. Furthermore we find that the effects upon the appellant of the fraud in mid to late 2017, were still in January 2019 directly responsible for the appellant's inability to pay its 01/19 VAT on time. In our view it is entirely reasonable for the appellant not to have recovered financially by January 2019 (ie within 16 months or so) from the significant fraud and theft committed against them, particularly with a seasonal restaurant business and where only one summer season has elapsed.

48. In our judgment, for the reasons we have provided, whilst HMRC validly raised the 01/19 VAT quarter penalty assessment, (as the appellant was mistaken and there was no time to pay agreement in relation to that quarter in place) never-the-less the appellant has established that it has a reasonable excuse for the late payment of VAT for the quarter under appeal.

49. We therefore allow the appeal and dismiss the penalty in the sum of £1,368.13

RIGHT TO APPLY FOR PERMISSION TO APPEAL

43. 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.

**G. NOEL BARRETT
TRIBUNAL PRESIDING MEMBER**

RELEASE DATE: 13 FEBRUARY 2020