



**TC03335**

**Appeals numbers: TC/2012/06507 & TC/2013/03009**

*VAT – default surcharges – s 59 VATA 1994 – whether reasonable excuse – whether disproportionate - appeals dismissed*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**EURO ARCHITECTURAL HARDWARE LIMITED      Appellant**

**- and -**

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

**TRIBUNAL: JUDGE PETER KEMPSTER  
MR WILL SILSBY**

**Sitting in public at Priory Courts, Birmingham on 8 January 2014**

**The Appellant did not appear and was not represented**

**Ms Lisa Taylor (HMRC Appeals Unit) for the Respondents**

## DECISION

1. The Appellant appeals against default surcharges imposed pursuant to s 59 VAT Act 1994 in respect of its VAT periods 02/12 and 11/12.

2. Prior to the hearing the Appellant wrote to the Tribunal to apologise for being unable to attend the hearing but requesting that the hearing take place in its absence. The Tribunal considered the Appellant's case was clearly stated in its grounds of appeal and thus the hearing should proceed.

### 10 **Legislation**

3. Section 59 VAT Act 1994 provides for default surcharges for late submission of VAT returns and/or late payment of VAT.

#### **“59 The default surcharge**

(1) Subject to subsection (1A) below, if, by the last day on which a taxable person is required in accordance with regulations under this Act to furnish a return for a prescribed accounting period—

(a) the Commissioners have not received that return, or

(b) the Commissioners have received that return but have not received the amount of VAT shown on the return as payable by him in respect of that period,

then that person shall be regarded for the purposes of this section as being in default in respect of that period.

(1A) A person shall not be regarded for the purposes of this section as being in default in respect of any prescribed accounting period if that period is one in respect of which he is required by virtue of any order under section 28 to make any payment on account of VAT.

(2) Subject to subsections (9) and (10) below, subsection (4) below applies in any case where—

(a) a taxable person is in default in respect of a prescribed accounting period; and

(b) the Commissioners serve notice on the taxable person (a “surcharge liability notice”) specifying as a surcharge period for the purposes of this section a period ending on the first anniversary of the last day of the period referred to in paragraph (a) above and beginning, subject to subsection (3) below, on the date of the notice.

(3) If a surcharge liability notice is served by reason of a default in respect of a prescribed accounting period and that period ends at or before the expiry of an existing surcharge period already notified to the taxable person concerned, the surcharge period specified in that notice shall be expressed as a continuation of the existing surcharge period and, accordingly, for the purposes of this section, that existing period and its extension shall be regarded as a single surcharge period.

(4) Subject to subsections (7) to (10) below, if a taxable person on whom a surcharge liability notice has been served—

(a) is in default in respect of a prescribed accounting period ending within the surcharge period specified in (or extended by) that notice, and

(b) has outstanding VAT for that prescribed accounting period, he shall be liable to a surcharge equal to whichever is the greater of the following, namely, the specified percentage of his outstanding VAT for that prescribed accounting period and £30.

(5) Subject to subsections (7) to (10) below, the specified percentage referred to in subsection (4) above shall be determined in relation to a prescribed accounting period by reference to the number of such periods in respect of which the taxable person is in default during the surcharge period and for which he has outstanding VAT, so that—

(a) in relation to the first such prescribed accounting period, the specified percentage is 2 per cent;

(b) in relation to the second such period, the specified percentage is 5 per cent;

(c) in relation to the third such period, the specified percentage is 10 per cent; and

(d) in relation to each such period after the third, the specified percentage is 15 per cent.

(6) For the purposes of subsections (4) and (5) above a person has outstanding VAT for a prescribed accounting period if some or all of the VAT for which he is liable in respect of that period has not been paid by the last day on which he is required (as mentioned in subsection (1) above) to make a return for that period; and the reference in subsection (4) above to a person's outstanding VAT for a prescribed accounting period is to so much of the VAT for which he is so liable as has not been paid by that day.

(7) If a person who, apart from this subsection, would be liable to a surcharge under subsection (4) above satisfies the Commissioners or, on appeal, a tribunal that, in the case of a default which is material to the surcharge—

(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,

he shall not be liable to the surcharge and for the purposes of the preceding provisions of this section he shall be treated as not having been in default in respect of the prescribed accounting period in question (and, accordingly, any surcharge liability notice the service of which depended upon that default shall be deemed not to have been served).

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

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

5 (b) it is a default which was taken into account in the service of the surcharge liability notice upon which the surcharge depends and the person concerned has not previously been liable to a surcharge in respect of a prescribed accounting period ending within the surcharge period specified in or extended by that notice.

10 (9) In any case where—

(a) the conduct by virtue of which a person is in default in respect of a prescribed accounting period is also conduct falling within section 69(1), and

15 (b) by reason of that conduct, the person concerned is assessed to a penalty under that section,

the default shall be left out of account for the purposes of subsections (2) to (5) above.

20 (10) If the Commissioners, after consultation with the Treasury, so direct, a default in respect of a prescribed accounting period specified in the direction shall be left out of account for the purposes of subsections (2) to (5) above.

(11) For the purposes of this section references to a thing's being done by any day include references to its being done on that day.”

25 4. Section 71 VAT Act 1994 construes “reasonable excuse” for the purposes of s 59:

**“71 Construction of sections 59 to 70**

(1) For the purpose of any provision of sections 59 to 70 which refers to a reasonable excuse for any conduct—

30 (a) an insufficiency of funds to pay any VAT due is not a reasonable excuse; and

(b) where reliance is placed on any other 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.

35 (2) In relation to a prescribed accounting period, any reference in sections 59 to 69 to credit for input tax includes a reference to any sum which, in a return for that period, is claimed as a deduction from VAT due.”

**Appellant’s Case**

5. In relation to the 02/12 period:

40 (1) The company had been badly affected by the economic recession, which had had particularly serious effects on the construction industry. Customer

orders had fallen. Staff redundancies had been made. Huge banking costs were being incurred to keep the company afloat. The surcharge could not be afforded.

5 (2) The company had requested a time-to-pay agreement but HMRC had refused this. The VAT had been paid in full by instalments.

6. In relation to the 11/12 period:

(1) The same factors as set out at paragraph 5(1) above.

(2) The company had again requested a time-to-pay agreement but HMRC had refused this also.

10 (3) Four customers had entered liquidation owing the company around £28,500.

(4) The company's bank had withdrawn its debt factoring arrangements and overdraft facility, and these had had to be renegotiated and replaced.

(5) Suppliers had changed their terms and now required payment with order.

15 (6) The amount of the surcharge was excessive, especially for a struggling company.

### **Respondents' Case**

7. The surcharge in respect of the 02/12 period had been reduced by HMRC from £2,850.15 to £1,425.07 (by letter dated 4 October 2012). There was no dispute that  
20 the relevant payments were late; nor that the relevant surcharge notices had been properly issued; nor that the calculations were correct.

8. The company had a history of time-to-pay requests dating back to 2008. That indicated that the cashflow problems were longstanding. Time-to-pay arrangements had been agreed by HMRC for every quarter over a two year period; such  
25 arrangements were designed only to be a short term remedy and could not be relied upon as an alternative to the company making adequate payment arrangements. That was why the requests had been refused for the two periods under appeal. The request in relation to the 11/12 period had not been made until the day after the due date, and although payment in full had been promised for 18 January, that had not been  
30 honoured.

9. Although HMRC were sympathetic to the difficult trading conditions – as witnessed by the extensive time-to-pay arrangements granted in the past – there was no indication that these were worse for the Appellant than for many other taxpayers who did pay their liabilities on time. For example, suppliers were generally  
35 tightening their credit terms.

10. The Appellant had confirmed in correspondence (letter 19 July 2013) that the change in the banking terms and invoice factoring dated back to summer 2009; that was not a recent development that might explain the defaults in 2012.

11. In relation to the bad debts, the schedules produced by the Appellant indicated that the bad debts in relation to the 02/12 period were only £434, which was immaterial to the company's ability to pay its VAT on time. The bank statements provided demonstrated that the company did have sufficient funds on the relevant date to pay the VAT liability. Although the bad debts in relation to the 11/12 period were larger, they still represented less than one per cent of the company's turnover, and so again were immaterial to the company's ability to pay its VAT on time.

12. The size of the surcharge was determined by legislation, and was not disproportionate: *HMRC v Total Technology (Engineering) Ltd* [2013] STC 681

## 10 Consideration and Conclusions

13. We take the Appellant's arguments as falling under two heads: reasonable excuse and proportionality.

14. *Reasonable excuse* – Although insufficiency of funds is itself prohibited from constituting a reasonable excuse for late payment (see s 71(1)(a)), we have examined whether there was some cause of that insufficiency that might be construed as a reasonable excuse. Although we are sympathetic to the financial problems faced by the Appellant, we cannot find (even after careful scrutiny of the bank statements and other documentation provided by the Appellant) that there was any particular event or events that might reasonably explain the late payment of the VAT liabilities. On the basis of the evidence provided to the Tribunal we cannot conclude that there was any reasonable excuse for either late payment.

15. *Proportionality* – We consider the Upper Tribunal decision in *Total Technology v HMRC* [2013] STC 681 (which is binding on this Tribunal) is clear that the general system of s 59 surcharges is not disproportionate. On the particular surcharge assessed on the Company, the Upper Tribunal stated (at [99]):

“In our judgment, there is nothing in the VAT default surcharge which leads us to the conclusion that its architecture is fatally flawed. There are, however, some aspects of it which may lead to the conclusion that, on the facts of a particular case, the penalty is disproportionate. But in assessing whether the penalty in any particular case is disproportionate, the tribunal must be astute not to substitute its own view of what is fair for the penalty which Parliament has imposed. It is right that the tribunal should show the greatest deference to the will of Parliament when considering a penalty regime just as it does in relation to legislation in the fields of social and economic policy which impact upon an individual's convention rights. The freedom which Parliament has in establishing the appropriate penalties is not, we think, necessarily exactly the same as the freedom which it has in accordance with its margin of appreciation in relation to convention rights (and even there, as we have explained, the margin of appreciation will vary depending on the right engaged).”

We cannot rule these surcharges disproportionate, given that it is an aggregate penalty of around £5,500 for two defaults within nine months, in relation to a taxpayer with annual turnover in excess of three million pounds.

**Decision**

5 16. The Tribunal decided that the appeals are DISMISSED.

17. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to “Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)” which accompanies and forms part of this decision notice.

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**PETER KEMPSTER  
TRIBUNAL JUDGE**

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**RELEASE DATE: 10 February 2014**