



TC03324

Appeal number: TC/2011/08620

***PENALTY FOR LATE PAYE PAYMENT –whether ‘EDP’ necessarily
proves date of payment - no – appeal allowed***

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

KESTREL GUARDS LIMITED

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE BARBARA MOSEDALE
CHARLES BAKER**

Sitting in public at Barrack Block, Southampton on 4 February 2014

Mrs P Morland, of HJS Accountants, for the Appellant

Mr P Shepherd, HMRC officer, for the Respondents

DECISION

Introduction

- 5 1. The company appeals against penalties imposed for late payment of PAYE in 2010/11. Penalties totalling £24,931.64 were imposed by letter dated 13 June 2011. The company appealed to HMRC who notified the appellant of the right to request an internal review. The review was carried out and notified to the appellant on 24 September 2011. This reduced the penalty to £13,330.89 on the basis that HMRC
10 accepted the appellant had a reasonable excuse for late payment in Months 1-3 of the PAYE year. HMRC also removed the penalty imposed for month 12 as they accepted (following *Agar Ltd* [2011] UKFTT 773 (TC)) that the payment due for the 12th month fell into the next tax year and could not be counted in year 10/11.
- 15 2. The appellant lodged an appeal with the Tribunal service. It was stayed pending the Upper Tribunal decision in *Hok Ltd* [2012] UKUT 363 (TCC) (see §52-54 below), and following the release of that decision has eventually come on for hearing.

Background facts

- 20 3. The appellant company was incorporated in 1988 and trades from Southampton. It has two directors, who are also shareholders. It has two other shareholders, one of whom is now retired and the other one works part-time. The director-shareholders are Mr Keith and Mr James Matthews, who both work full time in the business.
- 25 4. For financial security, cheques over £500 on the company's accounts require two signatures. The usual signatories are Mr Keith and Mr James Matthews but one of the other shareholders is also an authorised signatory. All cheques referred to in this appeal required two signatures.
- 30 5. Mr Keith Matthews became unexpectedly ill and required an emergency quadruple by-pass operation on 5 April 2010. This not only incapacitated him during that period, but meant that his son, Mr James Matthews had to run the business single handed as well as cope with the worry of his father's health. It was for this reason HMRC accepted that the appellant had a reasonable excuse for the late payments in May - July 2010 (ie months 1-3). By August 2010, HMRC expected that Mr James Matthews to have made any necessary adjustments to the business and to file the PAYE returns on time. We agree and the appellant does not suggest otherwise.
- 35 6. The appellant's case is that its returns for Months 4-10 and Month 12 (ie from August to April with the exception of March) were filed on time. Months 1-3 and 12 are irrelevant from the point of view of the calculation of the penalty (as explained above in §1) but are factually relevant to the evidence of patterns in the appellant's behaviour and so we refer to them below.
- 40 7. Mrs Morland produced a schedule of dates and payments which Mr Shepherd accepted was accurate. They disagreed over what it proved. That table is as follows:

Month	Day of week posted	Date of cheque	Date logged by HMRC	Date cash left Appellant's account	days between cheque date and EDP
1	Wednesday	19 th	25 th	27 th	6
2	Saturday	19 th	25 th	29 th	6
3	Friday	23 rd	28 th	30 th	5
4	Monday	16 th	20 th	24 th	4
5	Friday	17 th	21 st	23 rd	4
6	Monday	18 th	20 th	22 nd	2
7	Thursday	18 th	25 th	29 th	7
8	Thursday	16 th	5 th following	7 th following	20
9	Tuesday	18 th	25 th	27 th	7
10	Thursday	17 th	23 rd	25 th	4
11	Wednesday	23 rd	7 th following	11 th following	15
12	Sunday	17 th	21 st	27 th	4

8. The appellant disputed the accuracy of the dates that HMRC's records show that their payment by cheque was logged. It was HMRC's case that the logging date was the received date, and that HMRC treated the received date as the effective date of payment ("EDP").

9. HMRC's case on this boiled down to the computer record and Mr Shepherd's evidence that colleagues (unspecified) had told him that 99% of cheques would be logged the day they were received. He had no personal knowledge of HMRC's systems in the post room nor did he claim to have spoken to anyone who worked in the post received room. We had no evidence of HMRC's procedures on receipt of post.

10. Mr Shepherd pointed out that the EDP was mostly two working days before the cheque payment was shown as withdrawn from the appellant's account and noted that this was the same with the evidence in the *Calberto* case [2013] UKFTT 079 (TC). He suggested that this indicated that the cheques were presented on the date logged. We agree. But that does not tell us if the cheques were presented on the date they were received.

11. Mr Shepherd's case was that the appellant was warned about penalties and advised to allow 3 clear days for posting cheques. Mr James Matthews did not follow this advice. While we agree that other than for months 4 & 8, the appellant did not allow 3 clear days, that is irrelevant to the question of whether or not HMRC received the cheques on time. It could only be relevant to the question of reasonable excuse.

12. It was also Mr Shepherd's case that HMRC contacted the appellant 8 times in the year over the late payments. Again, that could only be relevant to a question of reasonable excuse and not to the question whether the payments were actually late.

5 13. More pertinently, Mr Shepherd did not accept Mr James Matthew's evidence that cheques were always posted on the day they were dated.

10 14. Mr James Matthews' evidence was that he had a system for the payment of PAYE. He explained why, using the system they had of paying employees, he thought it was not possible to calculate the amount of PAYE due until the week after the week in which the 5th of the month fell. In the past he had been in the habit of paying the due PAYE at the end of the month and never incurring penalties (apart from once incurring a very insignificant interest charge on a late year end payment). However, he clearly recollected being warned in early 2010 that from then onwards payments had to be received by 19th of each month and determining that from then onwards he would change his habit and in future would pay by the 19th in order to avoid penalties.

15 15. We found this evidence reliable. Mr James Matthews had a clear recollection of events and we formed the view that he was a man of orderly habits. We are aware that prior to 10/11 penalties were not charged for late PAYE payments as long as it was paid before the year end; HMRC's telephone records also record the phone call that Mr Matthews recollected. And in 10/11 the cheques were not dated near the end of the month.

20 16. We note that the system broke down in May-July 2010 but we find that that is explained by Mr Keith Matthews' illness.

25 17. Mr James Matthews explained in detail the system for writing the cheque. He would obtain his father's signature in addition to signing it himself and then post it on the day it was dated in a first class envelope provided by HMRC. We accept this evidence the veracity of which was not challenged by HMRC in any event. Mr Matthew explained the appellant's system for dealing with post and we are satisfied that the envelope would have been delivered to the post office before the time for last posting.

30 18. Mr Shepherd pointed out that Mr James Matthews did not obtain proof of posting. We accept Mr James Matthews' evidence that the appellant's post was taken down each day in two bundles (one first and one second class) and that it did not occur to him to obtain proof of posting of just one of the letters. We do not consider the failure to obtain proof of posting relevant: we accept Mr James Matthews' oral evidence that cheques were posted on the day the cheque was dated. Proof of posting could only corroborate this but corroboration we find is not needed.

19. In conclusion we accept that the date of the cheque was the date on which it was posted by first class post to HMRC.

40 20. We also accept that the Post Office's stated aim is to deliver 93% of first class post by the next day. We take judicial notice of the fact that in the ordinary course

first class post posted before the last collection time should arrive at its destination the next day. We certainly think it would be a rare event for a properly addressed first class letter to take more than 2 working days to reach its destination within the UK.

21. However, Mr Shepherd's case was that, of the 12 cheques posted by the appellant in properly addressed pre-franked first class envelopes, only one arrived in 2 days; 3 arrived in 4 days; 1 in 5 days; 3 in 6 days; 2 in 7 days; 1 in 15 days and 1 in 20 days. He was unable to produce any evidence that the postal service was as unreliable as these figures would appear to demonstrate, and considerably more unreliable than is public knowledge or as indicated by the Post Office website.

22. We also noted, as mentioned above, that the EDP appeared to be the actual date the cheque was paid in. This seemed to us to indicate if anything that the EDP was not the date the cheque was received. Logic suggests that around the 19th of every month HMRC would be inundated with PAYE payments from all employers and might be unable to deal with all the post on the day it was received. We would not expect the date received to always be the date the cheque was presented to the bank.

Our attention was drawn to the cheque dated 16 December 2010 that was not processed until 5 January 2011. We were also shown a copy of the cheque drawn in December 2013 and the bank statement showing that this cheque was not cashed until January 2014. It is not surprising that there would be some delay in processing over the Christmas period. However, it does cast further doubt on Mr Shepherd's claim that cheques are always processed on the day of receipt.

23. Mr Shepherd's case would have us believe that HMRC was so efficient and well-staffed that they were able to present to the bank every PAYE cheque on the day it was received but that the postal service is so inefficient and understaffed that it takes an average of about 5 days to deliver every first class letter. We think it more likely that the post office is considerably more efficient than this but that, particularly around the 19th of the month, HMRC is unable to deal with every envelope it receives on the day it receives it. While we do not criticise HMRC for this, we do think that the evidence in this case suggests that they do not have a system for recording the date that PAYE cheques are actually received as opposed to the date the envelope is opened and the cheque banked. We do take into account Mr Shepherd's hearsay evidence about what his colleagues have told him, but it is weak evidence as there is nothing to suggest his colleagues have any first hand knowledge of HMRC's post room procedures. We reject its reliability as it is not consistent with the other facts we have found in this case.

24. For these reasons, we are unable to find that the date HMRC logged the appellant's letters to its computer system (the EDP) reliably reflects the date that HMRC actually received them. Therefore we find that HMRC has not proved the date that any of the PAYE payments made by the appellant in 2010/11 were received. It has not shown that any of them were late other than those for months 1-3 and month 11, which the appellant accepts were late. All the others were posted by first class post in sufficient time to arrive on or before the due date and HMRC has failed to prove that they did not.

25. In any event, we note that the Interpretation Act 2010 provides as follows:

7 References to service by post

5 Where an Act authorises ... any document to be served by post...then, unless the contrary intention appears, the service is deemed to be effected by properly addressing, pre-paying and posting a letter containing the document and, unless the contrary is proved, to have been effected at the time at which the letter would be delivered in the ordinary course of post.”

10 26. We find that first class post is ordinarily delivered the day after posting (see §20 above). We find that HMRC has failed to prove the day on which the cheques arrived and they have therefore failed to prove that the cheques did not arrive the day after posting.

27. The appeal for months 4-10 must be allowed.

15 28. We note that our view is consistent with that expressed by Sir Stephen Oliver QC in *CED Ltd* [2013] TC 2633. We are unable to follow the reasoning in *Browns CTP Ltd* [2012] TC 2244 at §8-20 in which the Tribunal appears to have accepted without question or evidence that HMRC’s records of EDPs would reflect the actual date of receipt rather than the date the payment was entered onto the computer system.

20 *Reasonable excuse for month 11?*

25 29. Month 11 (March 2011) was paid late. There is no reasonable excuse for this: there is really no excuse at all as Mr Matthews is unable to remember why it was paid late. He thinks that either himself or his father was away on holiday but he can’t be sure and hasn’t checked. Even if Mr Matthews was certain that the cause of the lateness was holiday by one of the signatories, this would fail to explain why the third signatory wasn’t utilised. And in any event, a reasonable person would plan to meet his obligations despite an absence of a key individual on holiday, so absence on holiday would not normally constitute a reasonable excuse.

30 30. However, the rules (Paragraph 6(3) and paragraph 16(1)(b) of Schedule 56 to the Finance Act 2009) provide that the first default of a year does not incur a penalty and that late payments for which there is a reasonable excuse are not defaults. Therefore the first default of 10/11 was that of Month 11, and so no penalty arises in respect of it.

35 31. The appeal must therefore be allowed in its entirety and the penalty imposed discharged.

Reasonable excuse for months 4-10 and 12

32. In case this decision goes further, we record our findings on the appellant’s secondary case that it had a reasonable excuse for late payment in months 4-10. That claim is based on its belief that its cheque payments would be received in time.

33. We consider that a taxpayer will have a reasonable excuse when it behaves in the same way as someone who seriously intends to honour their tax liabilities and obligations would act.

5 34. We accept Mr Matthews' evidence that he genuinely believed that cheques posted by first class post would arrive the next day. So when he posted cheques on the 18th of the month or earlier he believed they would arrive on time. The question is whether it was reasonable for him to believe this.

10 35. The post office's stated aim is to deliver 93% of letters the next day. On this basis we consider Mr Matthew's actions were reasonable, particularly as he often posted earlier than the 18th.

36. Mr Shepherd's case is that Mr Matthews ought to have known that HMRC were not receiving the cheques on time. (Obviously this is hypothetical as we have already determined that HMRC have not proved that they were late). Mr Shepherd points to 8 telephone calls made by HMRC to the appellant during the tax year 10/11.

15 37. However, we find that the HMRC caller only actually spoke to Mr James Matthews in two calls made in months 1 & 3. Even on Mr Matthews' account the cheques were late at this time (due to illness) and so we find there is nothing in these calls to alert Mr Matthews to the fact his system was not working. All the other calls later in the year simply recorded that the HMRC caller had spoken to a third party and left a message to be called back. Mr Matthews' case was that he had not received these messages and in any event there was nothing to indicate from the message that HMRC considered the appellant's PAYE payments late.

25 38. Further, we are cautious to the extent we place reliance on these records. Two of the calls record that a message was left with someone with a name that Mr Matthews' evidence is did not work at the appellant. Further, one call was recorded as taking place on Christmas Day. Mr Shepherd's explanation of this was that the call took place the day before and the computer incorrectly logged it to the next day. More significantly, at points throughout the year, the records show the text "Refuses to pay".

30 39. Mr Shepherd's explanation for this was that it was a coding error. A particular coding which HMRC staff would use when payment was not received was interpreted by the computer as the taxpayer refusing to pay. Mr Shepherd accepted that the appellant had never refused to pay and the entries were erroneous. The issue was simply whether the payments were a few days late (and we have determined that HMRC have not proved this).

35 40. We find (were it necessary to do so) that the appellant never refused to pay. We have found, on the contrary, that none of its payments were shown to be late bar months 1-3 (for which HMRC found it had a reasonable excuse) and month 11.

40 41. We express our concern that this coding error exists at all, and that although identified in at least one earlier Tribunal decision (see *Calberto Ltd* at §23), it has not yet been rectified. If a taxpayer refused to pay its tax liability it would be a very

serious matter, potentially affecting its credit rating and company value. Further, it might indicate to a Tribunal that the taxpayer was not behaving as a taxpayer mindful of its duties to pay tax, which might affect whether it was found to have a reasonable excuse.

5 42. In keeping records, and producing them to the Tribunal, that untruthfully show the taxpayer as having refused to pay its tax liability, HMRC is acting unfairly and probably unlawfully. Fortunately, we have not been misled by this erroneous record.

43. The records do show that HMRC issued the taxpayer with P101s on a few times throughout the year. Mr Matthews' evidence was that he remembers receiving about
10 three of these. Despite our misgivings over the reliability of HMRC's records, we think it more likely than not that about 7 were issued as this is what is recorded. We think that Mr Matthews may well have forgotten how many he received in view of the fact his evidence was that he ignored them because they were always received after he had made payment. HMRC's records (in so far as the dates in them can be relied on –
15 see §38) confirm his account that they were issued after the date Mr Matthews sent the payments.

44. We find that the P101 was a "notice requiring payment" and stated that the PAYE for the previous month was "overdue". The notice went on to say "If you have made payment within the last few days, please ignore this Notice." And that is what
20 Mr Matthews did. We accept that he assumed, and we think he reasonably assumed, that the P101s were automatically generated like statements of account, sent out to remind taxpayers of the need to pay. They did not indicate that he had paid late because he had always paid before the P101 was received. They certainly did not say that payment had been received and was received late.

25 45. And in any event they were not sent every month, so they could not have been a warning of systematic failure. Mr Shepherd's evidence was that P101s would not be sent if the appellant was only one or two days' late. He was unable to explain this as a penalty is incurred if the payment is only one hour late. Our view is that it corroborates Mr Matthews' view that the P101 was intended by HMRC as a mere
30 reminder to pay and not a notification that penalties were being incurred.

46. We therefore find that there was nothing to put Mr Matthews on notice that his system of payment was resulting in the payments arriving late. There was no reason why a reasonable person, mindful of their tax obligations, would have been concerned that the cheques were late and therefore Mr Matthews, in continuing with his system,
35 was acting as a responsible taxpayer.

47. We find (were it necessary to do so) that the appellant would have had a reasonable excuse for making the payments on the dates it did in months 4-10 in 2010/11 had those payments actually been late.

48. In conclusion, were it necessary (which it is not) we would find that the
40 appellant had a reasonable excuse for late payment (had it been proved) in months 4-

10 (inclusive). (In this we agree with the reasoning in *Browns CTP Ltd* [2012] TC 2244).

Relevance of Hok

5 49. We note that this case took time to come on for hearing as it was stayed pending the Upper Tribunal decision in *Hok Ltd*. The decision of the Upper Tribunal was that this Tribunal has no jurisdiction to consider whether the penalty should be discharged because HMRC acted unlawfully (in a public law sense) by delaying notification of accumulating penalties to the taxpayer so that the taxpayer was not put on notice to rectify its failure.

10 50. The Upper Tribunal noted that the FTT had no evidence of why HMRC delayed notification of the penalties and was unable to determine, even if it had jurisdiction, whether HMRC had acted unfairly.

15 51. The Upper Tribunal did not make a finding that HMRC had acted fairly: it merely concluded that the jurisdiction to make such a determination rests with the Administrative Division of the High Court.

52. We note that it was Mr Shepherd's case that it was reasonable for HMRC to wait until end of year before notifying the appellant of the penalties it had incurred throughout the year because (he said) HMRC needed to see if the appellant had a reasonable excuse and in order to calculate the penalty.

20 53. HMRC issue the penalties without checking whether the taxpayer has a reasonable excuse in any event so the first reason given for this failure to warn is simply wrong; and as for the second reason given, HMRC does not need to be able to calculate the penalty before the end of the year, it just needs to notify the taxpayer that in its opinion the taxpayer is in default. The P101 could be modified to make this
25 clear to taxpayers, instead of inviting them to ignore the letter if they have already paid.

30 54. We are very concerned by HMRC's failure to issue warnings as the penalties accumulate. The PAYE penalties under Sch 56 are calculated based on the number of defaults and the amount of tax paid late. By being based in part on the number of defaults, Parliament clearly intended to incentivise taxpayers to minimise their defaults. Yet a taxpayer cannot minimise its defaults if it does not know it is in default.

35 55. We note that the legislation at Paragraph 11 of Schedule 56 specifically envisages the issue of a penalty notice before the end of the tax year with a supplementary penalty if the taxpayer continues to default. That further emphasises the intention of Parliament that HMRC should use the provisions to improve behaviour rather than simply collecting the maximum penalty.

56. We express the hope that in future HMRC will ensure that it notifies appellants each month it considers that it has received their PAYE late. We cannot think it fair

that a taxpayer is allowed to rack up penalties of £24,000 for 9 alleged late payments without any warnings.

5 57. 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.

**BARBARA MOSEDALE
TRIBUNAL JUDGE**

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RELEASE DATE: 14 February 2014