



**TC07901**

**Appeal number: TC/2019/01217**

*VAT default surcharges - insufficiency of funds - Appellant awaiting 'in year' CIS refund from HMRC - whether reasonable excuse - no - Appeal dismissed*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**TELEC UTILITIES LIMITED**

**Appellant**

**- and -**

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

**Respondents**

**TRIBUNAL: JUDGE: MICHAEL CONNELL  
MEMBER: MOHAMMED FAROOQ**

**Sitting in public at The Court House, Champney Road, Beverley, HU17 9EJ on  
11 February 2020**

**The Appellant Company was not represented**

**Ms Sophie Brown, Officer of HMRC, for the Respondents**

## DECISION

### **The Appeal**

1. Telec Utilities Limited (“the appellant”) appeals against a VAT default surcharge of £21,932.30, for its failure to submit in respect of its VAT period 05/15, by the due date, payment of VAT due. The surcharge was calculated at 15% of the VAT due of £146,215.36.
2. The appellant’s appeal to the Tribunal was out of time, but HMRC do not object to the appellant’s application for leave to appeal, which was granted.
3. The point at issue is whether the appellant has a reasonable excuse for making the late payment.
4. The appellant was not represented at 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.
5. On the same day as the hearing, but after the appeal had been heard, the appellant’s company accountant Ms Sarah Waites contacted the Tribunal Service to say the Company had not in fact received notice of the hearing. She said that the VAT default surcharge of £21,932.30 had however been paid in order ‘to settle the balance on the account’.
6. It was unclear whether the appellant had wished to withdraw the appeal. Given the grounds of appeal, it was assumed that they did not wish to do so.

### **Background**

7. The appellant has been VAT registered since 17 February 2012 and its business is that of construction of utility projects for electricity and telecommunications. Its VAT registration number is 127 0908 23 and this remains extant.
8. Prior to the default under appeal the appellant had previously defaulted on its VAT payment in period 11/12 when a VAT surcharge liability notice was issued. The appellant has been in the VAT default surcharge regime since then, having defaulted a further six times prior to the default period under appeal.
9. 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].
10. 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.
11. 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.

12. Period 05/15 VAT fell due on 7 July 2015 for electronic payments. The appellant submitted the return on time and paid after the due date in 5 instalments, the final payment was made on 1 September 2015, being 56 days late. A Surcharge Liability Notice Extension was issued on 17 July 2015 at 15% for the sum of £21,932.30.

13. 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 ..’

14. It is s 59(7)(b) on which the appellant seeks to rely. The burden falls on the appellant to establish that it has a reasonable excuse for the late payment in question.

15. 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 due is not a reasonable excuse.’

16. Although an insufficiency of funds to pay any VAT due is not a reasonable excuse, case law has established the principle that the underlying cause of any insufficiency of funds may constitute a reasonable excuse.

17. 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**

18. The appellant’s Notice of Appeal, received by the Tribunal Service on 20 February 2019 stated:

*“See attached letters/statements”*

However, the attachments were not included. HMRC spoke to Sarah Waites, the company accountant, by telephone on 19 March 2019 and Ms Waites agreed to forward the documents listed in the Notice of Appeal including “bank statement to show money was in bank”, “witness statement (director)” and “witness statement (accountant)”.

19. HMRC followed up the conversation by formally requesting the documents on 26 March 2019.

20. On 5 April 2019, Matthew Hague a director of the Company wrote to HMRC saying:

*I am writing in response to your letter dated 26<sup>th</sup> March 2019.*

*I am unable to find the statements referenced in the original paperwork but have enclosed a copy of the bank statement and the details of the appeal.*

*Telec Utilities received a Surcharge in July 2015, the appeal was made on the following grounds. The VAT was submitted on 2 July 2015, which was on time. At the time there was a credit amount on the CIS account which we were in communication with HMRC, this will be shown on the records at HMRC. Telec Utilities Ltd transferred to Gross Status in 2013 but continued to pay tax for the following year. I was advised that the amount would be confirmed and transferred over to the VAT account and the remaining amount if any, would be confirmed to me to pay. I went on holiday after the submission date and as I had not received confirmation of the credit amount on CIS, I was unsure if there was any VAT to pay. When I returned from my holiday, it was confirmed the amount of VAT had been to be paid and the CIS was to be sorted separately, this was not what we were advised initially.*

*I made the following payments to settle the account, the payment amounts are due to payment limits which were on our bank account at the time, £40,000 per day.*

08.08.15 £40,000

09.08.15 £40,000

24.08.15 £20,000

03.09.15 £53,391.87

*My company accountant, Sarah Waites has sent the appeal numerous times via letter, fax and email and has been chasing for a resolution. Sarah has been passed round many departments and been advised the first 3 times that HMRC had not received the paperwork. Sarah was also advised on 29.03.18 by Gillian at Glasgow reference CS10045, that the surcharge had been cancelled. This was also confirmed again on 28.09.18 after a phone call to HMRC.*

*Telec Utilities external accountant has been in communication with Sarah with regards to the CIS VAT account during 2015 as Sarah started employment (during 2015 and had not had time to go through the records when the appeal was done).*

*Please see attached copy of an email from her accountant confirming the credit balance we had on outside for CIS 2014-15. HMRC was questioning this at the time and advised the figures did not match. There have been numerous emails that Sarah has sent to resolve this. We are still waiting four years later.*

21. The appellant's grounds of appeal are in effect that an insufficiency of funds was created by circumstances outside its control. The appellant says that the shortage of funds significantly impacted upon its ability to discharge VAT on time.

### **HMRC's contentions**

22. The reverse of each default notice issued, up to and including period 05/15, contains details as to how surcharges are calculated and the percentages used in determining any financial surcharge in accordance with s5 9(5) VATA.

23. In accordance with s 59 VATA and s 40 VAT Regulations 1995, Section 21.1 of Notice 700 The VAT Guide (from January 2015) states:

*"You must make sure that your VAT return is received and any payment due clears HMRC's bank account by the due date shown on the return. If you fail to do this you could be liable to a default surcharge (see paragraph 21.2.2 below). Remember that if you are away from your place of business, you must make arrangements so that your VAT return is received and payment clears HMRC's bank account on time.*

*For more information about deadlines see the VAT Returns guidance. To help you work out when you need to set up a Direct Debit Instruction) or when you need to make your VAT payments, you can use the [VAT payment deadline calculator](#).*

*Prompt and correctly completed returns and payments are the best way of avoiding trouble. If you foresee any difficulty, your best course is to explain the circumstances in advance."*

24. Section 21.2.2 of Notice 700 The VAT Guide (from April 2012) states:

*"You are required by law to submit a VAT return and to make sure that payment of the VAT due has cleared to HMRC's bank account by the due date. If you fail to do so, you will be in default and you may have to pay a surcharge. A surcharge is an additional amount you may have to pay if you don't pay your return on time."*

25. The first default was recorded for period 11/12 and the appellant entered the default regime. The potential financial consequences attached to the risk of further default would have been known to the appellant from this point onward, given the information printed on the Surcharge Liability Notice.

26. The director has ultimate responsibility for the timely submission of the VAT return and any tax due thereon. The onus is on the appellant to ensure that they comply with tax regime requirements at all times and it is a reasonable expectation that an individual or business ensures they comply with their statutory obligations.

27. With regards to the Notice of Appeal, HMRC contacted the appellant by telephone on 19 March 2019 to explain that the documents mentioned in the Notice had not been attached. During that conversation the appellant's company accountant, Sarah Waites, stated that the payment had been late as *"there was no one in the office at the time"*.

28. The appellant did not take appropriate or sufficient steps to ensure they met their VAT payment obligation which was affected by the absence of staff. A reasonable and competent business would ensure arrangements were in place to cope with absence of key members of staff.

29. Reliance on a third party for completion, calculation and payment of VAT is excluded from providing a reasonable excuse by s 71 (1)(b) VATA.

30. The appellant states that they “*transferred to Gross Status in 2013 but continued to pay CIS tax for the following year*”.

31. HMRC’s records show that the appellant was not granted Gross Payment Status until 18 December 2015. Up until this date the appellant had been subject to deductions under the Construction Industry Scheme (CIS) at 20%. As such this would be considered to form part of its normal cash flow.

32. The appellant maintains they submitted their VAT return for period 05/15 on time, on 2 July 2015, and there was a credit amount on their CIS account at that time. They say that they were in communication with HMRC and maintain that they were advised that the CIS amount would be confirmed and transferred over to their VAT account, so that any remaining balance could be paid by the appellant.

33. Section 62(3) of the Finance Act 2004 states that CIS deductions are first to be treated as paid on account of any ‘relevant liabilities’ of the company. Relevant liabilities in this context means the company’s obligations to pay any PAYE, NICs or CIS deductions. Any excess CIS deductions determined at the end of the tax year when the Company has submitted its Employer Payment Summary (EPS) returns, can be set against Corporation Tax or repaid to the Company.

34. A trader must complete monthly EPS returns showing cumulative CIS deductions from its own income during the tax year. These amounts are off-set against the PAYE and NICs etc., it is due to pay for the tax year. Any excess of CIS deductions taken from the taxpayer’s own income is carried forwarded month by month until:

- I. All of the CIS deductions for the tax year are used, or
- II. The end of the tax year is reached.

35. A trader that has an excess of CIS deductions over and above the amount of tax that they are due to pay to HMRC in their capacity as an employer, will not be able to claim a repayment of these deductions until:

1. The final EPS for the year has been submitted (due by 19 April each year) where payments to employees are made in the period 06 March to 05 April.
- II. The contractor has paid all amounts due to HMRC for the tax year in their capacity as an employer/contractor.
- III. The tax year in which the CIS deductions were made from the contractor has ended.

36. Any excess CIS deductions which cannot be set-off and are still available at the end of the tax year may be refunded or set against other liabilities.

37. Repayment or off-set claims can only be dealt with when HMRC have reconciled the company’s CIS credits. If HMRC cannot agree the company’s whole claim they will ask for documents and supporting evidence of receipts. HMRC can consider a part repayment off-set for the deductions they can agree. Where there is a mismatch, HMRC will take up the discrepancy with the Company or Company agent.

38. The appellant has provided a copy of an email from their external accountant Trevor Davy dated 10 August 2015, stating that he had amended the original figure declared for the amount of CIS deductions to subcontractors for tax year 2014-15 in letters to HMRC dated 15 May 2015 and 9 June 2015.

39. The appellant also states in a letter received on 5 April 2019 regarding the CIS from 2014-15 “*HMRC was questioning this at the time and advised their figures did not match*”.

40. On 20 October 2015, Sarah Waites the Company accountant, spoke to HMRC and disputed the employer’s liability and the CIS credits for year 2014-15.

41. Any refund due is not available to be off-set against any other liabilities until such time as it is established that it is correctly due. HMRC contend that due to the ongoing issues, the CIS credit for 2014-15 was not reconciled and therefore not available for off-set on the due date of the 05-15 VAT return.

42. HMRC’s systems show notes of the ongoing dispute regarding the amount of CIS credits for year 2014-15. An established credit of £38,867.94 from 2014-15 was subsequently credited against the appellant’s PAYE on 15 December 2015.

43. However, until credit is agreed, it is not available for off-set. Whilst the appellant states they had a repayment due from CIS, they will have received the VAT due for the period under appeal at the due date to pay their VAT.

44. The appellant has provided a bank statement showing £398,463.08 in their bank account on the due date for the 05/15 VAT return, yet they still chose to rely on a CIS repayment to pay their VAT liability.

45. Regulation 40 of Value Added Tax Regulations 1995, states that “any person required to make a return” shall pay to HMRC “such amount of VAT as is payable by him in respect of the period to which the return relates not later than the last day on which he is required to make that return”. There is a statutory obligation on a person required to make a return, to pay the VAT to HMRC.

46. HMRC contend the appellant should not withhold a payment of a VAT return even if they are anticipating a refund from HMRC. Each VAT return is dealt with separately and any refund due in respect of another tax regime or VAT return will be refunded in due course.

47. The fact that the appellant is subject to CIS deductions which need to be verified at the end of a given tax year before any CIS overpayment can be agreed, does not go beyond normal hazards of business and as such, HMRC contend that this is not a reasonable excuse for the purposes of s 59(7) VATA. It is a reasonable expectation that a prudent business would put the necessary precautions in place to ensure they meet their legal obligations to submit VAT returns and payment by the due date.

48. HMRC note that in the case of *R (on the application of UK Tradecorp Ltd -v- Customs & Excise Commissioners)* [2004] EWCH 2515, Lightman J held:

“The right to deduct input tax was a fundamental principle of the common system of value added tax (VAT) established by the Sixth Directive and member states should not adopt measures designed to preserve the rights of the treasury which undermined the right to deduct VAT. However, the right to deduct did not arise as soon as a claim to deduct was

duly made. Moreover, the proposition that the claim itself was entitled to the same protection from derogation by national legislation as an admitted or established right to deduct was not correct. It was settled law that there was a critical distinction between an unadjudicated claim to input tax and an admitted or established claim. Until the claim was accepted or established there was no right to payment.”

49. The appellant states: “I went on holiday after the submission date and as I had not received the confirmation of the credit amount on CIS, I was unsure if there was any VAT to pay”.

50. HMRC maintain that a prudent person, exercising reasonable foresight and due diligence, having proper regard for their responsibility under the Tax Acts, would have put alternative payment measures in place if they were “unsure” whether a CIS credit would be available to cover the total VAT due for period 05/15 .

51. The appellant also maintains that they were advised that the amount of CIS credit for year 14/15 would be confirmed and transferred over to the VAT account.

52. Where there is a credit available from any CIS deductions, then this will in the first instance be set off against any outstanding PAYE and NIC liability and then secondly to Corporation Tax. Any balance remaining can be requested to be off-set against other heads of duty. HMRC have no records of such a request and in fact, the CIS credit for 14/15 was eventually off set against the appellant’s PAYE/NICS for months 1, 2 and 3 of year 2015-16 as confirmed in the appellant’s email to HMRC on 11 November 2015.

53. On 31 July 2015 the appellant’s Company accountant Sarah Waites, called HMRC’s Business Payment Support Helpline stating that the business had sufficient funds in its bank account, but were unable to pay in full due to a limit on daily transactions. The business wanted to make partial payments each day to clear the arrears and this would require three weeks to complete.

54. HMRC maintain that the onus is on the appellant to check their banks transaction limits and if not sufficient for business purposes, then to make arrangements that ensure their VAT obligations are met.

55. Section 108 of the Finance Act 2009 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.

56. HMRC accept that the appellant contacted the Business Payment Support Helpline on 31 July 2015 and a payment promise was agreed, however this was 24 days after the due date, and so relief under s 108 of the Finance Act 2009 could not apply.

57. There is no statutory definition of “reasonable excuse”. Whether or not a person had a reasonable excuse is an objective test and is a matter to be considered in the light of all the circumstances of the particular case.

58. In the Upper Tribunal case of *Christine Perrin*, at paragraph 81, Judges Herrington and Poole stated:

When considering a “reasonable excuse” defence, therefore, in our view the FTT can usefully approach matters in the following way:



(1) First, establish what facts the taxpayer asserts give rise to a reasonable excuse (this may include the belief, acts or omissions of the taxpayer or any other person, the taxpayer's own experience or relevant attributes, the situation of the taxpayer at any relevant time and any other relevant external facts).

(2) Second, decide which of those facts are proved.

(3) Third, decide whether, viewed objectively, those proven facts do indeed amount to an objectively reasonable excuse for the default and the time when that objectively reasonable excuse ceased. In doing so, it should take into account the experience and other relevant attributes of the taxpayer and the situation in which the taxpayer found himself at the relevant time or times. It might assist the FTT, in this context, to ask itself the question "was what the taxpayer did (or omitted to do or believed) objectively reasonable for this taxpayer in those circumstances?"

(4) Fourth, having decided when any reasonable excuse ceased, decide whether the taxpayer remedied the failure without unreasonable delay after that time (unless, exceptionally, the failure was remedied before the reasonable excuse ceased). In doing so, the FTT should again decide the matter objectively, but taking into account the experience and other relevant attributes of the taxpayer and the situation in which the taxpayer found himself at the relevant time or times.

59. HMRC maintain that the actions of the appellant should be considered from the perspective of a prudent person, exercising reasonable foresight and due diligence, having proper regard for their responsibilities under the VAT Act. The decision depends upon the particular circumstances in which the failure occurred and the particular abilities of the person who failed to file their return and/or make payment on time. The test is to determine what a reasonable trader, in the position of the appellant, would have done in those circumstances and by reference to that test to determine whether the conduct of the appellant can be regarded as conforming to that standard.

60. If there is a reasonable excuse it must exist throughout the period of default.

61. The appellant has not met that standard in its obligation to ensure payment of the VAT due for the period 05/15 was made on time.

62. HMRC's case is that the surcharge in respect of period 05/15 has been correctly issued in accordance with s 59(4) of the VAT Act 1994, payment having been received by HMRC after the due date.

## **Conclusion**

63. The appellant's grounds of appeal are that 'in year' CIS credits due to the company had not been refunded by HMRC and that consequently it suffered an insufficiency of funds.

64. The appellant was clearly aware of the due date for payment of its VAT and the potential consequences of late payment.

65. The Income Tax (Construction Industry Scheme) Regulations 2005 and Finance Act 2004 ss 61- 62 cover the requirement to deduct amounts under CIS and the treatment of the sums so deducted.

66. There is no provision that allows HMRC to off-set CIS deductions against the Company's VAT liability 'in year'. As such a limited company that has an excess of CIS

deductions over and above the amount of tax/NIC/CIS that it is due to pay to HMRC, will not be able to claim a repayment of those CIS deductions until:

- The final Employer Payment Summary for the year has been submitted (due by 19 April each year where payments to employees are made in the period 6 March to 5 April)
- The company has paid all amounts due to HMRC for the tax year, in its capacity as an employer/contractor
- The tax year in which the CIS deductions were made from the company has ended.

67. Value Added Tax Act 1994 (“VATA”), ss 59 and 71 set out the reasonable excuse provisions which apply to the default surcharge. It does not appear that the appellant Company was suffering any cash flow shortages but in any event, it is clear from s 71(a) VATA, that an insufficiency of funds to pay any VAT due is not in itself a reasonable excuse.

68. There was also nothing unforeseeable about the CIS deductions. As a sub-contractor within the CIS that did not qualify for ‘gross payment’ status, the deductions were clearly required by law and without set-off. They were an ordinary incident of trade.

69. The Company has not provided any evidence that it could not pay the VAT as it fell due. VAT never becomes the property of the Company. The money belongs to the Crown at all times and must be paid over as the law requires. The appellant should have had in place cash flow controls that ensured VAT was paid on time as and when it fell due.

70. The burden of proof is on the appellant to show that the underlying cause of its 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 05/15 period.

71. The appeal is accordingly dismissed and the surcharge upheld.

72. 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 CONNELL**

**TRIBUNAL JUDGE**

**RELEASE DATE: 27 OCTOBER 2020**



