



TC05174

Appeal number: TC/2016/00432

VAT – Default Surcharge; proportionality appeal dismissed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

HIGHLAND WOOD ENERGY LTD

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE J GORDON REID QC FCI Arb
MRS EILEEN A SUMPTER, WS**

Sitting in public at George House, 126 George Street, Edinburgh on 4 April 2016

Gary Wallace, CA, for the Appellant

Mark Boyle, Officer of HMRC, for the Respondents

DECISION

Introduction

5 1. This is a Default Surcharge appeal under the VAT regime. The amount at stake is £6,658.18. The return was submitted on time but the VAT payable was paid three days late. The appellant challenges the proportionality of the penalty imposed.

2. A hearing took place at George House, Edinburgh on 4 April 2016. The appellant was represented by Gary Wallace CA, the appellant's financial manager.
10 The respondents (HMRC) were represented by Mark Boyle, an HMRC officer. Neither side gave formal evidence. Mr Wallace explained the general background. Both parties made submissions. A bundle of documents and authorities was also produced.

Statutory Background

15 3. The default surcharge regime is well known. It is fully described in *Trinity Mirror plc v HMRC*¹ and in a number of other cases. Liability to pay a surcharge may be avoided where the failure timeously to despatch the return or make payment of the VAT declared to be due is attributable to a *reasonable excuse*. *Reasonable excuse* is not in issue in this appeal.

20 4. We have no statutory power to reduce the penalty, unlike other fiscal regimes.

Factual background

5. The appellant carries on business in Scotland in the biomass heating industry. It has premises in Glasgow and Fort William. There are two sides to its business. First the servicing side; it sells pellets and wood chips for boilers particularly between
25 October and March. That side of the business is not so busy in the summer.

6. Secondly, the project side; it installs boiler systems in schools, and for construction companies, individuals and public authorities. Mr Wallace described that side of the business as *lumpy*. There were cash flow problems earlier in 2015 which led to the appellant being in default and entering the surcharge regime.

30 7. Overall, the appellant has turnover of about £8m per year. It has about 42 employees including Mr Wallace and an assistant accountant. The assistant accountant was responsible for despatching the returns timeously and making the payment of VAT due each quarter. The appellant had no system in place for dealing with urgent duties.

35 8. The appellant entered the default surcharge regime following late payment of VAT for quarter to 31 December 2014. Payments for the subsequent two quarters

¹ [2015] UKUT 421 (TCC)

were also late by over a month giving rise to default surcharges at the rate of 2% and 5% respectively. The VAT due was paid, albeit, late.

9. The VAT return for the quarter between 1 July and 30 September 2015 (the period 9/15) was due to be furnished electronically to HMRC by 7 November 2015
5 along with declared VAT of £66,581.84. The return was received by HMRC on 22 October 2015. However, payment of the declared VAT was not made until 10 November 2015.

10. The assistant accountant had been absent from work between about 2 and 6 November due to ill health. On her return, she, unfortunately, omitted to make
10 payment of the VAT due to HMRC. This was not noticed by Mr Wallace until 10 November 2014. Payment was then made through the online banking system in three tranches, namely one payment of £16,581 and two payments of £25,000. The online system required the appellant to make three payments rather than one.

11. The default (relating to the period 9/15) incurred a penalty of £6,658.18
15 calculated at 10% of the amount declared to be due in the return. A Surcharge Liability Notice was issued on or about 13 November 2015.

12. The appellant operated the Time to Pay system in relation to its VAT liability for the period ended December 2015.

13. The appellant sought a review of the decision to issue a default surcharge, but it
20 was upheld by HMRC letter dated 3 December 2016 and what appears to be confirmation of the review in a letter dated 12 January 2016. The review noted that the appellant had failed to contact the National Advice Service or the Debt Management Unit, that circumstances relied upon did not constitute a reasonable excuse. Moreover, HMRC asserted that the penalty was not disproportionate.

25 14. The appellant has a relatively good fiscal record. The imposition of a penalty of a sum in the order of £6,000 will put the continuing viability of its business in doubt and make it difficult for it to obtain loans or further loans to maintain its business. A large contract has been lost. Should the business cease trading, jobs will be lost.

Grounds of Appeal

30 15. The appellant submits that (i) as the payment was only a few days late, (ii) having regard to the appellant's financial circumstances including (a) the loss of its largest contract, (b) the consequence of insolvency if the penalty is enforced, the imposition of a penalty of such magnitude was extreme and disproportionate.

Discussion and Decision

35 16. The appellant recognises that it does not have a *reasonable excuse*, but argues that the surcharge is disproportionate, essentially on the basis that the payment was only three days late, and there was no risk to the revenue.

17. HMRC say that the surcharge was not disproportionate and that this Tribunal is bound by *Trinity Mirror*.

18. We agree that we are bound by the ratio of the decision in *Trinity Mirror*. The Upper Tribunal (UT) allowed HMRC's appeal and re-made the decision, holding that a default surcharge of some £70,000 based on 2% of the VAT due, in respect of a return and relative payment being only one day late, was **not disproportionate**. In particular, the UT held that a penalty of 2% could not be regarded as so disproportionate to the gravity of the infringement as to constitute an obstacle to the underlying aim of the directive (presumably the Principal VAT Directive - no express provision of the relevant EU directives is discussed in detail). In addition, the UT concluded that the surcharge liability regime was Convention compliant. While the penalty might be considered harsh, it could not, it was said, be regarded as unfair or devoid of all reasonable foundation.² No specific Article of the Convention is discussed.

19. Had we been free of binding authority, and had we been favoured with a comprehensive review of the authorities on *proportionality*, we might well have come to the conclusion that a penalty of £6,000 for a minor administrative failing of very short duration was so plainly and obviously unfair as to be manifestly inappropriate.³ The gravity of the infringement was minimal. We are unaware of any regulatory regime that imposes such large penalties for such minor administrative indiscretions. We respectfully suggest that the proportionality (in EU law) of the default surcharge regime requires urgent consideration by and guidance from the Courts on an appropriate occasion.

20. Proportionality, as a general principle of EU law, seems to us to be concerned primarily with the suitability of the measure in question to achieve the objective being pursued; and whether the measure is necessary to achieve the objective ie could it be achieved by less onerous means; this may also involve balancing the burden being imposed with the benefits obtained. Here, the burden is extreme.

21. It has, however, to be recognised that the legislature must be allowed a wide margin of appreciation, particularly in relation to the measures to secure the payment of taxes, where provisions are not fully harmonised.

22. In the light of *Trinity Mirror*, its reasoning and the relatively brief discussion before us, we cannot hold that the imposition of a penalty of some £6000 for a minor administrative error enduring some three days, in circumstances in which there was no loss of or risk to the revenue was disproportionate and liable to be set aside.

Disposal

23. With some regret, the appeal is dismissed.

² See paragraphs 71 and 72

³ See *R (Lumsdon) v Legal Services Board* [2015] 3 WLR 121 *Euro Trade and Finance Ltd* UKFTT 25/4/16 (Judge Mosedale)

24. 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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**J GORDON REID QC FCIarb
TRIBUNAL JUDGE**

RELEASE DATE: 25 MAY 2016

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