TC04049

Appeal number: TC/2013/05012

VAT default surcharges - conjoined appeals relating to three separate VAT quarter - whether reasonable excuse late payment - insufficiency of funds - whether reasonable excuse - yes - whether time to pay arrangement in place - Appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

FOGARTY (FILLED PRODUCTS) LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE MICHAEL S CONNELL
MR TIM RATCLIFFE

Sitting in public at 4th Floor, Byron House, 2a Maid Marion Way, Nottingham NG1 6HS on 16 July 2014

Mr Gerry Tawton, Finance Director and Mr Stewart Macdonald, Managing Director of the Appellant Company for the Appellant

Mr Philip Oborne, Officer of HM Revenue and Customs, for the Respondents

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DECISION

The Appeal

1. Fogarty Filled Products Limited ("the Appellant") appeals against default surcharges for the periods 02/13 (TC 2013 05012), 08/13 (TC 2014 00797) and 11/13 (TC 2013 01939), for its failure to submit by the due date, in respect of the respective VAT periods, payment of the VAT due. The three appeals have been consolidated under appeal number TC 2013 05012.

2. The point at issue is whether the Appellant has a reasonable excuse for making late payments and whether the surcharges levied are disproportionate.

Background.

3. The Appellant Company is based in in Boston, Lincolnshire. It was established in 1877 as a feather processing company. The company produces duvets, quilts, pillows, cushions, nursery products and similar items using fabrics imported from Asia and a variety of fillings including feather, down and synthetic materials. The Appellant Company supplies major High Street companies such as M & S, BHS, Asda and other national retailers. It has approximately 260 employees.

4. The Appellant renders VAT payments and returns under the POA (POA) Scheme. Every VAT registered business with an annual VAT liability of more than £2.3 million (currently), is required to make payments on account. Under VATA 1994 Section 28(2), once in the POA regime, the business must make interim payments at the end of the second and third months of each VAT quarter. These interim payments are payments on account of the quarterly VAT liability. A balancing payment for the quarter is then made with the VAT return one month after the end of the quarter.

5. HMRC sends the business a payment schedule informing the business of the amount payable and listing all its payment dates. Each of the two Payments on Account is usually calculated as $1/24^{th}$ of the business's total VAT liability for the previous year.

6. All businesses in the POA regime are required to file their VAT returns online. Since April 2010 it is mandatory for all businesses with an annual turnover of £100,000 or more (excluding VAT) to pay electronically. HMRC normally have discretion to allow an extra seven day for payment when payments are made by electronic means. However businesses in the POA regime are not entitled to the seven day extension. Payments on Account must clear to HMRC's bank account by the last working day of the month in which they are due. The balancing payment for the VAT return must be received in HMRC's account on or before the due date indicated on the VAT return. If the due date falls on a weekend or bank holiday, the balancing payment must clear to HMRC's bank account by the last working day before the due date.

Period 02/13

7. The Appellant's payments for the periods 02/13 were due and paid as follows:

Tax Period	Amount	Due by	Paid on
02/2013	£86,191	31/01/2013	31/01/2013
02/2013	£86,191	28/02/2013	15/03/2013
02/2013	Balance due (£273,303)	29/03/2013	15/05/2013 (£136,651.65) 30/05/2013 (£136,651.65)

The Appellant was therefore on time with the first interim payment on account, but late in making the second interim payment and the balancing payment.

8. 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.

9. The Appellant had been in the default surcharge regime from period 11/10 onwards. Prior to the VAT periods subject to this appeal, eight earlier Surcharge Liability Notices had been issued.

10. On 18 April 2013 HMRC imposed a penalty of £53,924.00 in respect of the late payments for the period 02/2013. The Penalty was levied at 15% of £359,503.30 being the total amount of tax assessed as paid late (the second interim POA of £86,191 and the balancing payment of £273,313.30).

11. The Appellant pointed out that a Time To Pay agreement under Finance Act 2009 s108 had been reached on 27 February 2013, in respect of second interim POA for £86,191.00 and accordingly the default surcharge was reduced by HMRC to £40,995.49, being 15% of the balancing payment of £273,303.30.

12. Mr Tawton, the Finance Director, in a letter to HMRC dated 15 May 2013, appealed the penalty for the late balancing payment. He said that he had informed HMRC by email on 28th March 2013 that the company was not able to pay the balancing payment on the due date and that the payment would be made by 15 May.

13. He explained that the company had secured a large new contract with a major High Street retailer which was due to launch in late March 2013. Unfortunately due to unusually cold weather and the fact that the products to be sold were quilts with low tog ratings, the launch of the contract had been put back by the retailer from March to the end of April/early May 2013. The scale of the contract was such that the company had an exceptionally large amount of its working capital tied up in finished goods awaiting delivery and invoicing to the customer.

14. The Company had an invoice discounting facility provided by GE Capital which financed:

> 90% of sales invoiced, subject to industry standard debtor reserves (discounts, rebates, credit notes) and
>
> 80% of the Net liquidated value of finished goods stocks, subject to preferential creditor reserves.

The company was unable to issue invoices for finished goods until the customer took delivery and was therefore unable to maintain normal cash flow through the invoice discounting facility.

In addition to the debtor and stock reserves, GE held a £300,000 blocked cash reserve which further compounded the appellant's cash flow problems.

15. The Appellant's standard general trade terms were end of month plus 30 days, but all of its major customers were on specific extended payment terms of up to 90 days from invoice. As 90% of sales invoiced were funded by GE Capital upon invoicing, cash settlements by customers generated only the remaining 10% of the company's income.

16. Mr Tawton said that the company's cash flow was stretched beyond normal foreseeable limits. The Appellant's bank allowed the company a temporary and limited overdraft of £100,000. It also provided the company with a relatively modest import letter of credit facility. It had to pay its suppliers in Pakistan, for nearly all of its imported fabrics on a cash against documents basis to meaning that it enjoyed virtually no credit terms. He said that the company had started discussions with its bank to secure an increase in its important letter of credit facility which would enable it to obtain circa 90 day payment terms and that this would generate a significant benefit to its cash availability. However negotiations in March 2013 were at an early stage and any agreement would not have impacted on the company's cash position in time to enable payment of outstanding VAT for the 02/13 period.

17. The company had benefitted from previous Time to Pay (TTP) arrangements with HMRC, with which it had always complied. Due to the financial constraints outlined

above, on 28 March 2013 Mr Tawton asked for a TTP arrangement in respect of the balancing payment. (Paragraph 12 above).

18. The proposal was rejected by HMRC. The reason given was that "records show that when the company's last TTP arrangement was agreed, HMRC said that no further defaults would be waived."

19. In the event, the company was only able to pay 50% of the balancing payment amount (£136,652) on 15 May 2013. Mr Tawton informed HMRC that as a result of a major customer (and others) further deferring sales promotions from the end of March to the end of May, the unusual amount tied up in finished goods had severely impacted on the company's cash resources. He promised that the balance of £136,652 would be paid on 30 May 2013. When he had made the commitment to pay the full amount on 15 May 2013 he had no knowledge of the possibility of serious sales delays occurring beyond mid May 2013.

20. The Appellant therefore says that the delay in payment of its balancing payment was entirely due to unforeseen and inescapable circumstances and was fully communicated to HMRC. Payment of the balance was made by the company as soon as the company's cash position allowed. Mr Tawton said in his letter of appeal of 15 May 2013 to HMRC:

> "As with many companies, we are trying to survive in what are extremely challenging market conditions and maintain the security of employment of over 260 personnel. We service the retail sector, which has been impacted massively during the recession experienced over the past few years. In this context, penalties on the scale of the above, for a small manufacturing company like ours are extremely onerous and have a very significant negative impact on our cash resources.
>
> I have on several occasions requested that a meeting be arranged between representatives of Fogarty (Filled Products) Limited and HMRC to allow the Company to make personal representations regarding penalties such as these, however HMRC has stated that such meetings are not possible."

<u>"Reasonable excuse" and relevant legislation</u>

21. 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).

22. 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 –
>
> (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 ..'

It is s59(7)(b) on which the Appellant seeks to rely.

23. 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.'

24. 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 – *Customs & Excise Commissioners v Steptoe* 1992 STC 757 ("Steptoe").

25. 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

26. In its Notice of Appeal to the Tribunal the Appellant reiterates the grounds of appeal put to HMRC in its email of 28 March 2013 and letter of 15 May 2013 (paragraphs 12 – 16 and 20 above).

27. At the hearing, Mr Tawton said that at the time of the 02/13 default the company had limited overdraft facilities; its invoicing discounting facility provided a source of working capital, but unlike an overdraft, which might help a business through difficult times, invoice financing was relative to sales and during an unexpected downturn or interruption in sales the facility did not cushion a severe reduction in cash flow. To an extent the funder would lend on finished goods or work in progress, but at a much reduced discount percentage and subject to the imposition of stringent reserves.

28. Mr Tawton said that eight or nine large retailers made up the Appellant's main customer base and provided 90% of its income. Although the company had secured a major new contract, and sales may have been guaranteed, an exceptional amount of working capital had become tied up in finished goods and there was nothing that could have been done to avoid a cash flow crisis.

29. Mr Tawton said that he had explained the company's position fully to HMRC. The company was not suffering an insufficiency of funds as a result of poor trading or because of the normal hazards of business but because of exceptional events which had combined to cause a temporary but serious interruption in its cash flow. He said it was difficult to understand HMRC's reasoning in refusing time to pay. The company

had been offered time to pay previously and had always adhered to promised payment schedules.

30. Mr Tawton referred to HMRC's website which says that they will:

> "agree time to pay where it believes that you are genuinely unable to pay in full and on time. Also that by allowing you extra time it will mean that you can pay what is due and you can return to making future payments in full and on time".

No explanation had been given as to why the company was being refused a Time to Pay arrangement other than that it had been offered time to pay previously. It was clear that the company would be able to pay the VAT due. It simply required a one or two month deferral period.

HMRC's Case

31. 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 11/10, given the information contained in the Notice. Included within the notes on the reverse of the Surcharge Liability Notice, is the following, standard, paragraph:

> '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.'

32. 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.

33. 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).

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

35. HMRC's Notice 700/50 (December 2011) s 6.3 (the notice represents HMRC's policy and understanding of the relevant legislation) states that HMRC consider that genuine mistakes, honesty and acting in good faith are not acceptable as reasonable excuses for surcharge purposes.

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

37. The Finance Act 2009 Section 108 specifies that there is no liability to a default surcharge for a period where contact is made with HMRC prior to the due date in order to arrange a payment deferment and this is agreed by HMRC. In this case there was no agreement and whether or not a time to pay arrangement should be agreed is entirely within the discretion of HMRC.

38. Mr Oborne for HMRC said that the Appellant's arguments regarding financial constraints and the company's cash flow problems along with its efforts to meet its obligations were nothing out of the ordinary. The events that occurred were entirely foreseeable and in essence were in any event normal business risks. The financial challenges facing the appellant were nothing unusual or out of the ordinary. The deferred sales in May 2013, being several weeks after the due date for the 02/13 (29 March 2013) period, could not provide a reasonable excuse for the default.

Conclusion

39. It is clear from the facts that the Appellant had done everything it could to exercise reasonable foresight, due diligence and have due regard for the fact that its VAT was payable on the due date. It had in place invoice discounting facilities, and an overdraft with its bankers, albeit insufficient to cover its needs. The company enjoyed no credit facilities with its suppliers but conversely had to agree up to ninety day terms with its customers. It was endeavouring to negotiate credit with its suppliers but in the midst of these everyday problems suffered an unforeseeable cash flow interruption of crisis proportions.

40. The management acted proactively in ensuring that HMRC were aware of its position and put forward proposals regarding the date on which the VAT would be paid based on normally realistic forecasts. The Appellant underestimated the delays in sales but this was due to unseasonably inclement weather. The appellant paid the balance of its 02/13 VAT immediately it was able to.

41. HMRC argue that the causes of the insufficiency of funds were not exceptional. They argue that they were foreseeable and attributable to the ordinary hazards of trade. As such, they say that they could not be regarded as a reasonable excuse for the Appellant's late payment of VAT. However, that is to regard foreseeability as the sole criteria for determining whether a reasonable excuse has been shown and is not the correct approach and in any event it is difficult to see how the cash flow interruption between March and May 2013 could have been foreseen.

42. The issue of reasonable excuse and Section 71(1)(a) was considered in detail in *Steptoe*. The Court of Appeal held that although insufficiency of funds can never of itself constitute a reasonable excuse, the cause of that insufficiency, that is, the underlying cause of the taxpayer's default, might do so and in considering that, as Lord Donaldson MR explained, the question is whether the late payment was "reasonably avoidable". The test to apply can be found in his judgment where he said:

> "… If the exercise of reasonable foresight and of due diligence and a proper regard for the fact that the tax would become due on a particular date would not have avoided the insufficiency of funds which led to the default, then the

> taxpayer may well have a reasonable excuse for non-payment, but that excuse will be exhausted by the date on which such foresight, diligence and regard would have overcome the insufficiency of funds."

That is the correct test to be applied and is binding upon the Tribunal. In Steptoe Lord Nolan said that it is necessary to distinguish between the reason for non-payment and excuse for non-payment. The taxpayer here, is saying that it should be excused from the surcharge not because it was short of funds but because that shortage was brought about by circumstances which were unforeseeable and over which it had no control. Lord Nolan quoting from his own decision in *Customs and Excise Commissioners v Salevon* [1989] STC 907 said:

> "… It is worth bearing in mind that the penalties imposed for a delay or deficiency in payment, however slight, are fixed. Neither the commissioners nor the tribunal have any power to mitigate them by reference to the facts of the particular case. In these circumstances the wide discretion conferred on the commissioners and the tribunal by s19(6) should not in my view, be regarded as having been cut down by s33(2) to any greater extent than the language of the latter subsection strictly requires. The commissioners and the members of the tribunal are well qualified to distinguish between the trader who lacks the money to pay this tax by reason of culpable default and the trader who lacks the money by reason of unreasonable and inescapable misfortune."

43. Conditioned by their concerns about access to capital finance, the strategy of many businesses during recessionary times, when the bundle of resources normally available to them are non-existent, is retrenchment. Unlike many businesses, the Appellant was managing to trade relatively successfully, during what has been commonly regarded as the deepest and most challenging recession of the last half century. It is engaged in the production of specialist products. In the case of the Appellant it had accepted a contract with a nationally recognised blue chip customer with the intention of maintaining and promoting its profitability. Relative to the region in which it is based the company is a major employer. Completion of the contract would have added to the company's profits and provided ongoing security to its employees. The contract did not come without risk, albeit minimal, but to any financial director, the risk was worth taking. Risk and reward often go hand in hand and that is a fact of life which must be recognised particularly in determining what the 'normal hazards of trade' are. Ultimately revenue would be raised for the Exchequer from tax on corporate profits, employee's income, NIC and VAT.

44. Unfortunately for the Appellant a number of factors combined which caused an unusual and significant cash flow problem. As Mr Tawton said, the scale of the major contract which it received was such that the company had a substantial amount of its working capital tied up in goods awaiting delivery to the customer. Because the company's raw materials were mostly imported and the company had no credit terms with suppliers it had to pay for most of these on a cash basis. The company was endeavouring to arrange an increase in its Letter of Credit facility with its bank which would have effectively enabled it to obtain ninety day payment terms on its imports but those arrangements were not, at the end of March 2013, in place.

45. Even if we regard 'foreseeability' in the context of normal everyday business hazards as the sole criterion for establishing whether or not a reasonable excuse exists, the events which affected the Appellant's business and cash flow were outside what the exercise of reasonable foresight would have allowed or enabled the Appellant to do in order to avoid the shortage of funds which led to the late payment of VAT. It would be more apt to describe the appellant's inability to pay its VAT as having been caused by an unavoidable interruption to its cash flow rather than insufficiency of funds. In practical terms there is a clear distinction.

46. It has to be recognised of course that the Appellant Company's financial difficulties in period 02/13 were not an isolated event. They had continued for a considerable period as evidenced by the fact that the company had been in the VAT default surcharge system since period 11/10. It had benefited from several previous TTP arrangements with HMRC, with which it had always complied. That was in part a reflection of the financial difficulties caused by the recession and the lack of access to capital from banks which themselves were suffering liquidity problems.

47. There was clearly a history of the management taking such reasonable steps as they were able, to maintain the company's ability to discharge liabilities including VAT when they fell due. It is therefore difficult to understand why, given the facts as outlined to HMRC and the Appellant's compliance history, a TTP arrangement was not granted for period 02/13. That was course a matter entirely within the discretion of HMRC.

48. On the facts, in respect of the 02/13 period we find that there would have been no insufficiency of funds if it were not for the unexpected and inescapable financial constraints which beset the business. We find that the Appellant exercised reasonable foresight, due diligence and a proper regard for the fact that the tax would become due on the due dates. Its VAT returns were submitted on time and VAT liabilities were settled immediately the Appellant had the funds, deferred and by instalments. For the above reasons we find that the Appellant has shown that it had a reasonable excuse for the late payment of its VAT in period 02/13 and therefore allow that appeal.

Period 08/13

49. The Appellant's payments for the periods 08/13 were due as follows:

Tax Period	Amount	Due by	Paid by
08/2013	£82,991	31/07/2013	02/09/2013
08/2013	£82,991	30/08/2013	30/09/2013 (£105,108.89)
08/2013	Balance due (£525,979.49)	30/09/2013	As below

The balancing payment was paid by five instalments:

£44,804.11 paid on 1 October 2013,

£93,994.88 paid on 7 October 2013,

£93,994.87 paid on 14 October 2013,

£93,994.87 paid on 21 October 2013,

£93,994.87 paid on 28 October 2013.

The Appellant's first payment on account, second POA and balancing payment were therefore all late.

48. Prior to and during the 08/13 period, there had been a number of e-mails and faxes by the Appellant to HMRC:

(i) On 27 July 2013 Mr Tawton e-mailed Mr Dawson of HMRC's Large Business Unit requesting deferral by one month of the two payments on account of £82,991. He said that payment would be made on 30 August 2013 and 30 September 2013. The reasons he gave were that:

- "The Enforcement Office has agreed to a TTP arrangement in respect of the balance of the May 2013 quarter's VAT liability. This balance amounts to £309,548.09 and is payable in full by the end of August, the first payment of £103,182.69 having been made today. Whilst I will ensure that these payment commitments are adhered to, this amount, together with the estimated PAYE payments over the same period mean that over £600,000 is being paid to HMRC by the end of August which, given the trading conditions outlined below, means that it is not possible to make the VAT payments on account until the proposed dates.
- July is traditionally our lowest sales month, due primarily to the low unit sales value of products sold (mainly lower value quilts) and once again, due to depressed trading conditions. Our sales fell some 50% below our forecast projections. As our funding is based principally on an invoice discounting facility, this has currently put significant additional strains on our working capital and cash requirements.
- We are confident that we can achieve our forecast sales for August and September – sales in these months will show an uplift as we service promotions already in place ahead of the Bank Holiday period and start to enter the busier autumn/winter retail sales periods. We have conservatively forecast sales below prior year, which gives us confidence that as a business we can secure these sales, and thereby achieve the cash outgoings incorporated in the cash forecasts, which are based on these sales forecasts."

(ii) On 31 July 2013 Mr Tawton sent a copy of the above e-mail by fax to Mrs Booker of HMRC's Debt Management Service.

(iii) On 16 August 2013 Mr Tawton sent a further fax to Mrs Booker referring to an earlier "discussion" with her which reiterated the proposals contained in his e-mail of 27 July 2013.

(iv) On 30 August 2013 Mrs Tawton sent a further fax to Mrs Booker saying that the first interim POA promised for that day would now be made one working day late, on 2 September 2013. He had earlier telephoned to speak to Mrs Booker, but she was not available.

(v) On 27 September 2013 Mr Tawton sent a further fax to Mrs Booker saying that the company would be able to pay the second interim POA as promised but not the balancing payment due on 30 September 2013. He said that the company would be making a payment of £105,195.89 that day to cover the second POA, and four weekly payments of £105,195.89 from first of October 2013 to clear the balancing payment of £525,979.49, bringing all VAT due for 08/13 up to date by the end of October 2013. He asked for confirmation that his proposals were agreed and that no penalty surcharge would be levied for the "payments made after 30 September 2013".

(vi) On 30 September 2013 Mr Tawton sent another fax to Mrs Booker saying that the promised payment of £105,195.89 had been duly made on that date and that a further amount of £44,804.11 had also been made on account (although that payment had missed the Bank FPS cut off time and would not reach HMRC until 2 October 2013). He proposed that the reduced balancing payment of £375,979.49 be paid by four equal weekly instalments of £95,994.88 as previously stated, and again asked for confirmation that there would be no penalty surcharges for the payments made after 30 September 2013.

(vii) On 7 October 2013 Mrs Booker replied saying:

"On the basis that the VAT debt … will be cleared by the end of October I am prepared to support the proposal of the company.

I am however unable to confirm that a penalty surcharge will not be applied as this is not within my remit. You may need to contact the VAT help line …"

49. On 17 October 2013, 2013 HMRC imposed a penalty of £75,556.00 in respect of the late payments. The Penalty was levied at 15% of £503,773.00 being the total amount of tax assessed paid late.

50. The default surcharge was subsequently reduced from £75,566 to £24,897.80, being 15% of the VAT paid late in respect of the 1st and 2nd interim payments totalling £165,982 on the basis that there had been an agreement by HMRC that the balancing payment due on 30 September 2013 could be settled by 31 October 2013.

51. Mr Tawton appealed against the revised default surcharge of £24,897.80 on the following grounds:

> ".. It is clear from (my) communications to HMRC that the payment due on 30 September 2013 included the second POA of £82,991 — this liability was agreed by HMRC to be paid by 31 October 2013. The liability was paid in full by 31 October 2013 in line with this agreement. As this second POA was clearly part of the Time to Pay agreement for the balancing payment due on 30 September 2013, any default surcharge relating to this payment should be rescinded.
>
> I would also contend that the default surcharge in respect of the … first POA should be rescinded, as this delay was fully communicated to and implicitly agreed by HMRC as there was never any communication from either the Large Business Unit or the Enforcement Office stating that the deferral was not agreed, and there was no further communication from HMRC following up this late payment."

52. At the hearing Mr Tawton reiterated that, with regard to the first payment on account, even though the Appellant did not adhere strictly to the time to pay proposals put forward on 27 July 2013, the payment promised for Friday 30 August 2013 was paid only one working day late and the payment promised for 30 September was in fact paid on that date.

53. With regard to the time the payments were made in respect of the balancing payment due on 30 September 2013, there was no reason why HMRC's letter should not equally be regarded as agreeing, albeit retrospectively, to the Appellant's varied payment proposals as put forward in the faxes of 27 and 30 September 2013 in so far as these referred to payments already paid under the Appellant's original payment proposals and in particular the second interim payment paid on 30 September 2013. Mr Tawton said that despite his faxes and telephone conversations there are never been a formal response to his time to pay proposals for the first and second interim payments on account.

HMRC's case

54. With regard to the balancing payment due on 30 September 2013 HMRC agree that a retrospective TTP agreement was agreed on 7 October 2013, but assert that this did not also extend to the second interim payment as asserted by the Appellant.

55. Although the Appellant contends that the deferral of the two interim payments was 'implicitly agreed' by HMRC, in so far as there was neither a rejection of the proposal nor further communication following up late payment. The Appellant can only avail itself of the relief provided by Finance Act 2009 section 108 where deferment is *explicitly* agreed by HMRC.

56. HMRC contend that, given the Appellant's POA history and familiarity with both making prior TTP agreements and the default surcharge regime, it is not reasonable to assume HMRC's agreement to payment proposals can arise by default. The Appellant has not suggested further contact was made prior to the defaults to confirm that agreement had in fact been granted.

57. The Appellant's email of 31 July 2013 notified that the payment originally proposed for that day would instead be paid on 30 August 2013, but was actually paid on 2 September 2013. As such HMRC contend even if a TTP agreement could be regarded as having been implicitly agreed for the first interim payment on account, the surcharge has nonetheless been properly applied because the Appellant had not adhered to the arrangement (s 108 ss 3 and 4 FA 2009).

Conclusion

58. Mrs Booker's letter of 7 October 2013 is possibly ambiguous, but can be interpreted as confirming that a TTP arrangement had been agreed for the balancing payment but that there was no guarantee that a penalty surcharge would not be levied for the late payment of the two payments on account. However Mr Tawton first made his request for a TTP on 27 July 2013. He received no formal response. In the event his first POA was not made on the date promised – albeit only one working day late. The second POA was however paid on the day promised, i.e. 30 September 2013 and there had been no indication in the meantime that is since his second fax of 31 July 2013, that HMRC would not accept the payment proposals he had submitted. There had however been a telephone conversation prior to Mr Tawton's fax of 16 August 2013 when he reiterated his promise to pay the second POA on 30 September 2013.

59. Although a TTP has to be agreed with HMRC and silence or inaction on the part of HMRC cannot in itself be regarded as tacit acceptance of proposals, given that HMRC received no less than four e-mails/faxes from Mr Tawton and discussed the proposals with him at least once over the telephone, the conclusion has to be that it was reasonable for Mr Tawton to assume that a TTP arrangement had been agreed in respect of the second POA as part of his payment proposals to discharge that payment and the balancing payment by equal instalments, as referred to above.

60. That is not to say that a tentative arrangement had been agreed but it provides a reason why the appellant adhered to his payment proposals at least in respect of the second interim payment on account. Accordingly the Appellant has shown a reasonable excuse for the late second payment on account, having secured a TTP arrangement for that period. We accordingly allow that appeal.

61. With regard to the first payment on account, because it was not paid on the date promised and Mrs Booker could not retrospectively agree a TTP for a late payment after the event, the Appellant has not shown a reasonable excuse for the late payment and we disallow that appeal.

Period 11/13

62. The Appellant's payments for the period 11/13 were due as follows:

Tax Period	Amount	Due by	Paid on
11/2013	£82,991	31/10/2013	14/11/2013

11/2013	£82,991	29/11/2013	13/12/2013
11/2013	Balance due £364,396.99	31/12/2013	£50,000 31/12/2013
			£78,599.25 10/01/2014
			£78,599.25 22/01/2014
			£78,599.25 27/01/2014
			£78,599.25 30/01/2014

63. On 17 January 2014, 2013 HMRC imposed a penalty of £72,056.00 in respect of the late payments. The penalty was levied at 15% of £480,378.99 being the total amount of tax assessed, paid late.

The Appellant's contentions

64. In respect of the two payments on account, Mr Tawton says that on 31 October 2013, HMRC were informed by fax of the company's inability to pay the first POA on the due date and that payment would be made within 2 weeks. He asked for confirmation that no surcharge would be imposed for the delay in payment.

65. On 4 November 2013, Mrs Booker of HMRC's debt management unit, wrote to Mr Tawton acknowledging his fax saying:

> "……I note that you have indicated that you will not be in a position to submit the first POA against the 11/13 VAT until 14 November and have requested no default surcharge be applied.
>
> It may be worth you checking with the VAT helpline, but as far as I am aware, no default surcharge is applied to late remittance of payments on account. This is because they do not reflect an actual tax charge, simply a POA of a tax charge. A default surcharge would only be applied where following submission of the VAT return and the application of the payments on account the resulting balance was left unpaid when due."

66. Mr Tawton interpreted this response as meaning that his payment proposal for the first POA was effectively agreed by HMRC and that no surcharge would be levied. Payment of the first interim payment was duly made on 14 November 2013.

67. He says that on 29 November 2013, being the due date, he told HMRC that the Appellant would not be able to pay the second interim payment on time but that payment would be made by within two weeks. He received no response from HMRC and payment was duly made on 13 December 2013. Again he had assumed that the time to pay rent and was in place

68. With regard to the balancing payment, Mr Tawton says HMRC were informed by telephone on 31 December 2013 of the company's inability to pay the tax due. He informed HMRC that sales in December 2013 were well below forecasted levels. The forecast at the start of December was for sales for the month of £3,751,000 whereas actual sales were £3,541,000. After taking into account the 90% invoice discount rate, this restricted cash availability by £227,000.

69. With effect from 1 November 2013, the Appellant's temporary overdraft facility with Barclays Bank had been reduced from £100,000 to £50,000. However based on discussions with the Bank's relationship director, Mr Tawton had assumed that the £100,000 overdraft facility would remain in place beyond 31 December 2013. The reduction in the facility was communicated at short notice late in December, which did not allow time to take other action to compensate for the effective loss of £50,000 funding.

70. GE Capital had also increased the Appellant's blocked cash reserve from £300,000 to £500,000, effective from 6 December 2013. This created a direct restriction of £200,000 on the Appellant's cash availability in December 2013. The quantum of the restriction allied to the reduced sales and the termination of the overdraft facility caused an immediate cash flow problem and meant that settlement on the due date was not possible.

71. In order to partly offset the reduction in the company's overdraft and increase in the GE blocked cash reserve, the Company took out a short term loan with Lease Direct Finance Limited (LDF) for £100,000. The interest cost on the loan was onerous (£5,368.15 with full repayment by 8 April 2014), which Mr Tawton says illustrates the commitment of the Company to settle its VAT liabilities as soon as funds allowed.

72. Mr Tawton followed up his telephone call of 31 December 2013 with a fax to Mrs Booker on 2 January 2014, saying that he had been able to pay £50,000 on 31 December 2013, as promised in his conversation with HMRC two days earlier, and he reiterated the other proposals which he had discussed, being payment of the balance of £303,597 by four equal weekly instalments. As this proposal was not refused by HMRC, Mr Tawton assumed the payment schedule had been accepted and payment of the instalments were duly made on the dates promised.

HMRC's contentions

73. HMRC again refer to Finance Act 2009 s108(2)(b) which provides that HMRC may suspend a surcharge where time to pay is requested *before* the registered person becomes liable to a surcharge and HMRC agree to defer payment. A liability to surcharge arises on the day after the due date if no agreement has been reached.

74. Mr Oborne for HMRC said that the Appellant simply told HMRC when payment was to be made and an agreement to the proposed late payment was neither requested nor granted. Although Mr Tawton spoke to HMRC about a TTP arrangement on 31 December 2013, this was not followed up in writing until 2 January 2014, which was after the due date and the actual default and therefore regardless of whether Mr Tawton reasonably assumed that an agreement had been reached, it fell outside the provisions of the Finance Act 2009 s108(2)(b).

75. HMRC say that Mrs Booker's letter of 4 November 2013, although offering a personal but incorrect understanding that a VAT default surcharge is not payable on a late interim payment, nonetheless advise the Appellant to check the actual position with the VAT helpline. In any event, full guidance on how surcharges are applied in respect of late payments on account and the balancing payment, was provided to the Appellant on the reverse of the 08/13 Surcharge Liability Notice issued on 17 October 2013. S59A VATA 1994 specifically states that a taxpayer is liable to a default surcharge if late in making a payment on account.

76. HMRC say that, given the Appellant's Payments On Account history and familiarity with both making prior TTP agreements and the default surcharge regime, it was not reasonable to assume that an agreement to payment proposals has been reached by default.

Conclusion

77. It is clear from the Appellant's VAT payment history that because of a combination of factors it struggled to pay its VAT on time and during extended periods of regular contact with HMRC a pattern emerged of the Appellant proposing, and on some occasions HMRC agreeing, payment proposals. For the most part the Appellant adhered to its payment promises and always paid its VAT, albeit sometimes deferred and by instalments. In respect of the 02/13 period a TTP arrangement had been agreed in respect of the second interim payment on account. In the 08/13 period the Appellant's payment proposals in respect of the balancing payment (and in our view the second payment on account) were accepted under a TTP arrangement. No VAT default surcharges were imposed in period 05/13 as a TTP arrangement had been agreed in respect of the Appellant company's first and second payments on account and the balancing payment. There was a similar pattern of TTP arrangements in earlier years.

78. In respect of the two interim payments on account, given the pattern of dealings between the Appellant and HMRC it is understandable why Mr Tawton assumed that his TTP proposals had been agreed. Despite the telephone conversation and the

detailed proposals set out in Mr Tawton's fax, there was no indication from HMRC that they had not been agreed Nonetheless, on the facts with regard to the first and second payments on account we do not accept that a TTP arrangement was implicitly agreed with HMRC. The situation here was different to that in respect of the second interim payment on account for the earlier default period of 02/13 where we found in favour of the Appellant. In respect of this 08/13 default period, the Appellant did not have reasonable cause to believe that a time to pay arrangement had been agreed. Furthermore, the Appellant, given Mr Tawton's knowledge of the POA regime, should not have assumed that Mrs Booker's letter of 4 November 2013 accurately set out the position with regard to late interim payments.

79. In respect of the balancing payment, Mr Tawton's request for a TTP arrangement was made on 31 December 2013 and therefore, despite HMRC's assertions to the contrary, was not made after the due date.

80. We were not provided with a transcript of Mr Tawton's conversation with HMRC on 31 December 2013, but the conversation was followed up by his fax of 2 January 2014 setting out the company's proposals to pay the balance outstanding by the end of January 2014, which the Appellant duly adhered to. There does not appear to have been any response by HMRC to either Mr Tawton's telephone call or fax. A Surcharge Penalty Notice was not issued until 17 January 2014 and in fact appears to have been sent to the Appellant sometime after that, possibly after 30 January 2014. On that date Mr Tawton sent a fax to HMRC confirming that the final instalment promised had been paid, clearing the company's 11/13 VAT liability, but did not make any reference to the VAT penalty surcharge.

81. However, taking into account the constraints on the Appellant's cash flow as set out in paragraphs 68 - 70 above, and adopting the same reasoning as contained in paragraph 43 - 48 above, regarding period 02/13, we find that the Appellant has shown a reasonable excuse for the late payment of its VAT in period 11/13.

82. Accordingly, for period 11/13 the Appellant has shown a reasonable excuse for the late balancing payment, but not for the two interim payments on account which occurred prior to the exacerbation of the Appellant's cash flow difficulties in December 2013. The appeal is therefore allowed in part. The surcharge in respect of the late balancing payment is discharged. The surcharges in respect of the late interim payments on account are confirmed.

83. 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.

MICHAEL S CONNELL

TRIBUNAL JUDGE

RELEASE DATE: 7 October 2014