TC01687

Appeal number: TC/2011/6310

PAYE late payment penalty – Sch 56 FA 2009 – Whether a reasonable excuse or other statutory defence – Whether penalty disproportionate or otherwise unfair – Appeal allowed in part

FIRST-TIER TRIBUNAL

TAX

M&B PRECISION ENGINEERING (LEICESTER) LIMITED
Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS
Respondents

TRIBUNAL: Judge Peter Kempster
Mrs Maryvonne Hands

Sitting in public at Kings Court, Leicester on 8 November 2011

Mr Moulding (Director) for the Appellant

Mrs Walker (HMRC Appeals Unit) for the Respondents

DECISION

1. By a notice of appeal dated 11 August 2011 the Appellant ("the Company") appealed against a decision letter from the Respondents ("HMRC") dated 22 July 2011 confirming a PAYE late payment penalty for the tax year 2010-11 in the amount of £5,321.45.

2. With effect from April 2010 sch 56 FA 2009 introduced a new regime of penalties for late payment of PAYE by employers. The new regime is considerably more stringent than its predecessor. In summary, a tax-geared penalty is charged which depends on the number of failures, other than the first, in a tax year. Where there are ten or more failures, other than the first, in a tax year then the penalty is 4% of the late paid PAYE (para 6 sch 56).

3. The Company accepts that the PAYE was paid late every month and that the amount of the penalty has been correctly calculated. HMRC's schedule of payments shows that during 2010-11 the payments were, with the exception of one month, made 8 to 12 days late. In the previous year (before the new penalty regime) the payments were, again with the exception of one month, made 20 to 29 days late. In the current tax year the Company has (apart from the first month) paid on time.

4. Mr Moulding for the Company made the following submissions:

(1) The Company has had financial difficulties over the last two years. It was created by incorporation of a former unincorporated business which had been trading for 35 years and this change of status resulted in accelerated tax payments in excess of £250,000, all of which had been paid in accordance with a time-to-pay agreement reached with HMRC.

(2) Although PAYE was paid a few days late every month, there was no intention to avoid or evade payment and everything was now up-to-date.

(3) The Company had thought all was well. Although it received tax demands in May and July 2010 these showed a trivial amount due in respect of the tax year 2009-10, which was accountable by an HMRC error for not crediting an allowance for online filing (plus interest). The Company was not warned of the consequences of its late PAYE payments. Had it known of the serious penalties then it would have paid earlier – as it had done in the current tax year. It was unfair for HMRC to allow the Company to go the whole year accumulating penalties when HMRC knew the Company would be expensively punished.

(4) The Company was a small business drowning in "red tape" – much of it excessive. It could not be expected to keep abreast of every administrative development. HMRC failed to meet its various responsibilities with impunity but a taxpayer error on the minute details of the system was punished automatically. HMRC were in breach of their stated commitment to help small businesses in financial difficulties.

(5) The penalty was punitive and disproportionate. Calculating the penalty as an interest charge for overdue payment Mr Moulding calculated that in the

Company's case it was equivalent to 187% pa – the penalty for just the final month's late payment was equivalent to interest at 365% pa. This was not the sort of penalty appropriate to an honest mistake.

5. Mrs Walker for HMRC made the following submissions:

(1) The introduction of the new PAYE penalty regime had been preceded by extensive publicity, including press coverage and a podcast. For example, the September 2009 issue of HMRC's Employer Bulletin covered the topic in depth stating the amounts of the penalties; the due payment dates; and what to do if the employer anticipated difficulty in paying what was owed. The information was repeated in the Employer Bulletin for April 2010. That was the last paper edition of the Employer Bulletin, after which it was available online. The information was again repeated in the Employer Bulletins for August 2010 and February 2011. Mrs Walker understood the paper Bulletins would have been sent to the Company's accountants, who were registered to receive communications for the Company. On 17 December 2010 the Company signed-up to receive the electronic Bulletin by email alerts to the Company's company secretary.

(2) Although HMRC had no statutory obligation to issue reminders to employers, HMRC did as a customer service send a warning letter (Form FP12) to employers after the first PAYE default. HMRC's electronic folder recorded that the warning letter was issued on 28 May 2010 – Mrs Walker understood this would have been sent to the Company's accountants, who were registered to receive communications for the Company. That letter warned of liability to penalties if there were further late payments, and included a link to online guidance. Further, notices of default (Form P101(D)) were issued in-year and HMRC's electronic folder recorded that default notices were issued on 1 November 2010 and 29 March 2011– Mrs Walker understood these would have been sent to the Company direct and that was the address shown on the electronic folder entry. Moreover, the 29 March 2011 notice was prefaced by a telephone conversation on the same day with the Company's company secretary concerning the late payment.

(3) Paragraph 16 sch 56 gave the taxpayer a defence if there was a reasonable excuse for a late payment. HMRC did not accept that there was any reasonable excuse in the current case. Paragraph 16 explicitly excluded insufficiency of funds from constituting a reasonable excuse. Ignorance of the relevant law could not constitute a reasonable excuse. Adequate warnings had been given to the Company and its agents, even though HMRC had no statutory obligation to issue payment reminders.

(4) The rate of penalties was provided in recent legislation. The penalties were progressive and staged, and the 4% rate was reached only by persistent and repeated default. Parliament had taken the view that the penalties must be of sufficient weight to discourage late payment. The amounts did not attempt to reflect the commercial value of the late payment.

6. At the hearing Mr Moulding was accompanied by Mrs Heighton, the Company's company secretary, who stated to the Tribunal that she did not recall ever receiving

any default notices from HMRC, nor any information from the Company's accountants.

7. We consider the Company's grounds of appeal under three heads:

(1) The scheme of penalties in sch 56 is disproportionate.

(2) The Company has a statutory defence to the penalty.

(3) HMRC have acted unfairly in levying the penalty against the Company.

First contention - The scheme of penalties in sch 56 is disproportionate.

8. The sch 56 penalty regime is contained in legislation which has been relatively recently enacted by Parliament. Although the penalties are considerably more stringent than those previously levied for late payment by employers, the amounts are clearly set out in the legislation and must have been intended by Parliament. The purpose of a penalty is to penalise. It is not appropriate to compare a penalty for late payment with a calculation of the interest charge due for late payment. The penalty is not intended to compensate the Treasury for being kept out of its money; it is intended to deter non-compliance with the obligation to pay no later than the due date.

9. In *International Transport Roth GmbH v Home Secretary* [2003] QB 728 (not cited to the Tribunal) the Court of Appeal considered whether certain statutory penalties (related to illegal importation of immigrants) were so severe as to be invalid as being incompatible with a citizen's human rights. Simon Brown LJ stated (at ¶ 26):

> "… ultimately one single question arises for determination by the Court: is the [statutory] scheme not merely harsh but plainly unfair so that, however effectively that unfairness may assist in achieving the social goal, it simply cannot be permitted? In addressing this question I for my part would recognise a wide discretion in the Secretary of State in his task of devising a suitable scheme, and a high degree of deference due by the Court to Parliament when it comes to determining its legality. Our law is now replete with dicta at the very highest level commending the courts to show such deference."

10. Such a test is also applicable in taxation matters – see the European Court of Human Rights in *National and Provincial Society v United Kingdom* [1997] STC 1466 (at ¶ 80) (not cited to the Tribunal):

> "According to the court's well-established case law … an interference, including one resulting from a measure to secure the payment of taxes, must strike a 'fair balance' between the demands of the general interest of the community and the requirements of the protection of the individual's fundamental rights. The concern to achieve this balance is reflected in the structure of art 1 as a whole, including the second paragraph: there must therefore be a reasonable relationship of proportionality between the means employed and the aims pursued. Furthermore, in determining whether this requirement has been met, it is recognised that a contracting state, not least when framing and

> implementing policies in the area of taxation, enjoys a wide margin of appreciation and the court will respect the legislature's assessment in such matters unless it is devoid of reasonable foundation …"

11. Applying that test to the penalties provided for by sch 56 we note:

(1) The penalties are graduated to take account of the number of failures in a tax year (para 6 (4) to (7));

(2) The first failure in a tax year is forgiven (para 6(3));

(3) The top rate of 4% is triggered only if there are at least 11 (including the first) failures in a tax year (para 6(7));

(4) The penalty is geared to the amount of the underpayment (para 6(1));

(5) The taxpayer has a defence if he had a reasonable excuse for a failure (para 16);

(6) The taxpayer has a further defence if there were special circumstances (para 9); and

(7) The taxpayer has a right of appeal to this independent Tribunal (para 13).

12. Taking together all those factors we conclude that the scheme of penalties in sch 56, although perhaps harsh, falls within the "margin of appreciation" described by the ECHR in *National & Provincial* and thus is not "devoid of reasonable foundation". Accordingly, we conclude that the penalty regime in sch 56 is not ineffective by reason of disproportionality. We note that a differently constituted panel of this Tribunal recently came to the same conclusion in *Dina Foods Limited* (TC01546).

Second contention - The Company has a statutory defence to the penalty.

13. *Reasonable excuse (para 16 sch 56)* - Although the Company's grounds of appeal made reference to financial difficulties, it was now clear and accepted by Mr Moulding that the Company could have paid its PAYE liabilities on time, and would have done so if it had at the time realised the size of the penalties it would suffer by delaying payment by a few days each month. Therefore we do not need to consider the question of insufficiency of funds further. No other reasonable excuse was suggested and accordingly we conclude the Company did not have a reasonable excuse for the late payments of PAYE

14. *Agreement for deferred payment (para 10 sch 56)* - We considered whether the Company's time-to-pay arrangements were relevant but conclude that para 10 sch 56 does not assist the Company as the arrangements agreed concerned tax liabilities (corporation tax and income tax) other than the PAYE that was paid late.

15. *Special circumstances (para 9 sch 56)* - We considered whether there were any "special circumstances" within the meaning of para 9 sch 56 that might assist the Company but conclude that there are none.

16. For the reasons stated above we conclude the Company does not have a statutory defence to the penalty.

Third contention - HMRC have acted unfairly in levying the penalty against the Company.

17. From the evidence presented to us we find it is more likely than not that the warning letter and default notices were issued by HMRC to the Company or its agents; similarly, the telephone call to the company secretary on 29 March 2011.

18. While HMRC are under no statutory duty to remind taxpayers of their PAYE payment failures, they do so as what Mrs Walker for HMRC described as a customer service. They do so "in-year", so the taxpayer is alerted to the possibility of penalties, the method of calculation (and thus the scale) of which have been adequately publicised to the employer community by HMRC. The actual penalty is not assessed until the end of the tax year but that is, at least in part, a consequence of the statutory calculation method which requires consideration of the number of failures in the tax year.

19. We do not find any unfairness by HMRC in assessing the disputed penalties in this case.

Calculation of penalty

20. Although the Company does not challenge the calculation of the penalty, we consider the amount of the penalty needs to be adjusted for the following reason.

21. The amount of the penalty is "determined by reference to the number of defaults in relation to the same tax that [the taxpayer] has made during the tax year" (para 6(1)). A default occurs when the taxpayer "fails to pay an amount of that tax in full on or before the date on which it becomes due and payable" (para 6(2)). The penalty in dispute relates to the tax year ended 6 April 2011. The Company should have paid electronically its PAYE deduction in respect of the month ended 5 April 2011 no later than 20 April 2011. Although that payment was late, that failure occurred after 6 April 2011 and so should not be included in the penalty assessed in respect of the tax year 2010-11. (Instead it is the Company's first payment failure in relation to the tax year 2011-12, and so does not constitute a default for 2011-12: para 6(3).) Therefore, we adjust the 2010-11 penalty calculation by excluding the late payment due in respect of the month ended 5 April 2011; the rate of penalty remains at 4% (because even after that exclusion there were ten defaults in the tax year 2010-11).

Decision

22. For the reasons set out in ¶¶ 12, 16, 19 & 21 above, the appeal is ALLOWED IN PART, being to the extent of a recalculation of the penalty so as to remove the late payment due in respect of the month ended 5 April 2011. From the figures in the penalty notice dated 8 July 2011 we calculate that the penalty assessed of £5,321.45 should be reduced by £669.50 to give a revised penalty of £4,651.95.

23. 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.

TRIBUNAL JUDGE
RELEASE DATE: 22 December 2011