[2016] UKFTT 754 (TC)

TC05481

Appeal number: TC/2016/00599

VAT – default surcharge – payments failed to process as Faster Payment transactions – delay by one working day – whether there was effective service of the Surcharge Liability Notice – whether surcharge assessment for a default invalidated on revision – whether reasonable expectation of delivery of payment by the due date – whether reasonable excuse for mistake or mistaken belief – whether penalty disproportionate – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

M S RESOURCES LLP **Appellant**

- and -

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

TRIBUNAL: JUDGE HEIDI POON
EILEEN SUMPTER

Sitting in public at the Tribunal Centre, George House, 126 George Street, Edinburgh on 30 August 2016

Mr Colin Mitchell, Managing Partner for the Appellant

Ms Mary Donnelly, Presenting Officer of HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. The appellant, MS Resources LLP, appealed against two default surcharge notices, in the sum of £3,165.70 for VAT period 06/15, and in the sum of £4,942.80 for period 09/15.

2. Mr Mitchell, Managing Partner of the appellant, gave evidence and was cross-examined by Ms Donnelly. Ms Janie Barclay, an employee of the appellant with supervisory responsibilities of the accounts department, was present at the hearing but was not called as a witness. Nevertheless, Mr Mitchell looked to Ms Barclays to confirm certain facts to the Tribunal of which he was unsure. We accept Mr Mitchell's evidence without qualification.

The Law

3. The Tribunal is provided with the generic bundle of legislation and authorities in relation to the default surcharge regime. The legislation includes sections 59- 59A (on default surcharge), 70-71 (on mitigation of penalties), 83 (on appeal), of the VATA 1994 ('VATA'), and regulations 25, 25A and 40 of VAT Regulations 1995 on accounting, payment and records.

4. The provisions for the default surcharge regime are under s 59 of VATA. Of direct relevance to this appeal is sub-s 59(1)(b) VATA, which states that a taxable person shall be regarded as being in default in respect of a prescribed accounting period if, by the statutory due date, the Commissioners *have not received the amount of VAT shown on the return as payable by him in respect of that period*.

5. Similar wording to the same effect is found under sub-s 59A(1)(a) which provides for default surcharge in cases where payments on account are concerned, and the taxable person shall be regarded as in default if *a payment which he is so required to make in respect of that period has not been received in full by the Commissioners by the day on which it became due*.

6. By virtue of s 59(7), a taxable person is not liable to the surcharge if he '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, …'

7. The authorities referred to in this decision are: *Customs & Excise Comrs v Medway Draughting Technical Services Limited* [1989] STC 346 ('*Medway*'); Coales

v HMRC [2012] UKFTT 477 (TC) ('*Coales*'); *The Clean Car Company Ltd v C&E Comrs* [1991] VATTR 239 ('*Clean Car*'); *Garnmoss Ltd T/A Parham Builders v HMRC* [2012] UKFTT 315 (TC) ('*Garnmoss*'); *HMRC v Total Technology (Engineering) Ltd* [2012] UKUT 418 (TCC) ('*Total Technology*'); and *HMRC v Trinity Mirror Plc* [2015] UKUT 0421 (TCC) ('*Trinity Mirror'*).

The Facts

Background

8. The appellant is a limited liability partnership and registered for VAT in 2013. It submits VAT returns and makes VAT payments electronically in accordance with reg 25A of VAT Regulations 1995. The appellant has consistently made its VAT payments by Faster Payment Service (FPS).

9. The nature of the appellant's business is the supply of staff to Money Station Ltd. The appellant and Money Station Ltd are under common ownership, and the two entities have identical VAT quarter ends.

10. The business activity of Money Station Ltd is pawn-brooking; the company started trading in 2010, and now operates with ten shops in central Scotland. The appellant renders monthly invoices to Money Station Ltd for the supply of staff, and the output VAT payable by the appellant was in the range of £31,000 to £36,000 per quarter in the years of 2014 and 2015.

11. Money Station Ltd claims the VAT charged on the supply of staff as input VAT. With the two entities having identical quarter ends, the output VAT payable by the appellant is claimed as input VAT by Money Station Ltd in the same quarter, leaving Money Station Ltd with a net VAT liability of around £25,000 per quarter.

The history of defaults

12. The default history of the appellant is as follows:

(1) First default period 09/13, Surcharge Liability Notice (SLN) issued

(2) Second default period 06/14 at 2%

(3) Third default period 12/14 at 5%

(4) Fourth default period 03/15 at 10%

(5) Fifth default period 06/15 at 15%, surcharge of £4,748.55

(6) Sixth default period 09/15 at 15%, surcharge of £4,942.80

13. The surcharge notices under appeal relate to the fifth and sixth defaults. For period 06/15, the VAT payment due on 7 August was received on 10 August 2015; for period 09/15, the payment due on 7 November was received on 9 November 2015.

14. By letter dated 2 December 2015, Mr Mitchell requested a review of the two surcharge notices relating to the fifth and sixth defaults, stating that the payments

appeared to arrive a day or two late, and giving the possible explanation for the delay as: 'We can only assume this was an admin issue with our bank.'

HMRC's review decision

15. By letter dated 6 January 2016, HMRC's review decision upheld the surcharges. The review officer stated that HMRC will only cancel a default surcharge assessment if certain conditions apply, namely:

> '(1) we are satisfied that a business had a reasonable expectation that we would receive the payment and/or return by the due date;
>
> (2) there is a reasonable excuse for the payment and/or return being late;
>
> (3) a time to pay request had been agreed before the due date for payment.'

16. In response to the review decision, on 13 January 2016, Ms Barclay forwarded an email from the Bank of Scotland for HMRC to consider as 'additional information and reassess [their] decision'. The email from the Bank confirmed that the following payments were instructed to HMRC:

> '£31,657.04, debited your account on Mon 10 Aug 15 – instructed Friday 7th August 2015
>
> £32,952.05, debited your account on Mon 9 Nov 15 – instructed Friday 6th November 2015'

17. The email from the Bank continued to give what would appear to be the explanation as regards the timing difference between the date of instruction and the date of funds being cleared to HMRC:

> 'There were sufficient funds in the account to debit these payments however due to the maximum internet banking faster payment limit of £25k per transaction, the payments were debited 1 working day later as a Bill payment.'

18. On 15 January 2016, HMRC replied to the appellant. Referring to the transaction limit of £25,000 by faster payment, the review officer noted the following:

> 'I note from our records that you have previously made a Faster payment for the 09/14 return of £31,941.29 in two instalments of £6,941.29 and £25,000.00 so you should have been aware of the banks [sic] daily limit and we would have expected you to have submitted the payments for the 06/15 and 09/15 in two instalments.'

The Appellant's Grounds of Appeal

19. On 3 February 2016, Mr Mitchell lodged an appeal to the Tribunal. Notwithstanding the fact that HMRC did not receive the two payments on time, the appellant's main ground of the appeal is that it has met condition (1) in HMRC's decision letter of 6 January 2016, namely that the business had a *reasonable expectation* that HMRC would receive the payment by the due date.

20. Mr Mitchell emphasised that a management partner had ensured that the funds were in place before the instructions for payment; that the 'funds were attached to the instructions'; that although HMRC did not receive the payments until one working day later, the appellant had no access to the funds either; that 'a mistake was made by an employee who was unaware of the [transaction] limit'.

21. Mr Mitchell also raised doubt concerning HMRC's reply dated 15 January 2016 in the following terms:

> 'We are actually unsure whether the additional information was considered as the letter contradicts itself. It states they can only review it once and this was done on 06/01/16, but it also states they have considered the additional information.'

HMRC's Revision Letter

22. The lodging of the appeal to the Tribunal occasioned another review of the matter within HMRC in preparation for the hearing. By letter dated 8 March 2016, Officer Anderson, who was not formerly involved in the case, wrote to the appellant to cancel the default surcharge for the period 09/13 because a 'Time-to-Pay' arrangement had been agreed before the due date.

23. Period 09/13 was the first default in the appellant's history of defaults, and did not attract any surcharge at the time, but a Surcharge Liability Notice was issued. (The issue whether there had been effective service of an SLN was raised by the Tribunal at the hearing, and a short adjournment followed to enable HMRC to consider the matter and to obtain a copy of the SLN and Surcharge Notice that were in force at the time. This preliminary matter is addressed later in the decision.)

24. In consequence of the cancellation of period 09/13 as a default, the percentages of the subsequent defaults were adjusted as follows:

(1) First default period 09/13, Time-to-Pay agreement, default cancelled

(2) Second default period 06/14 at 2%, revised to 0%

(3) Third default period 12/14 at 5%, revised to 2%

(4) Fourth default period 03/15 at 10%, revised to 5%

(5) Fifth default period 06/15 at 15%, revised to 10%, surcharge reduced to £3,165.70

(6) Sixth default period 09/15 at 15% (no revision due), surcharge remains at £4,942.80

Appellant's Oral Evidence

25. In evidence, Mr Mitchell informed the Tribunal that a new assistant to Ms Barclay (by the name Laura) was appointed in March 2015. Laura was responsible for instructing the payments to HMRC; the instructions were done via internet banking as a 'Faster Payment', which means a same-day payment.

26. The internet banking instruction for a VAT payment is preceded by internal authorisation, whereby a managing partner would authorise an 'inter-company' transfer to move the requisite funds into the business account to make the VAT payment. Mr Mitchell emphasised that the funds were lodged into the paying account before the VAT payments were due on both occasions.

27. As indicated on the bank statements, the brought-forward balance on 7 August 2015 was £31,718.91 to fund the VAT payment of £31,657.04 for period 06/15, and the brought-forward balance on 6 November 2015 of £34,181.36 was for the VAT payment of £32,952.05 for period 09/15.

28. The Tribunal noted the VAT payment for 06/15 appears on the bank statement as a 'Bill Payment' and asked whether the internet banking instruction on 7 August 2015 would have indicated at the time that the payment would not be transacted as a 'Faster Payment' on the same day. Mr Mitchell informed the Tribunal that 'nothing even flagged up that the payment was late'; that different colleagues regularly go on to the website to check account transactions and there was no indication that the payment did not go through.

29. The Tribunal then asked why the 'Bill Payment' for period 06/15 did not alert the management to the fact that the 'Faster Payment' instruction did not go through as a faster payment on the same day, and that the mistake was allowed to repeat for the subsequent period 09/15. Mr Mitchell was unable to answer the question and looked to Ms Barclay for a response.

30. Ms Barclay said something about mistaking the transaction date for the 06/15 payment being 10 August as a result of a Direct Debit arrangement, that the due date for payment by Direct Debit method is the tenth and not the seventh; that she had not thought the payment for 06/15 was late; that it was a genuine mistake. (A Direct Debit arrangement means a VAT payment is applied for by HMRC on the due date, and extra three working days are allowed for the payment to reach HMRC's account.)

31. The Tribunal then asked whether the surcharge notice for 06/15 would have alerted the management that the VAT payment for 06/15 was late from HMRC's perspective. The surcharge notice was dated 14 August 2015 and could be expected to reach the appellant within two weeks after the default had occurred.

32. In relation to the surcharge notice for 06/15 default, Mr Mitchell's reply was rather vague: 'can't say if open or un-open; probably should end up on my desk; can't say hand on heart.'

33. In cross-examination, Ms Donnelly asked if it might have been the case that there was a daily cut-off time for making a faster payment, in that the instruction for the transaction must be given by a certain time of the day for it to be processed on the same day; and that cut-off time was missed on those occasions. Mr Mitchell confirmed that there was no daily cut-off time for making a faster payment via internet banking, other than by reference to the 24-hour time frame of a day.

The Parties' Submissions

34. HMRC submitted that the onus is on the appellant to establish it had a reasonable excuse to expect the payments would reach HMRC by their due dates; that the appellant has not discharged the onus.

35. HMRC further submitted that the appellant's preferred method of payment has consistently been by Faster Payment Service and should have known of the transaction limit of £25,000 on each transaction. Whether a payment is on time is referential to the time HMRC receive the payment; that the delay of one or two days does not render the surcharge disproportionate as established by *Total Technology* and *Trinity Mirror*.

36. In submission, Mr Mitchell argued that the surcharge liability assessment for 06/15 should be set aside as invalid because the original amount was wrongly calculated to be £4,748.55; that it was wrong in the first place should render it invalid therefore. He emphasised the long delay in the discovery of the 'error' by HMRC that the default for 09/13 had been wrongly imposed; that it had taken over a year for the default for 06/15 to be revised.

37. In respect of the payments arriving late, Mr Mitchell's main ground for reasonable excuse was that there was nothing on the internet page when the payments to HMRC were instructed on the respective due dates to indicate that the payments would not be processed as a faster payment to arrive at HMRC's on the same day.

Discussion

Whether there was effective service of a Surcharge Liability Notice

38. The preliminary issue for the Tribunal to address is whether there had been effective service of a Surcharge Liability Notice (SLN). HMRC's revision letter of 8 March 2016 cancelled the default for the period 09/13. The SLN issued for that default was the statutory notice that brought the appellant into the surcharge regime by triggering the surcharge liability period for the purpose of reckoning VAT defaults.

39. On the cancellation of the default related to period 09/13 due to a Time-to-Pay agreement being in place, the SLN that was 'attached' to the period no longer had its legal effect. The original 'second' default related to period 06/14 became the first default on the cancellation of the default for 09/13. The 06/14 default would have occasioned a 'VAT Notice of assessment of surcharge', and not a 'VAT Surcharge liability notice' (SLN).

40. The Tribunal has regard to the High Court judgment[1] on *C&E Comrs v Medway* ('*Medway*'), in which the receipt of the SLN is held to be crucial for the purpose of enabling the person to whom it was addressed to take requisite action, and the rolling

[1] The judgement covers the two appeals *Customs & Excise Comrs v Medway Draughting Technical Services Limited; Customs & Excise Comrs v Adplates Offset Limited* [1989] STC 346.

12-month surcharge liability period could not be triggered unless there had been effective service of the SLN.

41. The statutory notice served on the appellant occasioned by the default for 06/14 is headed 'VAT Notice of assessment of surcharge and surcharge liability notice extension'. During the short adjournment, Ms Donnelly was able to obtain a copy of the notice in force for period 06/14, which contains the following paragraph:

> 'If no surcharge period has been notified to you previously, the period beginning on the date of this notice and ending on DD Month xx YYYY is hereby specified as the surcharge period for the purposes of Section 59 and 59A of the VAT Act 1994.'

42. The Tribunal is satisfied that the paragraph contained in the notice of assessment for period 06/14 effectively stands in for the purpose and function of the SLN that has been vacated in consequence of the default for 09/13 being cancelled. In other words, there has been effective notice served on the appellant to trigger the surcharge period by the default in relation to 06/14.

Whether the surcharge for period 06/15 is invalid

43. In relation to period 06/15 under appeal, Mr Mitchell argued that since the original surcharge had been 'wrongly' calculated at 15%, the subsequent, revised assessment in relation to that default was rendered invalid.

44. Such an argument has no basis in law. A surcharge assessment is valid when there is a default. Mr Mitchell did not dispute that the VAT payment for period 06/15 did arrive late, and triggered a default, and where there is a default, a surcharge liability arises.

45. The reduction of the surcharge percentage from 15% to 10% for period 06/15 was a direct consequence in cancelling the default relating to 09/13. A revision of the surcharge percentage for subsequent defaults does not remove the surcharge liabilities that have been occasioned by each of these defaults.

46. It is worth noting that a 'Time-to-Pay' agreement is a concession given by HMRC at their discretion. HMRC's 'Action History' details numerous instances of the appellant requesting a Time-to-Pay arrangement, and apart from the period 09/13, there were other Time-to-Pay agreements granted. For example, the entry for 6 August 2014 records: 'Ms Barclay … rang for TTP for 06/14 to cover 2 business's [sic] with a combined VAT liability of approx. £45,619.91, TTP … refused becos the biz has had 2 TTP in consecutive quarters'.

47. The grant of the Time-to-Pay concession has enabled the appellant to avoid a default on more than one occasion. To turn such a concession into a ground of challenge, directly or indirectly, of the validity of the surcharge assessment of a subsequent default that has the surcharge percentage reduced would seem to be an example of biting the hand that feeds you; there can be no equitable foundation to such an argument.

Whether reasonable expectation that the payments would arrive by the due date

48. The main ground of appeal stated in the Notice of Appeal is that the VAT payments were despatched at such a time and in such a manner that it was reasonable to expect that they would be received by HMRC by their due dates.

49. There is no doubt that Mr Mitchell had such an expectation, but we do not consider that Mr Mitchell's expectation was *reasonable*.

50. The Tribunal finds Mr Mitchell a credible witness; nevertheless we find his evidence on the whole tending towards vagueness. Mr Mitchell clearly did not know of the transaction limit of £25,000 being imposed by the bank for Faster Payment transactions; he could not be sure how the surcharge assessments would have been dealt with in the office; he said the bank accounts of the business are constantly monitored by his colleagues (but not by him) and they were not alerted to the delay in the transactions; he had to look to Ms Barclay for answers on more than one occasion; he was not sure whether Direct Debit arrangements were in place to make VAT payments. Mr Mitchell clearly was not the person with the level of control and knowledge of the accounts operation in his business; and this fact was reflected in the vagueness of his evidence.

51. The appellant produced two pages of the bank account statements showing the VAT payments. Though the VAT payments were for MS Resources, the payments were made from the business account of Money Station Ltd. Very few third-party transactions pass through this account at the relevant times; most of the transactions would appear to be inter-company transfers. The bank statements show a column indicating 'Payment type' for each transaction, which includes: Transfer, Faster Payment, Bill Payment, Direct Debit.

52. The only two Bill Payment transactions on the bank statements are the VAT payments to HMRC. We do not doubt that the two VAT payments were instructed on Friday 7 August 2015 and Friday 6 November 2015 as a Faster Payment. There are other payments made successfully as a Faster Payment and these are clearly indicated on the day it was made, with the exact time; e.g. '11Aug15 14:49' to 'Moneystation RBS' are details shown for a Faster Payment on 11 August 2015 on the bank statement. If the account transactions were closely monitored through internet banking as Mr Mitchell suggested, it would seem that these two payments would have failed to show up as a Faster Payment on the day of instruction, and could have alerted someone to take requisite action on the day.

53. We also note that someone within the accounts department did know of the transaction limit and had split the VAT payment into £25,000 and the balance on 25 August 2014. That someone might have left, and his knowledge of the transaction limit might not have been passed on. The delegation of the task to effect the VAT payments on time to the new assistant does not exonerate the management from its overall responsibility of ensuring the payments were indeed made on time, nor could her ignorance of the transaction limit convert the mere expectation of the management into reasonable expectation that the payments would be made on time.

Whether reasonable excuse in mistaken belief

54. In evidence, Mr Mitchell referred to not knowing about the transaction limit for a Faster Payment as a mistake. As to the failure of management to notice that the August 2015 VAT payment was not processed as a Faster Payment, Ms Barclay's supplemental explanation referred to the mistaken belief that there had been a Direct Debit arrangement to pay the VAT; that the payment was made on 10 August which dovetailed with the due date for a Direct Debit payment. The Tribunal concludes that neither the mistake described by Mr Mitchell, nor the mistaken belief referred to by Ms Barclay, can amount to a reasonable excuse.

55. In *Garnmoss*, where there was a *bona fide* mistake made, Judge Hellier states at [12] that while the mistake 'was not a blameworthy one, the Act does not provide shelter for mistakes, only for reasonable excuse.'

56. In *Coales*, Judge Brannan states at [32]: 'The test contained in the statute is not whether the taxpayer has an honest and genuine belief but whether there is a reasonable excuse.' He rejects the notion that an honest and genuine belief, even if unreasonable, can amount to a reasonable excuse, and that the reasonableness of a belief has to be subject to the same *objective* test for reasonable excuse as set out by Judge Medd in *Clean Car*:

> '… can the fact that the taxpayer honestly and genuinely believed that what he did was in accordance with his duty in relation to claiming input tax, by itself provide him with a reasonable excuse. In my view, it cannot. … In my judgment it is an objective test in this sense. One must ask oneself: was what the taxpayer did a reasonable thing for a responsible trader conscious of and intending to comply with his obligations regarding tax, but having the experience and other relevant attributes of the taxpayer and placed in the situation that the taxpayer found himself at the relevant time, a reasonable thing to do?'

57. Mr Mitchell is a man of business who has successfully helped grow the business within a short time since 2010 to its current scale of operating ten shops in central Scotland. The business seems to operate within a group structure with a number of associated companies, and inter-company bank transfers appear to occur daily as a way the management governs the finances of the group. It is reasonable to expect the managing partner of a business of this scale to have a good understanding of the terms and conditions of the banking facilities under which the various bank accounts operate. Even if Mr Mitchell himself does not have the detailed knowledge of the limits and restrictions on the banking facilities, he as the managing partner has the overall responsibility to ensure that someone knows within the business so that these terms and conditions can be adhered to. His so-called mistake in not registering the transaction limit on this particular account from which the VAT payments were made cannot amount to a reasonable excuse.

58. As to Ms Barclay's explanation that there was a mistaken belief that a Direct Debit arrangement to pay the VAT liability was in place, we have difficulty giving credence to her explanation. It was not clear how this belief originated; the appellant has consistently paid VAT by Faster Payment Service, and no VAT payments seem to

have ever been made by Direct Debit. Ms Barclay herself had attempted to request a Time-to-Pay arrangement for the appellant on numerous occasions, which suggests that Direct Debit payment method would not have been suitable since the appellant did not have the funds in place every quarter end for HMRC to apply for the full payment.

59. The mistaken belief that a Direct Debit arrangement was involved, even if it had any basis, cannot amount to a reasonable excuse as it is only right and proper that whoever was responsible for discharging the appellant's VAT liability for the disputed periods should have full knowledge of the chosen method of payment.

The delay was by one working day

60. Mr Mitchell has emphasised that the delay was only by one working day. First, the reckoning of due date for s 59 VATA purposes does not distinguish between working or non-working days. Secondly, applying the principles from *Total Technology*, the surcharge regime is 'for failure to file and pay by the due date, not for delay after the due date' (at [89]). The scaling in the surcharge regime is not by reference to the number of days a payment is made late, but by the number of defaults in a surcharge rolling period, which gives rise to an escalating percentage of surcharge rate, at 2%, 5%, 10% and 15%, in proportion to the number of defaults in a rolling period. The Upper Tribunal decision in *Trinity Mirror* supports the conclusions reached in *Total Technology*, and states that the surcharge regime, viewed as whole, is a rational scheme that does not infringe Convention rights or the principle of proportionality under EU law.

Decision

61. The appeal is accordingly dismissed. The surcharge assessments of £3,165.70 for period 06/15 and of £4,942.80 for period 09/15 are confirmed.

62. 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.

DR HEIDI POON
TRIBUNAL JUDGE

RELEASE DATE: 10 NOVEMBER 2016