



**TC03596**

**Appeal number: TC/2012/05614**

*VAT default surcharge - VAT paid late - insufficiency of funds - Appellant awaiting payment for construction work undertaken from bodies within the public sector - whether reasonable excuse - no - Appeal dismissed*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**WESTOAK CONSTRUCTION LTD**

**Appellant**

**- and -**

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

**TRIBUNAL:    JUDGE MICHAEL S CONNELL  
                  MRS BEVERLY TANNER**

**Sitting in public at Alexandra House, The Parsonage Manchester on 5 February  
2014**

**The Appellant Company did not attend and was not represented**

**Ms Lisa Fletcher, Officer of HM Revenue and Customs, for the Respondents**

## DECISION

### The Appeal

5 1. Westoak Construction Limited (“the Appellant”) appeals against a default surcharge of £30,165.74, for its failure to submit payment of the VAT due, in respect of its VAT period ended 12/11, by the due date. The surcharge was calculated at 15% of the VAT due of £211,641.55

10 2. The Appellant did not attend the hearing. The Tribunal was satisfied that the Appellant had been given notice of the time, date and venue of the appeal hearing and that it was in the interests of justice to proceed.

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

### Background.

15 4. The Appellant had previously defaulted on VAT payments in period 12/09 when a VAT surcharge liability notice was issued and again in four further periods prior to the default period under appeal.

20 5. 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]. Payment was normally made electronically by BACS or CHAPS.

6. The 12/11 period had a due date of 31 January 2012 for filing of its return and payment of the VAT due. The Appellant submitted the VAT return on the 31 January 2012 in the amount of £211,641.55. The Appellant’s return was therefore received by HMRC on time.

25 7. HMRC have discretion to allow extra time for both filing and payment when these are carried out by electronic means. [VAT Regulations 1995 SI 1995/2518 regs 25A (20), 40(2)]. Under that discretion, HMRC allow a further seven days for filing and payment. The due date for the 12/11 period, if payment was made electronically, was 7 February 2012.

30 8. Payment of the Appellant’s VAT for period 12/11 was made in four instalments of £50,000 on 12 March 2012, 23 March 2012, 17 April 2012 and 27 April 2012. A final payment of £20,000 was made on 12 June 2012.

### Relevant legislation

35 9. 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 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 to the first default the specified percentage is 2%. The percentage ascends to 5%, 10% and 15% for the second, third and fourth default.

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 : -

‘(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 –

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

#### Appellant’s Case

12. The Appellant does not dispute that its VAT payment for the period 12/11 was due no later than 7 December 2011.

13. On the 29 February 2012 Mr Hardman, the Appellant’s company secretary, appealed the imposition of the penalty saying that the Appellant was suffering severe cash flow shortages and that the Appellant “..has been in agreement with HMRC in a ‘time to pay arrangement’ and as such no surcharges should have been issued”.

14. HMRC’s Local Compliance and Reviews reviewed the surcharge and reduced it to £30,000.00, advising the Appellant that a payment of £11,641.55 previously allocated to an earlier debt reduced the VAT outstanding at the date of imposition of the surcharge. However, the balance of the surcharge remained payable.

15. The Appellant lodged Notice of Appeal with the Tribunal on 11 April 2012. The stated grounds of appeal were:

5            “We have had various time to pay agreements with HMRC with regard to both VAT and PAYE due to severe cash flow issues within our business caused by the economic downturn within the construction industry, coupled with the fact that most of our work is within the public sector financed by government or local councils who, as can be demonstrated by the enclosed, have not been paying us on time or for the full value of work completed.

              We have been making payments under a time to pay arrangement and were unaware that a surcharge would be issued whilst we were paying within an agreement.”

10        16. With its notice of appeal, the Appellant enclosed a schedule of nine public sector jobs on which it was engaged between May 2010 and August 2011 together with details of sums ‘applied for’ and ‘certified’. The schedule showed the difference between the amounts applied for and the amounts certified (that is certified as having been satisfactorily completed), which resulted in a difference of £841,256, which the Appellant said was the reason for its cash flow shortages.

15        17. On 2 August 2012 HMRC responded by asking the Appellant for:

              (a) a breakdown of the monies received for the period 01/12/11 to 31/01/12,

20            (b) copy bank statements showing the balance at the due date, including details of any overdraft limit in place and a copy of the bank’s facilitation letter,

              (c) details of any action taken by the Appellant to recover outstanding debts and whether the business factored its invoices,

              (d) details of the Appellant’s customer base, with approximate percentages where possible,

25            (e) confirmation of the Appellant’s accounting basis – i.e. cash accounting or invoice accounting,

              (f) details of its standard credit terms and a breakdown of its VAT debts (by customer) up to the date of appeal,

              (g) any other information/documentation to be considered.

30        18. The Appellant provided the information requested. It explained that the company’s quantity surveyor goes on site and puts in “an application” for work done that particular month. The customer’s surveyor then certifies the amount to be paid for work satisfactorily completed. The Appellant said that the difference between the amount applied for and certified satisfactorily completed tended to get greater until  
35        the last payment was made. However, even when this was paid the amount paid is rarely the full amount and sometimes could be as low as 80%. HMRC pointed out that the figures submitted by the Appellant were the same as those in its notice of appeal which related to a later year. Mr. Hardman accepted this and said he must have made a mistake. When asked where he had obtained the initial figures from, he said that it  
40        was just a spreadsheet they had prepared and not from original records. It was not clear, therefore, how accurate the figures were.

19. Included with the information provided by the Appellant was a copy of its bank statements and bank facility agreement, which showed that the Appellant had an overdraft facility of £350,000, and at the time of the default the Appellant was operating well within its limit.

5 20. There was no evidence that the Appellant company was in a time to pay arrangement with HMRC.

#### HMRC's case

10 21. Ms Fletcher for HMRC said that the potential financial consequences attached to the risk of further defaults would have been known to the Appellant after issue of the Surcharge Liability Notice for period 12/09 particularly given the information contained in the Notice which on the reverse states:

15 '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.'

22. 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.
- 20 • On the actual website [www.hmrc.gov.uk](http://www.hmrc.gov.uk)
- On the E-VAT return acknowledgement.

23. There had been four further defaults and the reverse of each default notice detailed how surcharges are calculated and the percentages used in determining any financial surcharge in accordance with the VAT Act 1994 s 59(5).

25 24. Ms Fletcher said that there is no evidence that the Appellant had contacted the National Advice Service or the Business Payment Support Service prior to period 12/11 to discuss late payment proposals. The 12/11 VAT due was £211,641.56, of which £200,000 was paid after the due date. The Appellant's bank statement showed that on 7 February 2012, based on an overdraft facility of £350,000, there were  
30 available funds to discharge the outstanding VAT.

25. The Appellant has acknowledged in telephone conversations with HMRC that it was normal practice for there to be a difference between the amount applied for under construction contracts and the amounts certified by the quantity surveyor as payable by the client, and therefore these circumstances, where foreseeable, did not go beyond  
35 the normal hazards of business.

26. S 71(1)(a) VATA1994 specifically excludes insufficiency of funds from being a reasonable excuse for the late payment of VAT. The default surcharge of £30,165.74.

for the period 12/11 is less than 1.2% of the total value of the Appellant's sales net of VAT, which amounted to £2,662,333.00.

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

5 Conclusion

28. The Appellant was clearly aware of the due date for payments of its VAT and the potential consequences of late payment. Its grounds of appeal are that it was suffering severe cash flow shortages at the time of the default. As HMRC say, s 71(1)(a) VATA1994 specifically excludes insufficiency of funds from being a  
10 reasonable excuse for the late payment of VAT.

29. In *Customs & Excise Commissioners –v- Steptoe* [1992] STC 757 the taxpayer argued that although the proximate cause of his default was insufficiency of funds, the underlying cause of that insufficiency, namely the unexpected failure by a major customer to pay him on time, amounted to a reasonable excuse. The Court determined  
15 on a majority that the statutory exclusion of insufficiency of funds as an excuse did not preclude consideration of the underlying cause of insufficiency and that a trader might have a reasonable excuse if it were caused by an unforeseeable or inescapable event or when, despite the exercise of reasonable forethought and due diligence, it could not have been avoided. The Court nevertheless made it clear that the test had to  
20 be applied strictly.

30. 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 should then ask itself, with that comparable person in mind,  
25 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.

31. The Appellant appeared to have sufficient bank facilities to cover the VAT paid  
30 late. It could also have requested a time to pay arrangement but did not do so. The Appellant could have also asked HMRC to agree to cash accounting, which allows a taxpayer to pay VAT only on payments received from customers rather than invoices issued, although it is unclear whether the Appellant only invoiced amounts certified as due for payment, in any event.

32. The burden of proof is on the Appellant to show that the underlying cause of its  
35 failure to meet its VAT payment obligations was due to unforeseen circumstances or events beyond its control. In the Tribunal's view, for the reasons given above, that burden has not been discharged and there was no reasonable excuse for the Appellant's late payment of VAT for the 12/11 period.

40 33. The surcharge of £30,000 is accordingly upheld.

34. 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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**MICHAEL S CONNELL**

**TRIBUNAL JUDGE**

**RELEASE DATE: 15 May 2014**

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