



TC03831

Appeal number: TC/2012/09647

VAT default surcharge - insufficiency of funds - HMRC refused a time to pay arrangement - whether reasonable excuse - no - Appeal dismissed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

COCHRAN STREET SOCIAL CLUB LTD

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE MICHAEL S CONNELL
MR WARREN SNOWDON**

**Sitting in public at King's Court Royal Quays Earl Grey Way North Shields
NE29 6AR on 19 May 2014**

Mr S Nicholson Club Secretary and Mrs J Allen of the Appellant Company

Mrs R Oliver, Officer of HM Revenue and Customs, for the Respondents

DECISION

The Appeal

5 1. Cochran Street Social Club Limited (“the Appellant”) appeals against default surcharges imposed for its failure to make quarterly VAT Returns and/or payment of VAT by the due dates for the quarters ended, 09/11, 12/11, 03/12, and 06/12.

2. The point at issue is whether or not the Appellant has a reasonable excuse for making late payments.

Background

10 3. The Appellant had previously defaulted on VAT payments in period 12/10 when a VAT surcharge liability notice was issued and again on 03/11 and 06/12 prior to the default periods under appeal.

15 4. 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].

5. The Appellant’s returns were late in each period under appeal apart from 09/11. The VAT due under the 09/11 and 12/11 periods was paid late and the VAT due under the 03/12 and 06/12 periods remained outstanding at the date of this appeal.

20 6. Section 59 Value Added Tax Act 1994 (“VATA”) 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. The Commissioners may then serve a surcharge liability notice on the defaulting taxable person, which brings him within the default
25 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
30 to the first default the specified percentage is 2%. The percentage ascends to 5%, 10% and 15% for the second, third and fourth default.

35 7. A trader's liability to surcharge expires if all the returns and payments for tax periods ending on or before the end of the period covered by the Surcharge Liability Notice (SLN) or Surcharge Liability Notice Extension (SLNE) are received on time. This means that four quarterly returns and payments need to be made on time to exit the surcharge system.

8. Each SLN or SLNE is sent with notes advising what a default is and what will happen within a default period.

9. The notes also advise the trader to contact the local Debt Management Unit if they expect to have difficulty paying VAT on time.

10. 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 : -

10 ‘(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 –

(b) there is a reasonable excuse for the return of VAT not having been so despatched then

15 - 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 ..’

11. The burden falls on the Appellant to establish that it has a reasonable excuse for the late payment in question.

20 12. 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 is not reasonable excuse.’

25 13. Although an insufficiency of funds to pay any VAT due is not a reasonable excuse, the underlying cause of any insufficiency of funds if entirely unforeseen and outside the control of the taxpayer, may constitute a reasonable excuse.

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

Appellant’s Case

15. The Appellant does not dispute that its VAT returns were late in each default period, nor that the amounts due remain outstanding.

35 16. Mr Nicholson, the club secretary, in the Appellant’s notice of appeal to the Tribunal said that the club had on numerous occasions attempted to set up a payment plan with HMRC. He said that the Appellant had contacted HMRC prior to the due date of payment for each return and had offered to discharge the arrears of VAT by entering into a time to pay arrangement.

17. Mr Nicholson said that the club, like all other licensed businesses, was suffering financially from the recession and that it was difficult to understand why HMRC refused to accept a payment plan when the club could not afford to pay the full amount due. The alternative was that the club would pay nothing. Mr Nicholson said
5 that the club had traded very poorly since 2010 and nearly closed in 2011. The club owed money to its landlord and the brewery. It was unable to secure any further lending facilities from its bank.

18. Mrs Allen, the club's bookkeeper, said that the club could not afford to pay the VAT surcharges and in fact was struggling to pay the outstanding VAT, which
10 totalled £11,817. More recent VAT due to HMRC was also outstanding. She estimated that the total due was approximately £17,500. She agreed that the club was a cash business and that the VAT should not have been used as part of the club's cash flow. She said that if the surcharges were confirmed and if HMRC did not allow the club to enter into a time to pay arrangement it would, in all likelihood, have to be
15 wound up.

19. Mrs Allen said that the club's payment plan has not been accepted by HMRC whereas other businesses in a similar position have been allowed time to pay arrangements. She said that it appeared to be a lottery as to whether HMRC allowed time to pay and this was unreasonable.

20 HMRC's Case

20. The potential financial consequences attached to the risk of further default would have been known to the Appellant after issue of the Surcharge Liability Notice for the period 12/10, given the information contained in the Notice. Included within the notes on the reverse of the Surcharge Liability Notice, is the following, standard, paragraph:

25 'Please remember: Your VAT returns and any tax due must reach HMRC by the due date. If you expect to have any difficulties contact either your local VAT office, listed under HM Revenue & Customs in the phone book as soon as possible, or the National Advice Service on 0845 010 9000.'

30 21. The requirements for submitting timely electronic payments can also be found -

- In notice 700 "the VAT guide" paragraph 21.3.1 which is issued to every trader upon registration.
- On the actual website www.hmrc.gov.uk
- On the E-VAT return acknowledgement.

35 22. Also the reverse of each default notice details how surcharges are calculated and the percentages used in determining any financial surcharge in accordance with the VAT Act 1994 s 59(5).

23. It is also specifically stated in s 71(1) VATA 1994 that any insufficiency of funds to pay any VAT is not reasonable excuse. The underlying cause for insufficiency of

funds may amount to a reasonable excuse if the trader can demonstrate that the circumstances that led to the loss of income and subsequent defaults were unforeseen and outside his influence and control.

5 24. Mrs Oliver for HMRC said that in order to establish a reasonable excuse, a trader must have evidence that his circumstances fall outside the normal risks of his particular business or that there was a misfortune that was unforeseeable and could not be prevented or avoided. That is not the position in this case. The Appellant club has been struggling financially for a number of years and the default in each quarter under appeal was entirely foreseeable.

10 25. It was not unreasonable for HMRC to reject the Appellant's payment proposals, which were considered to be entirely unrealistic. The Appellant had not demonstrated an ability to pay VAT as and when it fell due, and therefore there was little prospect of it being able to adhere to a payment plan which involved payment of historic outstanding VAT. Time to pay arrangements were entirely within the discretion of
15 HMRC and there had to be a realistic prospect of the taxpayer being able to recover from its financial difficulties and to repay all outstanding VAT due within a reasonable period.

26. Therefore HMRC say that the surcharge has been correctly issued in accordance with the VAT Act 1994 s 59(4).

20 Conclusion

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

28. Essentially the Appellant's grounds of appeal are that it is suffering a cash flow shortage caused by the recession and difficult trading conditions. It says that HMRC
25 should have allowed it to enter into a time to pay arrangement and that it therefore has a reasonable excuse for the defaults.

29. To decide whether a reasonable excuse exists where insufficiency of funds causes the failure the Tribunal must take for comparison a person in a similar situation to that of the actual taxpayer who is relying on the reasonable excuse defence. The Tribunal
30 should then ask itself, with that comparable person in mind, whether notwithstanding that person's exercise of reasonable foresight, due diligence and a proper regard for the fact that the tax would become payable on the particular dates, those factors would not have avoided the insufficiency of funds which led to the failures.

30. Plainly, the cause of the defaults was not an unforeseen event outside the control
35 of the Appellant. The Appellant has suffered poor trading conditions for some time and has been using the VAT as part of its cash flow. It has gradually slid into serious financial difficulties from which it is hard to see how it might recover. It was not unreasonable for HMRC to refuse a time to pay arrangement when it was clear that there was little prospect of the Appellant clearing its indebtedness within a reasonable
40 period.

31. The burden of proof is on the Appellant to show a reasonable excuse for the late VAT payments. In the Tribunal's view, for the reasons given above, that burden has not been discharged and there was no reasonable excuse for the defaults under appeal.

32. The appeal is accordingly dismissed and the surcharges upheld.

5 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
10 "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

MICHAEL S CONNELL

15

TRIBUNAL JUDGE

RELEASE DATE: 22 July 2014