TC07931

VAT – default surcharge – return received timeously – no payment made – can it be offset against un-adjudicated repayment claims? – no - DCM (Optical Holdings) Limited applied - can it be offset against cash seized – no - reasonable excuse – no - appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2019/05125

BETWEEN

MOHAMMAD AMEEN MIRZA **Appellant**

-and-

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

TRIBUNAL: JUDGE ANNE SCOTT

The hearing took place on 20 October 2020 by way of a video hearing on the Tribunal Video Platform. A face to face hearing was not held because of restrictions arising from the Covid-19 pandemic.

Mr T Nawaz, for the Appellant

Mr M Boyle, litigator of HM Revenue and Customs' Solicitor's Office for the Respondents

DECISION

INTRODUCTION

1. This is an appeal against a default surcharge in respect of period 02/19 in the sum of £3,701.55 issued by the respondents ("HMRC") on 12 April 2019 in terms of Section 59 Value Added Tax Act 1994 ("VATA").

Factual background

2. The appellant has been registered for VAT since May 1999 as a grocer/general store.

3. It is not disputed that the appellant has been in the default surcharge regime from 08/10 onwards and that a Surcharge Liability Notice ("SLN") was issued on 15 October 2010 and Surcharge Liability Notice Extensions ("SLNEs") were issued in respect of every subsequent period.

4. SLNs and SLNEs are computer generated by an automated process and state that the taxpayer has been sent the notice because it is in default. The percentage rates of surcharge are identified and advice is given on how to avoid defaults. In any event, all SLNs and SLNEs were issued to the appellant's principal place of business in accordance with Section 98 VATA and therefore in terms of Section 7 Interpretation Act 1978 they are deemed to have been delivered unless the contrary is proven.

5. Electronic VAT returns have been lodged for the periods 08/10 to 08/13 inclusive and 11/16 to 02/19 inclusive. Paper returns were lodged for periods 11/13 to 08/16 inclusive on 24 October 2016.

6. Where the returns were not received by the due date, the appellant was issued with centrally issued tax Assessments. The Assessments were set aside when the relevant return was submitted and the surcharge was recalculated.

7. The default surcharges for the periods 05/18, 08/18 and 11/18 were withdrawn on 12 August 2019 due to an error in the notification of the liability.

8. In addition to the centrally issued Assessments, Officer Assessments have also been issued.

9. The SLNE for 02/19 was issued on 12 April 2019. On 25 April 2019, the appellant's then accountant wrote to HMRC requesting a review on the basis that "…payment was not made as HMRC hold in excess of £500,000 seized from Mr Mirza and VAT returns submitted result in a credit still being due to him."

10. A review of the default surcharge for period 02/19 was undertaken on 8 July 2019 and the outcome was to uphold the surcharge.

11. It is not disputed that the return for period 02/19 shows VAT due in the sum of £24,677. If the default surcharge is upheld it is correctly calculated at the rate of 15% in the sum of £3,701.55.

12. The VAT due to HMRC for the periods 08/10 to 11/11 was paid.

13. No VAT has been paid since 02/12.

14. The appellant has lodged a number of claims for repayment of input tax and that has been the subject matter of extensive correspondence between the parties. HMRC have repeatedly requested evidence vouching those claims and, to date, in the absence of such evidence have not accepted the claims.

15. The appellant has lodged two appeals with the Tribunal (TC/2017/04646 and TC/2018/06162) in respect of VAT assessments relating to disallowed input tax. Those appeals have been sisted.

Appellant's arguments

16. In the Notice of appeal the appellant's agent stated:

> "This appeal is in respect of a surcharge which is incorrect as the return was submitted on time but without a payment as HMRC are already sitting on £559K worth of funds of the Appellant and as such no payment is being made until the funds are either returned or otherwise exhausted in any way."

17. In the appellant's Skeleton Argument, the appellant denies that payment had not been made on the basis that, as at the date of the submission of the return, the appellant had overpaid VAT to HMRC. The appellant produced a summary of the alleged VAT liabilities and that is derived from the returns for the period 02/12 to 08/19 inclusive.

18. It is argued that the appellant is due a net repayment of £190,289.32 and that looking at the "overall VAT account" there was therefore no tax due for 02/19. Therefore there can be no default surcharge.

19. Further, the appellant argues that there can be no unpaid liability for 02/19 because HMRC had "confiscated £559,200 from the appellant on 22 October 2015" and that the appellant is setting off sums due for ongoing liabilities for VAT, PAYE and Self-Assessment against that figure. The appellant calculates that, even allowing for that, HMRC owes him £251,386.99 as at 08/19.

20. In oral argument, Mr Nawaz argued that the sums seized (see paragraph 42 below) had not been subject to a "freezing order" and therefore were at the appellant's disposal unless and until a Proceeds of Crime Order was made (not that he expected that outcome).

HMRC's arguments

21. HMRC maintain that the appellant has no right to withhold payment of VAT due for the period 02/19 in anticipation of a refund from another period where an input tax claim has been submitted. Until the claim has been verified by HMRC any repayment is not available to the appellant.

22. The seizure of cash is not relevant. The appellant has charged VAT to his customers for period 02/19 and is under a legal obligation to render payment to HMRC in accordance with Regulation 40(2) of the Value Added Tax Regulations 1995 ("the 1995 Regulations").

The Law

23. Section 59 VATA reads:

> **"**59 The Default surcharge
> (1) Subject to subsection (1A) below, if, by the last day on which a taxable person is required in accordance with regulations under this Act to furnish a return for a prescribed accounting period-
> (a) the Commissioners have not received that return, or
> (b) the Commissioners have received that return but **have not received the amount of VAT shown on the return as payable by him for that period**,
> then that person shall be regarded for the purpose of this section as being in default in respect of that period." (my emphasis)

24. Section 59(7)(b) VATA provides that a surcharge does not arise in relation to a default if the taxpayer satisfies HMRC or, on appeal to the Tribunal, that there was a reasonable excuse for the default.

25. Regulation 40 of the 1995 Regulations reads:

"VAT to be accounted for on returns and payment of VAT

40. Save as the Commissioners may otherwise allow or direct—

(a) any person making a return shall account therein for all his output tax and all VAT for which he is accountable by virtue of Part XVI of these Regulations in respect of the period to which the return relates, and the amounts to be entered on that return shall be determined in accordance with these Regulations; and

(b) any person required to make a return shall **pay** to the Controller 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.**" (my emphasis)

Discussion

26. The appellant freely admits that he has paid no VAT in respect of period 02/19. His case was predicated on the argument that HMRC owes him money and he is entitled to set off current liabilities against that and thus payment had been made timeously. If he is wrong in that, he argues that he had every reason to believe that he was entitled to do so and thus he had a reasonable excuse for the default.

27. At the outset of the hearing Mr Nawaz argued that the appellant was entitled to offset the then current VAT liabilities against the repayment claims and he referenced the schedule attached to his Skeleton Argument. At that juncture he said that he was not arguing an offset against the cash seized by HMRC. It is not in dispute that HMRC have not accepted the repayment claims; indeed the appellant is indignant that matters have not progressed.

28. Neither party referred to the relevant law which applies where a claim for repayment is denied so I referenced it and read out the relevant quotations.

29. In *Garage Molenheide BVBA v Belgium*[1] ("Garage Molenheide") the Court of Justice ruled that national laws which enabled the tax authorities to retain, as a protective measure, refundable amounts of VAT where *inter alia* there were grounds for suspecting tax evasion, or where a debt was due by the taxpayer, did not contravene the provisions of the Directive concerning the right to deduct.

30. In this case the appellant's VAT "position" has been referred to the Crown Office and Procurator Fiscal Service. Mr Nawaz confirmed that on 14 October 2020 the process had moved ahead with service of documents, which might be an Indictment and which referred to VATA and the Proceeds of Crime Act ("POCA"). Nothing was produced to the Tribunal (nor did it need to be, I simply state the facts in the interests of transparency).

31. The *Garage Molenheide* decision was considered and applied by Lightman J in *R (UK Tradecorp Ltd) v C&E Commrs*[2] ("Tradecorp"), in which the Commissioners had delayed making repayments to a trader pending investigation of suspected missing trader intracommunity fraud. Lightman J made the following general observations (paragraph 18):

> "The Commissioners are under a duty to conduct a reasonable and proportionate investigation into the validity of claims for a refund and repayment and a duty to act proportionately both in respect of the investigation and in dealing with the taxable person's claims generally… The duty embraces an obligation to keep all investigations under review. The Commissioners are entitled to take a reasonable time to investigate claims prior to authorising deductions and repayments and what is a reasonable time within which to complete an investigation must depend on the particular facts... The availability and proper exercise of the Commissioners' powers of investigation are essential to maintain the fiscal neutrality of VAT and prevent refunds being made to parties not entitled to them. The postponement of repayment of input tax pending the outcome of the investigation is, as a matter of principle and subject to questions of proportionality, entirely compatible with the Sixth Directive. Whilst the burden of proof is upon the taxable person to establish that the investigation of his unadmitted and unadjudicated claim and

[1] [1998] STC 126
[2] [2005] STC 138

> the failure to make a part or interim payment is unreasonable or disproportionate, the burden is on the Commissioners to justify non-payment of it once the claim is admitted or established…".

32. Lord Doherty in *DCM (Optical Holdings) Limited v HMRC*[3] referred to that paragraph of *Tradecorp* (and two others) at paragraph 41 *et seq* and stated:-

> "41. It is common ground that HMRC are not bound to accept and give credit for a claim for input tax [Tradecorp] … Before deciding whether to accept a claim HMRC are entitled to scrutinise it and subject it to a process of verification, notwithstanding the fact s25(2) and (3) and Sched 11, paras 1 and 4 do not make express provision to that effect …
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> 43. Rather, the crux is whether HMRC have the power to refuse to accept (in whole or in part) a sum claimed as input tax. We agree with the FTT and the UT that it is clear that HMRC do have that power. In our opinion, just as it is implicit in s25(2) and (3) and Sched 11, paras 1 and 4 that the allowance of an input tax claim is conditional upon the claim's verification, it is also implicit in those provisions that HMRC may accept or reject the claim in whole or in part. The fact that the input tax which is claimed and the input tax which is in fact allowable may differ is self-evident – that is why the process of verification and adjudication is necessary. The fact that the input tax claimed and the input tax allowed may differ is also recognised elsewhere in VATA (eg in s79(2)(c)).

33. Shortly put, HMRC have the appellant's repayment claims and they have not been accepted. Unless and until a Tribunal finds in the appellant's favour and upholds those claims no sums are due to the appellant. Therefore, insofar as set off against the repayment claims are concerned, the appellant has **not** paid the tax due for 02/19 and the default surcharge has been competently and timeously raised and notified and is in the correct amount.

34. Mr Nawaz, very properly, conceded that in light of that case law the appellant would be unable to offset VAT due in 2019 against un-adjudicated repayment claims.

35. He therefore reverted to the argument in the Notice of Appeal to the effect that he was entitled to set off the then current liabilities against the sums seized by HMRC.

36. In that regard he relied upon a letter dated 8 November 2019 ("the Letter") from HMRC Fraud Investigation Services to the appellant's agent (not Mr Nawaz) which he argued meant that HMRC had agreed that there could be such a set off.

37. The copy in the Bundle I hold is not capable of being read by me but Mr Nawaz read it out to the Tribunal and HMRC very helpfully subsequently provided a clear copy. The first paragraph does not relate to the appellant but to companies owned by his sons. As I pointed out, any arrangement with any other taxpayer cannot, and does not, impact on this appeal.

38. The part of the Letter that relates to the appellant reads as follows:-

> "The report made to COPFS concerns Value Added Tax (VAT) for periods up to 2015. I understand that the civil assessments of VAT issued by HMRC for those periods have been appealed to a First Tier Tax Tribunal by Mr Mirza and that the collection of those VAT debts are suspended pending the outcome of that tribunal. I also understand from the HMRC department that deals with such appeals that the tribunal hearing is itself sisted until the outcome of the criminal case is known.
>
> I believe that Mr Mirza has also been issued with assessments for other taxes and is accruing debts for other ongoing liabilities to HMRC. These other taxes and liabilities are entirely outwith our criminal investigation and I believe the amounts outstanding are far in excess of any cash seized.
>
> Mr Mirza should contact the HMRC department that issued the assessments and/or the HMRC Debt Management department that has contacted him for payment with any representations that he wishes to make. I understand that the firm of T Nawaz & Co may have done so already on his behalf."

39. Mr Nawaz confirmed to the Tribunal that he had contacted HMRC about income tax assessments in excess of £1m where HMRC had refused to admit late appeals but on 15 January 2019, the day before a Tribunal hearing, the late appeals were admitted and all of

[3] [2020] CSIH 60

the tax postponed. He had not contacted the VAT authorities since he had understood that ongoing VAT liabilities could be set off against the repayment claims.

40. I simply cannot accept that the Letter authorises the appellant to offset liabilities against the sums seized and nor would it have been reasonable for the appellant or his advisors to think so. The Letter is explicit and points out in the second paragraph that the amounts outstanding "**are far in excess of any cash seized**". It also effectively states that the appellant should negotiate with HMRC, if so advised.

41. I asked whether the appellant or his accountant had ever asked for a Time to Pay Agreement ("TTP") (in terms of section 108 Finance Act 2009) in respect of VAT. The simple, and honest, answer was "No" because they had always relied on the fact that they had very large repayment claims. Mr Nawaz argued that it was entirely reasonable for the appellant to believe that he could make such a set off. That amounted to a reasonable excuse if the appellant was not entitled to set off liabilities, so therefore payment had not been made and the Default Surcharge regime applied.

42. I will deal with the concept of reasonable excuse later.

43. No evidence was produced in relation to the seizure beyond the fact that HMRC accompanied by Police Scotland, had seized documents and certainly £550,200 in a raid on 22 October 2015. Mr Nawaz showed the Tribunal hearing a "Property Control Sheet" relating to the seizure. Given his statement that the Proceeds of Crime Act ("POCA") has been invoked in the recent process (see paragraph 19 above), on the balance of probability, the seizure was rooted in POCA and therefore the basic and clear point is that the cash having been seized, the appellant had, and has currently, no control at all in regard thereto. He certainly has no access to those funds nor is he likely to have, if at all, until the criminal proceedings conclude.

44. The issue of freezing orders is not relevant since it is cash that has been seized.

45. By any standard, as the writer of the Letter, upon which the appellant relies, made explicit, the various liabilities far exceed the sums seized. The disputed income tax liabilities of £1m alone are far in excess of the cash seized. Therefore it is difficult to understand why the appellant might have any grounds to think that PAYE, VAT or anything else should be offset against the seized sums. The Letter makes that clear.

46. HMRC argue that they have not received the VAT due. The Oxford English Dictionary states that to "receive" means "To take or accept into one's hands". HMRC have not "taken" that sum of money as the appellant cannot unilaterally state that part or all of any sums seized by HMRC represent VAT due more than three years later. Patently, HMRC do not accept that they have taken anything or that they have received payment of VAT. I agree with HMRC that the sums seized by HMRC in 2015, cannot possibly be described as payment of VAT in 2019.

47. The appellant's primary argument that he is not in the Default Surcharge regime because he has "paid" the VAT is simply not accepted for the reasons given.

48. Lastly, I point out that VAT never becomes the property of the taxpayer; it belongs to the Crown at all times and must be paid over as the law requires and in this case that is Regulation 40 of the 1995 Regulations.

49. I must therefore turn to reasonable excuse.

50. Was there any reasonable excuse? There is no statutory definition of reasonable excuse. HMRC correctly referred to *Rowland v HMRC*[4] which at paragraph 18 makes it clear that a reasonable excuse "… is a matter to be considered in the light of all the circumstances of the particular case".

51. I agree with Judge Tildesley in *Schola UK Limited v HMRC*,[5] which although not looking at VAT, indicates that in considering a reasonable excuse the Tribunal must consider the actions of the appellant from the perspective of a prudent taxpayer exercising reasonable foresight and due diligence whilst also having proper regard for his responsibility under the Tax Acts.

52. HMRC, and indeed the appellant, also relied on *Perrin v HMRC*[6] where the Upper Tribunal stated:

> "70 … the task facing the FTT when considering a reasonable excuse defence is to determine whether facts exist which, when judged objectively, amount to a reasonable excuse for the default and accordingly give rise to a valid defence. The burden of establishing the existence of those facts, on a balance of probabilities, lies on the taxpayer….
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> 71. In deciding whether the excuse put forward is, viewed objectively, sufficient to amount to a reasonable excuse, the tribunal should bear in mind all relevant circumstances; because the issue is whether the particular taxpayer has a reasonable excuse, the experience, knowledge and other attributes of the particular taxpayer should be taken into account, as well as the situation in which that taxpayer was at the relevant time or times (in accordance with the decisions in *The Clean Car Co* and *Coales*)….
>
> 75. It follows from the above that we consider the FTT was correct to say (at [88] of the 2014 Decision) that 'to be a reasonable excuse, the excuse must not only be genuine, but also objectively reasonable when the circumstances and attributes of the actual taxpayer are taken into account'."

53. Firstly, no evidence was led as to the appellant's state of mind or indeed his attributes. All that is known about him is that he is a businessman who is in dispute with HMRC and is facing possible criminal prosecution in relation to VAT. He was professionally advised. Mr Nawaz stated that the accountants had had documents seized on three or four occasions and as can be seen from paragraph 8 above it was they who advanced the original arguments for non-payment of VAT. It was simply argued by Mr Nawaz that the appellant's actions in making no payments and relying on sums that he believed were due to him had been entirely reasonable.

54. Was it reasonable for the appellant to believe that he could offset current (2019) VAT liabilities against the repayments that he had claimed? The short answer to that is that *Tradecorp* is not new law and the appellant has been professionally advised throughout, albeit Mr Nawaz has only been retained latterly. Firstly, even if he thought that he could offset the liability the appellant's representative, and indeed he, should have known about TTP arrangements; the appellant has been in the Default Surcharge regime since 08/10 and no payment of VAT has been made since 02/12. The Letter flagged up the need to talk to HMRC. Nothing was done in relation to VAT and TPP. That does not amount to a reasonable excuse.

55. If his accountant had told him that he could offset it without seeking TTP then that advice was incorrect.

56. I was not referred to it, and it does not deal with VAT, but I am bound by the principle enunciated by the Upper Tribunal in *HMRC v Katib*[7] where at paragraph 58 they stated:

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[4] 2006 STC (SCD) 536

[5] 2011 UKFTT 130 (TC)

[6]

[7] [2019] UKUT 189 (TCC)

> "58. It is clear from the Decision that Mr Bridger did not provide competent advice to Mr Katib, misled him as to what steps were being taken, and needed to be taken, to appeal against the PLNs and failed to appeal against the PLNs on Mr Katib's behalf (see [7] and [16]). But extraordinary though some of Mr Bridger's correspondence was, the core of Mr Katib's complaint is that Mr Bridger was incompetent, did not give proper advice, failed to appeal on time and told Mr Katib that matters were in hand when they were not. In other words, he did not do his job. That core complaint is, unfortunately, not as uncommon as it should be. It may be that the nature of the incompetence is rather more striking, if not spectacular, than one normally sees, but that makes no difference in these circumstances. It cannot be the case that a greater degree of adviser incompetence improves one's chances of an appeal, either by enabling the client to distance himself from the activity or otherwise."

57. In summary, if the appellant's then advisor did not know about *Tradecorp* or did not advise him about that, that is not a reasonable excuse. He knew or should have known that the repayment claims had not been agreed with HMRC and are the subject of a long running dispute. There is no guarantee that the repayments will ever be agreed. TTP should have been sought and agreed in advance of the due date. It was not. The appellant's remedy is with his advisor. It does not amount to a reasonable excuse.

58. As far as a set off against the funds seized are concerned, the onus of proof lies with the appellant but no evidence has been produced. As I indicate at paragraph 43 the terms of the Letter are very clear. The fact is that HMRC got a warrant to seize those funds in 2015 and that certainly does not mean that those funds are at the appellant's disposal or that he can decide how they should be applied. Looked at objectively, the possibility exists that he may never be able to access those funds.

59. In terms of Regulation 40 of the 1995 Regulations the appellant was obliged to pay the VAT that he had received from his customers to HMRC by the due date. He did not. He has no reasonable excuse for failing to do so.

60. The appeal is therefore dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

61. 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.

ANNE SCOTT

TRIBUNAL JUDGE

RELEASE DATE: 9 NOVEMBER 2020