TC07126

[2019] UKFTT 287 (TC)

VAT - PENALTIES – section 59(7) VAT Act 1994 - default surcharge – whether genuine but mistaken belief that direct debit in place reasonable excuse – yes - appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2018/03509

BETWEEN

NORFOLK PREMIER COACHWORKS LIMITED** **Appellant**

-and-

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

TRIBUNAL: JUDGE GREG SINFIELD
MRS JANET WILKINS

Sitting in public at The Old Bakery, 115 Queens Road, Norwich NR1 3PL on 17 April 2019

Gary Steward, director of the Appellant, for the Appellant

Alexander Danks, litigator of HM Revenue and Customs' Solicitor's Office, for the Respondents

DECISION

INTRODUCTION

1. This is an appeal by Norfolk Premier Coachworks Limited ("NPCL") against a VAT default surcharge for accounting period 12/17 at the rate of 15% amounting to £2,635.50 issued by the Respondents ("HMRC"). For the reasons given below, we have decided that the appeal should be allowed.

LIABILITY FOR A DEFAULT SURCHARGE

2. Regulation 25(1) of the VAT Regulations 1995 provides that a person who is registered for VAT (or liable to be so registered) must submit a VAT return to HMRC no later than the last day of the month next following the end of the VAT accounting period to which it relates. Under regulation 40(2), any person required to make a return must pay any VAT shown as payable on the return to HMRC not later than the last day on which that return is due. However, there is a seven day extension for persons who pay by Direct Debit and a ten day extension for persons who submit their VAT returns online and use the Online VAT Direct Debit.

3. Liability for a default surcharge arises under section 59 VATA94. Section 59(1) provides that a taxable person is in default where HMRC do not receive a VAT return and any VAT shown as payable on such return on or before the due date. Where a person is in default, HMRC may issue a surcharge liability notice ('SLN'). If, having been served with a SLN, the taxable person defaults again during the period of one year ('the Surcharge Liability Period') from the end of the period of default, the person becomes liable to a surcharge. On each subsequent default, the Surcharge Liability Period is extended to run for 12 months from the end of the latest period of default.

4. The surcharge is the greater of £30 and a specified percentage of the outstanding VAT. The percentage specified increases according to the number of VAT periods in respect of which the person is in default during the Surcharge Liability Period starting with 2% for the first period of default. For the second period in respect of which the taxable person is in default during the Surcharge Liability Period, the specified percentage is 5%. The maximum percentage is 15% where there have been four or more periods in default during the Surcharge Liability Period.

5. Section 59(7) VATA94 provides that a taxable person is not treated as in default in respect of any VAT period if the person satisfies HMRC, or on appeal the FTT, that in respect of the period:

   (1) the return or the VAT due was despatched at such a time and in such a manner that it was reasonable to expect that it would be received by HMRC within the time limit; or

   (2) there is a reasonable excuse for the return or VAT not having been so despatched.

6. Section 71(1)(a) VATA94 provides that for these purposes an insufficiency of funds to pay any VAT due is not a reasonable excuse. Section 71(1)(b) VATA94 further provides that, where reliance is placed on any other person to perform any task, neither the fact of that reliance nor any dilatoriness or inaccuracy on the part of the person relied upon is a reasonable excuse.

EVIDENCE

7. HMRC provided a bundle of documents. As well as the notice of appeal and statement of case, it included correspondence between NPCL and HMRC, schedules of defaults and payments and a helpful glossary of terms. Mr Steward gave oral evidence about the events that gave rise to the default surcharge.

FACTUAL BACKGROUND

8. In an appeal such as this, HMRC have the burden of proving that the appellant failed to pay the VAT on time and is liable to pay the default surcharge. The onus then passes to the appellant to prove that he had a reasonable excuse for his failure to pay on time. There was no dispute about the relevant facts. Mr Steward fully accepted that NPCL had failed to pay VAT by the due date previously as set out in [9] below and did not contest the default surcharges for those periods. The only issue in the appeal was whether NPCL had a reasonable excuse for its failure to pay the VAT due for period 12/17 on time. On the basis of the parties' evidence, which we accept, we find that the material facts are as set out below.

9. HMRC produced a schedule of NPCL's defaults which was accepted by Mr Steward. It showed that NPCL had been in the default surcharge regime since period 06/16 and was as follows:

Period	Due date	Amount due	Date of return	Amount paid late	Surcharge %	Surcharge amount
06/16	07/08/16	16,099.80	07/08/16	16,099.80	SLN issued	0.00
12/16	07/02/17	14,223.49	07/02/17	14,223.49	2%	0.00
03/17	07/05/17	22,427.28	04/05/17	22,427.28	5%	1,121.39
06/17	07/08/17	9,479.64	02/08/17	9,479.64	10%	947.96
12/17	07/02/18	17,570.00	02/02/18	17,570.00	15%	2,635.50

As stated above, where payment is made electronically, the due date for payment is extended to seven days after the statutory due date unless that falls on a bank holiday or weekend when the payment must be made before. The due dates in the table above reflect the fact that NPCL made payments of VAT due electronically.

10. In relation to period 06/16, NPCL sought and was granted approval from HMRC for a time to pay arrangement but only after the due date for payment had passed. Under the agreed time to pay arrangement, NPCL paid HMRC the amount due in six instalments of £2,683.30 each between 26 August and 29 September 2016. The first instalment was paid using the Telephone Payment Service ("TPS"). The TPS is a method by which payments can be made to HMRC by telephone using a debit or credit card. The other instalments were paid at weekly intervals by the National Direct Debit Service/System ("NDDS"). The NDDS is a direct debit system used for specified amounts and dates.

11. NPCL sought approval for a time to pay arrangement again in relation to period 12/16 but only after the due date for payment had passed. Once again, NPCL entered into a time to pay arrangement with HMRC under which NPCL paid the VAT due. This time in nine instalments. The first instalment of £4,223.49 was paid by the Faster Payment Service/Scheme ("FPS") on 10 February 2017. The FPS is a system which allows payments to be made between banks on the same day. The balance was paid using the NDDS in eight weekly instalments of £1,250 between 16 February and 6 April 2017.

12. On 10 February 2017, ie the date of the payment of the first instalment of VAT due for period 12/16 by the FPS, a letter was sent by HMRC advising NPCL that its Direct Debit had been cancelled. The letter of 10 February 2017 from HMRC to NPCL was headed "Advice of cancelled Direct Debit Instruction" and stated:

> "This is to advise you that the above Direct Debit Instruction has been cancelled.
>
> If you wish to pay your VAT by Direct Debit in the future you will have to complete another Direct Debit Instruction, either online or by sending us a paper Instruction."

13. A further letter was sent by HMRC on 13 February 2017. That letter was headed "Unpaid Direct Debit". It was sent following failure of a payment by Direct Debit on 10 February and stated:

> "The Direct Debit payment described above has been returned unpaid as your bank has stated that your Direct Debit Instruction (DDI) has been cancelled.
>
> HM Revenue and Customs will not make a further request for this payment by Direct Debit. This means that you need to arrange to pay the amount shown immediately, unless you have already done so.
>
> …
>
> If you wish to continue to use the Direct Debit, you will need to set up a new instruction."

14. By the time the letter of 13 February was sent, the amount agreed under the time to pay arrangement to be payable on 10 February had already been paid by NPCL using the FPS. The February letters show that, prior to 10 February 2017, NPCL had a Direct Debit in favour of HMRC in place. Notwithstanding those letters, payments were made on 16 February and weekly thereafter until 6 April by the NDDS.

15. Mr Steward said that he was not aware of the February 2017 letters from HMRC. Correspondence with HMRC would have been dealt with by the company's bookkeeper. In response to a question from the Tribunal, Mr Steward confirmed that he dealt with the bank and matters concerning it so he would have expected the bookkeeper to show him or tell him about the letters but he had no recollection of them. The company's bookkeeper left NPCL early in 2018 and sadly died shortly thereafter.

16. In relation to period 03/17, NPCL once again sought and was granted approval for a time to pay arrangement after the due date for payment had passed. NPCL made the first payment of £11,000 on 8 May by the TPS. That was followed by six instalments of £1,500 and a further instalment of £2,424.92, all paid at paid weekly intervals until 27 June 2017 using the NDDS. Mysteriously, the final payment left £2.36 unpaid, however, the schedule of payments shows that £3.00 was paid to HMRC on 29 March 2018 by the NDDS.

17. In relation to period 06/17, NPCL asked for a time to pay arrangement but HMRC refused to grant it. NPCL paid the amount due in two instalments. The first instalment of £3,479.64 was paid on 8 August 2017 using the TPS. The second instalment of £6,000 was paid on 4 September 2017 using the FPS.

18. In relation to the period under appeal, period 12/17, the due date was 7 February 2018 for electronic submission of the VAT return and payment of VAT due. NPCL's return was received before the due date on 2 February 2018. In a telephone call on 6 February 2018, ie the day before the due date, NPCL asked HMRC for time to pay. HMRC refused.

19. Mr Steward said that when HMRC refused to grant NPCL time to pay the VAT due for period 12/17, they made great efforts, including personal borrowing, to ensure that there were sufficient funds to pay HMRC. On 7 February, NPCL's bank account had sufficient funds to

pay the VAT due of £17,570 but the money remained in the account. No payment was made to HMRC on 7 February because there was no Direct Debit in place.

20. Mr Steward only discovered that the payment had not been made when he checked the account on 9 February and found that the money still in the bank account. He then immediately telephoned HMRC and made a payment by debit card using the TPS. The payment was received by HMRC on 9 February, ie two days later than the due date.

GROUNDS OF APPEAL

21. NPCL's grounds of appeal, in so far as material, were as follows:

> "We had a dreadful 12 months trading during 2017 due to a very large debt. As a consequence we have had to enter into arrangements with HMRC and other creditors to survive. We have not missed one payment on any of these.
>
> When it came to the return in question we contacted HMRC to see whether we could make 2 payments instead of one as we did not have sufficient funds to meet the whole liability. We were told "no" so we moved heaven and earth to get funds together to meet payment. I even borrowed personally £8000, as evidenced by our bank statements to ensure funds were there on the 7th February 2018. When the monies were not collected, I telephoned HMRC on the 9th Feb and made a VISA payment for the full amount. The only thing we got wrong was that we were unaware that an effective [Direct Debit Mandate] was not in force.
>
> To be charged 15% of the liability as a fine seem so incredibly harsh when we had made attempts to keep everyone informed and remained proactive after the due date. We do take our HMRC liabilities seriously."

22. The grounds of appeal raise two issues, namely:

(1) reasonable excuse; and

(2) fairness or proportionality.

REASONABLE EXCUSE

23. The Upper Tribunal has recently considered the correct test for reasonable excuse in *Perrin v HMRC* [2018] UKUT 156 (TCC). At [75], the Upper Tribunal concluded that the FTT in that case had correctly stated 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."

24. The full passage is at [69] – [76]:

> "69. Before any question of reasonable excuse comes into play, it is important to remember that the initial burden lies on HMRC to establish that events have occurred as a result of which a penalty is, prima facie, due. A mere assertion of the occurrence of the relevant events in a statement of case is not sufficient. Evidence is required and unless sufficient evidence is provided to prove the relevant facts on a balance of probabilities, the penalty must be cancelled without any question of "reasonable excuse" becoming relevant.
>
> 70. Assuming that hurdle to have been overcome by HMRC, 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. In making its determination, the tribunal is making a value

judgment which, assuming it has (a) found facts capable of being supported by the evidence, (b) applied the correct legal test and (c) come to a conclusion which is within the range of reasonable conclusions, no appellate tribunal or court can interfere with.

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*).

72. Where the facts upon which the taxpayer relies include assertions as to some individual's state of mind (e.g. "I thought I had filed the required return", or "I did not believe it was necessary to file a return in these circumstances"), the question of whether that state of mind actually existed must be decided by the FTT just as much as any other facts relied on. In doing so, the FTT, as the primary fact-finding tribunal, is entitled to make an assessment of the credibility of the relevant witness using all the usual tools available to it, and one of those tools is the inherent probability (or otherwise) that the belief which is being asserted was in fact held; as Lord Hoffman said in *In re B (Children)* [2008] UKHL 35, [2009] 1AC 11 at [15]:

> "There is only one rule of law, namely that the occurrence of the fact in issue must be proved to have been more probable than not. Common sense, not law, requires that in deciding this question, regard should be had, to whatever extent appropriate, to inherent probabilities."

73. Once it has made its findings of all the relevant facts, then the FTT must assess whether those facts (including, where relevant, the state of mind of any relevant witness) are sufficient to amount to a reasonable excuse, judged objectively.

74. Where a taxpayer's belief is in issue, it is often put forward as either the sole or main fact which is being relied on – e.g. "I did not think it was necessary to file a return", or "I genuinely and honestly believed that I had submitted a return". In such cases, the FTT may accept that the taxpayer did indeed genuinely and honestly hold the belief that he/she asserts; however that fact on its own is not enough. The FTT must still reach a decision as to whether that belief, in all the circumstances, was enough to amount to a reasonable excuse. So a taxpayer who was well used to filing annual self assessment returns but was told by a friend one year in the pub that the annual filing requirement had been abolished might persuade a tribunal that he honestly and genuinely believed he was not required to file a return, but he would be unlikely to persuade it that the belief was objectively a reasonable one which could give rise to a reasonable excuse.

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."

76. The FTT therefore identified the correct legal test for deciding whether the facts that it had found amounted to a reasonable excuse."

25. The approach to be taken by the FTT in a reasonable excuse case is described in [81] of *Perrin* as follows:

> "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 proven.
>
> (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."

SUBMISSIONS

26. Mr Steward explained by way of background that, in October 2016, a customer of NPCL became insolvent leaving the company with a bad debt that was subsequently assessed as £160,000. That caused significant cash flow problems for NPCL. The company had various time to pay arrangements with HMRC and other creditors and gradually got back on its feet. Mr Steward said that he had believed that the payment for period 12/17 would be made on time by Direct Debit and when he discovered that it had not been, he took steps to pay the VAT due as soon as possible. Mr Steward also contended that a penalty of 15% for a two day delay seemed to be unfair and disproportionate.

27. Mr Danks submitted that the NDDS is materially different to the Direct Debit. The NDDS is a different form of direct debit which is initiated by the payer to make payment of a specified amount on a given date following a time to pay agreement with HMRC. The Direct Debit, however, specifies neither the amount payable nor the date for payment but enables HMRC to collect payments of tax due. Mr Danks acknowledged that some confusion may exist. That was reflected HMRC's statement of case which stated:

> "This could potentially [be] where confusion has arisen on the part of the Appellant where they believed that a [Direct Debit Mandate] was still in place. However genuine mistakes, honesty and acting in good faith are not usually considered reasonable excuses for surcharge purposes, unless it can be shown that in the particular circumstances concerned, the actions of the trader were reasonable."

28. HMRC's view, as expressed in the statement of case, is that the actions of the taxpayer should be considered from the perspective of a prudent person, exercising reasonable foresight and due diligence, having proper regard for their responsibilities under the legislation. Whether there is a reasonable excuse depends on the particular circumstances in which the failure occurred and the particular circumstances and abilities of the person who failed to file their return on time. The test is to determine what a reasonable taxpayer, in the position of the actual taxpayer, would have done in those circumstances and, by reference to that test, to determine whether the conduct of the taxpayer can be regarded as conforming to that standard.

29. Mr Danks submitted that a mistaken belief could not be a reasonable excuse. We were referred to Tribunal's comment in *Garnmoss Ltd (/a Parham Builders) v HMRC* [2012] UKFTT 315 (TC) ("*Garnmoss*") at [12]:

> "What is clear is that there was a muddle and a bona fide mistake was made. We all make mistakes. This was not a blameworthy one. But the Act does not provide shelter for mistakes, only for reasonable excuses. We cannot say that this confusion was a reasonable excuse."

30. Mr Danks explained that when a return is filed electronically, the system explains when and how the amount due must be paid. Mr Danks submitted that, on submitting the return for 12/17, NPCL would have received an acknowledgement that indicated that any tax due must be paid electronically (by BACS, CHAPS, FPS), however, we were not provided with any copy of such acknowledgement.

31. In relation to the issue of proportionality or unfairness, Mr Danks referred us to the decision of the Upper Tribunal in *HMRC v Trinity Mirror Plc* [2015] UKUT 421 (TCC) ('*Trinity Mirror'*). That case concerned a filing of a VAT return and payment of VAT due that was late by one day. The Upper Tribunal held that the surcharge regime, viewed as whole, is a rational scheme that does not infringe the principle of proportionality under EU law.

DISCUSSION

32. All other relevant matters, such as lateness of payments and liability to previous default surcharges being agreed or not disputed, the only issues in this appeal are whether NPCL had a reasonable excuse for the payment for period 12/17 not being made by the due date and, if not, whether the default surcharge of £2,635.50 is disproportionate.

33. The first ground of appeal put forward by NPCL is that it had a reasonable excuse in that Mr Steward genuinely but mistakenly believed that NPCL had an effective Direct Debit in place. We accept that Mr Steward genuinely believed that the payment of the VAT due for period 12/17 would be taken from NPCL's bank account by Direct Debit on 7 February 2018. We say this because we accept his evidence and because it would be offensive to common sense to suggest that the directors of NPCL would take pains, including personal borrowing, to ensure that it had the money to pay HMRC and then deliberately leave that money sitting in its account. Indeed, we did not understand Mr Danks to suggest that Mr Steward did not genuinely believe that NPCL had a Direct Debit in place.

34. Mr Danks's submission was that a mistaken belief is not a reasonable excuse. We disagree. It is clear from *Perrin* that a mistaken belief can be a reasonable excuse if the belief was objectively reasonable. The qualification that the mistake must be objectively reasonable is critical. As the Upper Tribunal says in [74], a genuine belief on its own is not enough. As well as being genuinely held, the belief must, when the circumstances and attributes of the particular taxpayer are taken into account, be objectively reasonable to be capable of being a reasonable excuse.

35. We also consider that Mr Danks's reliance on the passage from *Garnmoss* is misplaced. The "muddle" referred to in that case was an accounting entry error which resulted in an underpayment of VAT. It was a deliberate decision to underpay the tax due not as the result of a mistaken belief as to the existence of a state of affairs (eg that a Direct Debit was in place) but as a result of a misposted journal entry on the accounting system. That is a very different mistake to the one in this case. In any event, *Perrin* is a decision of the Upper Tribunal which is binding on us and, in so far as there is any inconsistency between it and *Garnmoss*, *Perrin* must be preferred.

36. The question for us is whether Mr Steward's belief that the payment of the VAT due would be taken from NPCL's bank account on 7 February by Direct Debit was objectively reasonable. Taking account of NPCL's VAT payment history, we consider that Mr Steward's belief that there was a Direct Debit arrangement in place that would result in the payment being taken from the account on 7 February 2018 was objectively reasonable. We say that because NPCL had paid amounts of VAT due to HMRC by NDDS in August and September 2016 and February, March, April, May and June 2017. Mr Danks contended that the letters in February 2017 clearly advised NPCL that its Direct Debit had been cancelled. In our view, the position was far from clear because, notwithstanding those letters, payments of VAT continued to be made via NDDS. However, in the absence of a time to pay arrangement, no specified amounts or dates had been agreed which would be paid via NDDS in relation to period 12/17.

37. We consider that it is understandable that a person such as Mr Steward might have failed to appreciate the distinction between a Direct Debit and the NDDS. Indeed, the author of HMRC's statement of case recognised that as a potential source of confusion (see [27] above). We were not referred to any published guidance that stated that the NDDS was only used to make payments of specified amounts on specified dates and we accept that Mr Steward did not appreciate the distinction between a Direct Debit and the NDDS. We also note that the distinction is blurred in HMRC's own guidance. In the Direct Debits FAQs section on HMRC's website it states:

> "Is Direct Debit payment the same as National Direct Debit Service/System (NDDS)?
>
> Yes, this is the same service."

38. The confusion means that, even if Mr Steward had been aware of the letters in February 2017 stating that NPCL's Direct Debit had been cancelled, he might reasonably have believed that it had been reinstated because the company continued to make payments by the NDDS after that date. In fact, we accept that Mr Steward did not know about the letters cancelling the Direct Debit.

39. Taking account of NPCL's VAT payment history as well as the experience and knowledge of Mr Steward, we conclude that his belief that that NPCL had an effective Direct Debit in place was objectively reasonable and was a reasonable excuse for the payment of the VAT due for period 12/17 not being made on the due date.

40. We also find that, once he became aware of the situation on 9 February 2017 (and the reasonable excuse ended), Mr Steward took steps to pay the VAT due without unreasonable delay on the same day.

41. We discussed whether the bookkeeper's departure and unfortunate death at or around the time of the payment was due may have contributed to the mistaken belief and/or the late payment in February 2017. On reflection, we concluded that we should not give this any weight

as we did not have any clear evidence of the impact on the payment of the VAT due and it appears that Mr Steward dealt with the bank.

42. Mr Steward also contended that a penalty of 15% for a two day delay was unfair and disproportionate. We are bound by the decision of the Upper Tribunal in *Trinity Mirror*, discussed at [31] above, with which we respectfully agree. Accordingly, we hold that the default surcharge is not disproportionate.

DECISION

43. For the reasons given above, NPCL's appeal is allowed and the default surcharge penalty for period 12/17 is discharged.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

44. 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.

JUDGE GREG SINFIELD
CHAMBER PRESIDENT

RELEASE DATE: 01 MAY 2019