



Neutral Citation: [2024] UKFTT 00032 (TC)

Case Number: TC09025

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

By remote video/telephone hearing

Appeal reference: TC/2022/13028

VAT - Default Surcharge – Meaning of Section 108 of the Finance Act 2009 considered - Whether agreement by HMRC to TTP required before payment of VAT due – no – whether approach by taxpayer required before payment of VAT due - yes - Whether reasonable excuse established - no

**Heard on: 14 November 2023
Judgment date: 18 December 2023**

Before

**TRIBUNAL JUDGE DAVID HARKNESS
TRIBUNAL MEMBER GILL HUNTER**

Between

PRACYVA LTD

Appellant

and

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

Respondents

Representation:

For the Appellant: Mr Saleh Ahmed, Londongate Accountancy Limited

For the Respondents: Mr Tony Paterson, litigator, of HM Revenue and Customs' Solicitor's Office

DECISION

INTRODUCTION

1. The hearing took place on 14 November 2023 using the Tribunal's own video hearing system. We heard Mr Saleh Ahmed for the Appellant and Mr Tony Paterson, litigator, of HM Revenue and Customs' solicitor's office, for the Respondents.
2. The documents to which we were referred were a document bundle comprising 109 pages, a 157 page generic bundle of legislation and case law, and a statement of case produced by HMRC of 23 pages. At the hearing we gave directions for the Respondents to make written submissions to us regarding s108 Finance Act 2009 by 28 November 2023 and for the Appellant to have the opportunity to comment on those submissions by no later than 12 December 2023; we subsequently received a submission of 3 pages from the Respondents dated 24 November 2023 (the "Respondents' Written Submission") and a response from the Appellant of two pages dated 7 December 2023 (the "Appellant's Written Submission"). We were grateful to both parties for preparing these written submissions, which were very helpful.
3. Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.
4. The Tribunal decided that:
 - (1) As regards the default surcharge for VAT Period 12/21, in the light of the Respondents' Written Submission that that default surcharge had been cancelled, there was no matter requiring our decision; and
 - (2) As regards the default surcharge for VAT Period 9/21, the appeal should be dismissed.

BACKGROUND

5. The Appellant ("Pracyva") appeals against VAT default surcharges issued by HMRC pursuant to s.59 Value Added Tax Act 1994 ("VATA") in respect of Pracyva's VAT periods ended 09/21 (in the amount of £32,164.12) and 12/21 (in the amount of £41,116.73).
6. As regards the default surcharge for VAT Period 12/21, in the light of the Respondents' Written Submission that that default surcharge had been cancelled, there was no matter requiring our decision.

Background facts

7. We find the following background facts which were not disputed by Pracyva:
 - (1) Pracyva is an IT consulting business first registered for VAT in June 2018;
 - (2) Pracyva submits VAT Returns on a quarterly basis;
 - (3) Period 3/19 covered the period to 31 March 2019. The due date for the VAT return and payment was 7 May 2019. The return was received on 15 May 2019. The VAT was paid to HMRC in part on 3 April 2020 and the remainder on 7 May 2020;
 - (4) Period 6/19 covered the period to 30 June 2019. The due date for the VAT return and payment was 7 August 2019. The return was received on that date. The VAT was paid to HMRC in parts, the first of which was on 14 February 2020 and last of which was on 12 February 2021;

- (5) Period 6/20 covered the period to 30 June 2020. The due date for the VAT return and payment was 7 August 2020. The return was received on 17 August 2020. The VAT was paid to HMRC in part on 12 February 2021 and the remainder on 13 March 2021;
- (6) Period 9/20 covered the period to 30 September 2020. The due date for the VAT return and payment was 7 November 2020. The return was received on that date. The VAT was paid to HMRC in parts, starting on 14 April 2021 and finishing on 28 October 2021;
- (7) Period 12/20 covered the period to 31 December 2020. The due date for the VAT return and payment was 7 February 2021. The return was received on 6 February 2021. The VAT was paid to HMRC on 6 May 2022;
- (8) Period 9/21 covered the period to 30 September 2021. The due date for the VAT return and payment was 7 November 2021. The return was received on 4 November 2021. The VAT was paid to HMRC in part on 1 September 2022 and the remainder on 29 September 2022;
- (9) Period 12/21 covered the period to 31 December 2021. The due date for the VAT return and payment was 7 February 2022. The return was received on 3 February 2022. The VAT was paid to HMRC in parts starting on 8 February 2022 and finishing on 30 December 2022;
- (10) On 8 November 2021 (i.e. the day after the VAT for period 9/21 was due to have been paid), an approach was made to HMRC by the Appellant seeking a time to pay (“TTP”) agreement for outstanding PAYE and VAT. A TTP in respect of that aggregate amount was later agreed (further detail on this issue is set out below);
- (11) Pracyva was issued with Surcharge Liability Notices and/or Surcharge Liability Notices of Extension in relation to these periods and accordingly became liable to a surcharge in respect of period 9/21;
- (12) HMRC initially charged a default surcharge in respect of period 12/21, but subsequently in the Respondents’ Written Submission that surcharge was cancelled;
- (13) Pracyva did not dispute that the Surcharge Assessment for period 9/21 was validly issued and correctly calculated in the amount of £32,164.12.

ISSUES FOR CONSIDERATION

8. Given these findings, in particular 4 (8), (10), (11) and (13), the principal questions were therefore whether s108 Finance Act 2009 (“FA 2009”) operated so as to relieve the surcharge in respect of the period 9/21 and, if not, if Pracyva had a reasonable excuse within the meaning of section 59(7) VATA for the default in timely payment of VAT in respect of the period 9/21.

FACTS RELEVANT TO THESE ISSUES

9. Mr Amit Warwatkar, a director of Pracyva, gave evidence on behalf of Pracyva. We found that Mr Warwatkar was a patently truthful and honest witness. We accepted his evidence which was not challenged by HMRC. Mr Warwatkar’s evidence was that:

- (1) He, his brother and his wife are the three directors of Pracyva. Mr Warwatkar is the chief executive and in charge of finance, one other director overseeing product delivery and the third being part time and providing support as needed;
- (2) At the relevant time Pracyva had some 89 consultants in the UK and 37 outside the UK. There was a three member finance team;

(3) As a result of the Covid pandemic and the move to digital working, Pracyva's business had expanded rapidly in 2020 and 2021 but this had posed various difficulties for the firm. Pracyva had needed to make significant investments in order to scale up its business to cope with the increased demand. Pracyva had experienced cash flow problems – its typical business model was to be paid upon the achievement of project milestones but owing to cashflow problems with its clients, the typical time for payment of invoices had stretched from 45-60 days pre pandemic to more than 120 days. These cashflow problems made it difficult for Pracyva to pay its VAT liabilities on time;

(4) Problems had also been caused by Covid related sickness which had affected the directors, their families and staff and their families. Mr Warwatkar and his family had suffered from Covid. Mr Warwatkar had to travel to India twice to attend to his mother who had contracted Covid. Mr Warwatkar himself contracted Covid and was hospitalised and remained unwell until 31 March 2022, suffering complications owing to underlying health issues. These problems meant that Mr Warwatkar was unable to manage the business with his normal diligence due to concerns over his parents' health and his own health issues;

(5) In order to get reliable information as to the timetable for Pracyva's clients to pay it, Mr Warwatkar had to make contact at a senior level with Pracyva's clients in the latter part of 2021 and early part of 2022. At that time it was difficult to get hold of senior staff at Pracyva's clients in a timely manner;

(6) VAT returns are prepared by an external adviser (Mr Ahmed) based on information submitted by Pracyva, approved by Mr Warwatkar, and then submitted by Mr Ahmed. Mr Ahmed is not involved in the actual payment of VAT or of discussions with HMRC;

(7) While some routine contact with HMRC might be made by the Pracyva finance team, any major matters were dealt with personally by Mr Warwatkar.

10. We found the following further facts based on evidence presented by HMRC which was not challenged by Pracyva:

(1) A TTP arrangement covering outstanding balances for both PAYE and VAT had been in place during 2021 and Mr Warwatkar contacted HMRC by telephone regarding this on 28 October 2021 to explain that he would like to agree a new TTP covering a larger balance. He was advised that a new TTP could not be agreed while a current plan was running and accordingly had paid the amount outstanding on the existing plan;

(2) Because the amount of PAYE owing was unclear and a revised PAYE return was to be submitted no request for a new TTP was made on the 28 October telephone call;

(3) On that call Mr Warwatkar was told that there remained outstanding debts and that these may give rise to penalties;

(4) On 8 November 2021 (i.e. the day after the VAT for period 9/21 was due to have been paid), Mr Warwatkar called HMRC to seek a TTP for the revised outstanding PAYE and VAT debt (the PAYE amount having been revised). A TTP in respect of that aggregate amount was later agreed;

(5) On at least one occasion a director other than Mr Warwatkar had been involved in a payment to HMRC (Mrs Barwankar in July 2021).

11. In relation to the question of when a request for deferral was made by Pracyva, that in the Appellant's Written Submission it was stated that the relevant deferral request was made

on 8 November 2021. Accordingly Pracyva accepts that that was the date the deferral request was made.

12. Based on these facts, we considered that application of s108 FA 2009 and whether Pracyva had a reasonable excuse under s59(7) VATA.

CONSIDERATION

Section 108

13. The relevant parts of s108 FA 2009 provide:

“(1) This section applies if—

(a) a person (“P”) fails to pay an amount of tax falling within the Table in subsection (5) when it becomes due and payable,

(b) P makes a request to an officer of Revenue and Customs that payment of the amount of tax be deferred, and

(c) an officer of Revenue and Customs agrees that payment of that amount may be deferred for a period (“the deferral period”).

(2) P is not liable to a penalty for failing to pay the amount mentioned in subsection (1) if—

(a) the penalty falls within the Table, and

(b) P would (apart from this subsection) become liable to it between the date on which P makes the request and the end of the deferral period.

(3) But if—

(a) P breaks the agreement (see subsection (4)), and

(b) an officer of Revenue and Customs serves on P a notice specifying any penalty to which P would become liable apart from subsection (2), P becomes liable, at the date of the notice, to that penalty.

(4) P breaks an agreement if—

(a) P fails to pay the amount of tax in question when the deferral period ends, or

(b) the deferral is subject to P complying with a condition (including a condition that part of the amount be paid during the deferral period) and P fails to comply with it.”

14. In other words a taxpayer is not liable to a default surcharge for a period where contact is made with HMRC prior to the due date in order to arrange a payment deferment and this is subsequently agreed by HMRC. There is a contrast between s108(1) which provides for the overall application of the section and includes a requirement that HMRC agrees to the payment deferral and s108(2) which provides that certain penalties are not due where the taxpayer “would (apart from this subsection) become liable to [the penalty] **between the date on which [the taxpayer] makes the request** and the end of the deferral period” (emphasis added). It seemed to us clear from this that if a taxpayer approaches HMRC to ask for time to pay a sum (call it the principal sum) before the due date for a penalty and HMRC subsequently agree to the deferral of the principal sum, then a penalty due in respect of a failure to pay triggered on a date **after** the approach is not due, even if HMRC’s agreement to the deferral is itself after the due date. The critical event is that the taxpayer makes a request before the due date. At the hearing the Respondents did not accept this, but later conceded

the point in the Respondents' Written Submission and accepted that the effect of s108(2) is that a taxpayer is not liable to a penalty in respect of failure to make a payment on a particular date if a request to defer payment of an amount is made by the taxpayer to HMRC before that date even if HMRC do not agree to that deferral until after that date.

15. The effect of this concession by the Respondents was that the default surcharge for Period 12/21 should have been suspended because the Appellant had approached HMRC for a TTP on the date the VAT was due (i.e. before the surcharge had arisen) and a TTP had subsequently been agreed in respect of the amounts due. Because Pracyva had complied with the TTP that was agreed in respect of the amounts due, the Respondents ought subsequently to have cancelled that default surcharge in respect of that period. The Respondents therefore were correct in our view to cancel this surcharge for period 12/21.

16. In the Appellant's Written Submission, Pracyva sought to go further and argued that if a deferral request is made *at any time* by a taxpayer and a TTP agreed by HMRC, that deferral request operates to relieve a taxpayer from a default surcharge accrued before the request was made. Pracyva based this submission on s108(1)(b) which it was argued merely states that a deferral request needs to have been made by the taxpayer. Pracyva's argument was that if a TTP is sought and agreed, then it applies to discharge default surcharges incurred before the TTP is sought. We do not think that argument is correct. The effect of s108(1) is simply to set out the conditions for the application of the remainder of the section, namely that the section applies if a person fails to pay an amount of tax falling within the table (set out in s108(5)) when due and the person makes a request for deferral which request HMRC accept. It is the application of s108(2) that relieves penalties by providing that a person is not liable to a penalty if the penalty falls within the table and the person would otherwise be liable to the penalty between the date on which the person makes a deferral request to HMRC and the end of the deferral period. If a penalty has already become due when a request for deferral is made, then s108 cannot discharge the penalty.

17. Unfortunately for Pracyva, we found as a fact that Mr Warwatkar approached HMRC to ask for time to pay in respect of the 9/21 period on 8 November (after the due date). So it follows that s108 cannot apply. The penalties were due on a date before the day of the approach. We carefully considered the evidence of the contact between Mr Warwatkar and HMRC immediately before 7 November 2021 (in particular a call between Mr Warwatkar and HMRC on 28 October) but, as noted above, we found as a fact that there was no request to defer payment until 8 November 2021. Accordingly, s108 did not operate to discharge the penalty due for the failure to pay for period 9/21.

18. We went on to consider the question of reasonable excuse.

Reasonable Excuse

19. A taxpayer may avoid a penalty if they have a reasonable excuse. There is no statutory definition of a "reasonable excuse". Whether or not a person has a reasonable excuse is an objective test and is a matter to be considered in the light of all of the circumstances of the particular case: *Rowland v R & C Commrs* (2006) Sp C 548 ("*Rowland*"), at [19].

20. We approached the question of a reasonable excuse in line with the Upper Tribunal decision in *Perrin v HMRC* [2018] UKUT 156 (TCC) ("*Perrin*"). At [75], the Upper Tribunal concluded that the FTT in that case had correctly stated that "to be a reasonable excuse, the excuse must not only be genuine, but also objectively reasonable when the circumstances and attributes of the actual taxpayer are taken into account." The Upper Tribunal set out helpful guidance as to how the FTT should approach the issue of reasonable excuse at [81] of *Perrin* 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?”

21. We also considered the decision of the VAT Tribunal in *The Clean Car Co Ltd v Customs and Excise Commissioners* [1991] VATTR 234. In that case, HH Judge Medd QC held:

“... 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 in at the relevant time, a reasonable thing to do? Put in another way which does not I think alter the sense of the question: was what the taxpayer did not an unreasonable thing for a trader of the sort I have envisaged, in the position the taxpayer found himself, to do? ... It seems to me that Parliament in passing this legislation must have intended that the question of whether a particular trader had a reasonable excuse should be judged by the standards of reasonableness which one would expect to be exhibited by a taxpayer who had a responsible attitude to his duties as a taxpayer, but who in other respects shared such attributes of the particular appellant as the tribunal considered relevant to the situation being considered. Thus though such a taxpayer would give a reasonable priority to complying with his duties in regard to tax and would conscientiously seek to ensure that his returns were accurate and made timeously, his age and experience, his health or the incidence of some particular difficulty or misfortune and, doubtless, many other facts, may all have a bearing on whether, in acting as he did, he acted reasonably and so had a reasonable excuse.”

22. The burden of proof was on the Appellant to demonstrate there is a reasonable excuse on the balance of probabilities.

23. Applying the approach of *Perrin*, we sought to (1) establish what facts the taxpayer asserts give rise to a reasonable excuse, (2) decide which of those facts are proven (3) decide whether, viewed objectively, those proven facts do indeed amount to an objectively reasonable excuse for the default. In relation to (3) we considered the experience and other relevant attributes of the taxpayer and the situation in which the taxpayer found themselves at the relevant time. We asked ourselves whether what the taxpayer did (or omitted to do or believed) was objectively reasonable for this taxpayer in those circumstances?

24. The facts relied upon by Pracyva are set out above but in summary were that:

- (1) In relation to period 9/21, on behalf of Pracyva Mr Warwatkar had approached HMRC on 8 November for a time to pay agreement which he believed would cover the amount due on 7 November 2021;
- (2) Pracyva had cashflow problems;
- (3) Mr Warwatkar had health and family issues that made it difficult for him to run the business properly at this time;
- (4) Overall business conditions caused by Covid meant it was more difficult to manage the business than usual;
- (5) The approach to HMRC for a TTP arrangement for period 9/21 was made only one day after the VAT due date (this was an additional point raised in the Appellant's Written Submission).

25. We found those facts to be proven, so we then considered if those facts amounted to a reasonable excuse.

26. We are extremely sympathetic to Mr Warwatkar and his family's health difficulties and can well understand that they played a part in the failure to pay VAT on time. We are also admiring of the efforts Mr Warwatkar made to run and expand his business in difficult circumstances.

27. However, considering the question of whether the facts advanced by Pracyva amounted to a reasonable excuse for the defaults, we found:

- (1) That Mr Warwatkar's belief in November 2021 that HMRC would give time to pay did not amount to an objectively reasonable excuse;
- (2) Approaching HMRC for a TTP arrangement one day after the VAT due date cannot amount to a reasonable excuse for failing to pay the VAT due the day before the approach;
- (3) Because of section s.71 VATA (insufficiency of funds to pay VAT is not a reasonable excuse), Pracyva's cashflow problems and uncertainty about when its customers would pay, do not amount to a reasonable excuse;
- (4) We accept that Mr Warwatkar had significant health and family problems and that the overall business conditions caused by Covid meant it was more difficult to manage the business than usual in 2021. Nevertheless, judged objectively, we do not consider that these problems amounted to a reasonable excuse for the default. In particular (a) in spite of a significant number of staff being employed by Pracyva (including a three person finance team) no contingency plan seems to have been put in place for a second point of contact with HMRC in the event of Mr Warwatkar not being available, (b) a second director had had contact with HMRC in 2021 and presumably could have been tasked to undertake that contact again, (c) the Covid pandemic had been going on since March 2020 and a reasonable taxpayer would have been expected to be prepared for the difficulties in which Pracyva found itself by the time of this default.
- (5) As for the assertion made on behalf of Pracyva (which we did not find proven) that Pracyva had a positive record on TTP arrangements historically, we did not consider this could amount to a reasonable excuse for the default even if we had found it proven.

28. In relation to Pracyva's cashflow problems, we considered *Customs & Excise Commrs v Steptoe* (1992) STC 757 ("*Steptoe*"), where the Court of Appeal held that notwithstanding

s71 VATA (which provides that an insufficiency of funds can never of itself constitute a reasonable excuse), the reasons for an insufficiency of funds might do so. In the case of a default occasioned by an insufficiency of funds, Lord Donaldson MR indicated 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.”

29. In *Stepto*, the taxpayer argued that although the immediate cause of the default was shortage of funds and therefore could not be a reasonable excuse, the underlying cause of that shortage did amount to a reasonable excuse. The court determined that a trader might have a reasonable excuse in relation to an insufficiency of funds if it were caused by an unforeseeable or inescapable event or when, despite the exercise of reasonable foresight and due diligence, it could not have been avoided. We considered whether the reasons for Pracyva’s insufficiency of funds, or the underlying cause of the default, might constitute a reasonable excuse in Pracyva’s circumstances. While we accept that trading conditions were challenging for Pracyva because customers were paying more slowly than usual, that is a normal (if unwelcome) incidence of doing business rather than something unforeseeable or inescapable that could not have been avoided by the exercise of reasonable foresight.

30. We therefore found that those facts did not amount to a reasonable excuse for the defaults.

CONCLUSION

31. Accordingly, we dismiss the appeal as regards the default surcharge for VAT Period 9/21.

32. As regards the default surcharge for VAT Period 12/21, in the light of the Respondents’ Written Submission that that default surcharge had been cancelled, there was no matter requiring our decision.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

33. 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.

**DAVID HARKNESS
TRIBUNAL JUDGE**

Release date: 18th DECEMBER 2023