



Neutral Citation: [2024] UKFTT 00746 (TC)

Case Number: TC09264

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

By remote video hearing

Appeal reference: TC/2023/01039

VAT DEFAULT SURCHARGE – Section 59 Value Added Tax Act 1994 - Were the default surcharges correctly issued – Yes – Does the Appellant have a Reasonable Excuse for the defaults under Appeal – Yes - Appeal Allowed and default surcharges in the sum of £247,151.18 dismissed

Heard on: 15 March 2024

Judgment date: 15 August 2024

Before

**TRIBUNAL PRESIDING MEMBER: G. NOEL BARRETT
MEMBER: SONIA GABLE**

Between

MPMH CONSTRUCTION LIMITED

Appellant

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Mrs Eilidh MacEwan

For the Respondents: Mr Colin Williams, Presenting Officer HM Revenue and Customs

DECISION

INTRODUCTION

1. With the consent of the parties, the form of the hearing was V (video) and the remote platform used was the Tribunal video hearing system. A face to face hearing was not held, because neither party objected to the same and the Tribunal decided a remote hearing was appropriate. The documents to which we were referred were the hearing bundle extending to 279 electronic pages and a joint legislation and authorities bundle extending to 197 electronic pages. We had also received before the hearing an application for an extension of time, HMRC's skeleton argument extending to eight pages and the appellant's skeleton argument extending to three pages

2. Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.

PRELIMINARY MATTERS

3. As HMRC had no objection to the appellant's application, to extend the time limit within which to lodge their skeleton argument, from 19 October 2023 to 5pm on 12 March 2024 and the appellant had no objection to extending the time limit within which HMRC had to file the joint authorities bundle, to 5pm on 13 March, we allowed both applications.

4. It was noted by both parties, that the hearing bundle had not been compiled strictly in accordance with the FTT's General Guidance on PDF Bundles. Nevertheless, as the parties and the Tribunal all had satisfactory electronic access to the same, we ordered that it should be properly admitted and used in the Hearing.

5. There was a suggestion that the appellant's appeal was made late, as HMRC's decision letter was dated 23 December 2022 and the appellant did not appeal until 8 March 2023. However the appellant had provided further evidence to HMRC in January 2023, upon receipt of which HMRC issued a further decision letter dated 9 February 2023. As the appellant's appeal was made within 30 days of this further decision letter and on the basis that HMRC did not object, then in so far as the appellant's appeal was in fact late, we formally admit the same.

APPEAL SUMMARY AND THE LAW

6. This is an appeal against default surcharges for the VAT periods 02/21, 05/21, 08/21, 11/21 and 02/22 totalling £247,151.18 calculated at 15%, for late payment of VAT, the due dates being 07/04/21, 07/07/21, 07/10/21, 07/01/22 and 07/04/22 respectively.

7. *Regulation 25(1) of the Value Added Tax Regulations 1995 provides:*

That a return must be submitted to HMRC by all VAT registered persons not later than the last day of the month following the end of the period to which it relates.

8. *Regulation 40 of the Value Added Tax Regulations 1995 provides:*

Any person required to make a return shall pay 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

9. The provisions of *Section 59(1) (a) and (b) of the Value Added Tax Act 1994 (VATA)* operate such that a person shall be regarded as being in default for that period if by the last day on which a taxable person is required ... to furnish a return ... HMRC either have not received the return or have received the return but have not received the amount of VAT shown on the return.
10. Where a default occurs and HMRC serves a surcharge liability notice (SLNE), then if the taxable person is again in default before the expiry of the first anniversary of the last day of the period referred to in the surcharge notice, then the taxable person becomes liable to a surcharge being the greater of the specified percentage or £30.
11. The specified percentages are set out in *Section 59 (5) VATA*:
 - (a) in relation to the first such prescribed period the specified percentage is 2%
 - (b) in relation to the second such period the specified percentage is 5%
 - (c) in relation to the third such period the specified percentage is 10%
 - (d) in relation to such period after the third the specified percentage is 15%
12. The specified percentage for all the defaults that are the subject of this appeal is 15%.
13. *Section 59(7) (b) VATA* provides that the taxable person shall not be liable to the surcharge and shall not be treated as having been in default if there is a reasonable excuse for the return or the VAT not having been despatched within the appropriate time limit.
14. *Section 59(7) VATA* allows a trader to appeal to the tribunal, the onus being placed on the trader to satisfy the tribunal that either the payment 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 there is a reasonable excuse for the return or VAT not having been despatched on time.
15. If the trader satisfies the tribunal on either of these grounds then the trader will be treated as not being in default in respect of the accounting period in question.
16. *Section 71(1) VATA* provides that:
 - (a) an insufficiency of funds to pay any VAT due is not a reasonable excuse: and
 - (b) where reliance is placed on any 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.
17. HMRC do not however issue a surcharge at the rate of 2% or 5% if it is less than £400.
18. For returns submitted electronically, the due date is extended by seven days, under directions made under the VAT Regulations 1995.
19. HMRC send each SLNE to the taxable person with notes advising what a default is and the consequences which will flow from further defaults. Those notes also advise the taxable person to contact HMRC's Debt Management Unit if they expect to have difficulty paying VAT on time.
20. Copies of the first and subsequent default surcharge notices, are exhibited at electronic page numbers 14 to 18 of the Hearing Bundle.
21. A Schedule of the appellant's defaults is exhibited at electronic pages numbers 52 to 56 of the Hearing Bundle
22. The appellants grounds of appeal are:-
 - (1) The appellant company has never tried to avoid its VAT obligations nor unreasonably withhold payment.

- (2) During the COVID pandemic, weekly changes in government guidance, disruption to staffing and scheduling, due to the immediate halting of work through isolation and limitations to imports or availability of goods, caused significant operational challenges
- (3) The appellant company was at the relevant time engaged principally on NHS Hospital contracts, where PPE and social distancing was essential. This severely impacted productivity.
- (4) The appellant's staff were exposed to COVID and sites were forced to close during outbreaks of COVID.
- (5) Projects suffered delays and the appellant had to wait for revenue (payments) for far longer periods of time than normal, as a result of NHS financial staff either shielding and/or working from home and/or simply not being contactable.
- (6) The agreed formulas and time scales for valuations of work being approved and/or certified by the NHS, so that invoices could be raised and paid, simply did not happen.
- (7) The cumulative impact on the cash position of the appellant was substantial, as a result of the COVID 19 related business interruption and additional costs
- (8) Specifically £500,000 due in respect of NHS contracts was outstanding between December 2021 and October 2022.
- (9) This caused severe cash flow problems and created VAT liabilities for invoices which had not been paid.
- (10) Accordingly, VAT was not despatched in full on the due dates in consequence of a string of factors all linked to COVID 19.
- (11) Payment of the full liabilities would have left the appellant company in a position where it could not meet its other liabilities.
- (12) For the period ending 2/21, the VAT was paid in full on 9 April 2021.
- (13) The 5/21 return was submitted timeously and payments totalling £231,867.86 were rendered on dates between 23 July and 17 September 2021.
- (14) The 8/21 return was submitted timeously and VAT of £254,288.28 was paid on dates between 8 October 2021 and 13 January 2022.
- (15) The 11/21 return was submitted timeously and payment in full was rendered on 11 and 12 January 2022.
- (16) The 2/22 return was submitted timeously and the VAT was paid in full on 8 and 11 April 2022.
- (17) The appellant's VAT advisers wrote to HMRC on 31 October 2022 offering to enter into a time to pay arrangement. No response was received. The Appellant has nevertheless continued to make payments towards the outstanding balance.

THE EVIDENCE AND OUR FINDINGS OF FACT

23. The appellant company first entered the default surcharge regime when it paid its VAT late for the quarter ending 30 November 2017.

24. It defaulted a second time by making its return late and paying VAT late for the quarter ending 31 August 2018 on which a 2% surcharge was payable.
25. The appellant defaulted a third time when it again submitted its return and paid its VAT late for the quarter ending 30 November 2018 on which a 5% surcharge was payable.
26. The appellant defaulted a fourth time when it again submitted its return and paid its VAT late for the quarter ending 31 May 2019 on which a 10% surcharge was payable.
27. The appellant defaulted a fifth time when it paid its VAT late for the quarter ending 30 May 2020 on which a 15% surcharge was payable.
28. The appellant defaulted again in the VAT quarters ending 31 August 2020 and 30 November 2020 and so remained in the VAT default surcharge regime at the rate of 15% at the time the penalties under this appeal were incurred.
29. The appellant paid the above surcharges, all of which predated the COVID 19 pandemic, and moreover, none of these penalties were appealed nor challenged by the appellant.
30. We are satisfied, on the evidence provided by HMRC, that the default surcharges, both prior to those now being appealed ie those detailed in paragraphs 23 to 28 above and those under appeal as detailed in paragraph 6 above, have been correctly calculated and that the required notices of default have been properly served on the appellant company.
31. Further the company's Managing Director, Mr Snodgrass, accepts the calculation and notification of all the penalties, in his evidence.
32. Having found that HMRC have proved that the calculation of the surcharges has been correctly made and that the notices have been correctly served, the burden of proving, to the required civil standard (on the balance of probabilities) that a reasonable excuse exists for the late payment, rests with the appellant company.
33. Mr Snodgrass gave oral evidence.
34. He confirmed and we accepted that the appellant company carried out highly specialised construction work for the NHS and other government or quasi government bodies under framework agreements and had delivered more healthcare construction projects than any other contractor in Scotland over the last few years.
35. He confirmed and we also accepted that either side of the COVID 19 pandemic around 75% of the company's work was for the NHS under the framework agreements which he had described and that during the COVID 19 pandemic 100% of the company's work was for the NHS.
36. Mr Snodgrass explained and we accepted that there was a very strict and prescriptive contractual process (to which both parties to the contract had to adhere) for valuing work done under the framework agreements and then rendering accounts therefore. Generally, monthly valuations of work-in-progress, would be submitted to the contract administrator for the particular NHS Health Board and once the valuations had been approved the work, as valued and approved, was VAT invoiced. Thereafter, the relevant NHS Health Board finance department would make payment to the appellant company, usually within 14 days and at the outside, 21 days.
37. He explained that as a result of the COVID 19 pandemic, work reduced and those NHS Boards for whom the appellant company was still working ceased to comply with the framework agreements regarding payment terms. Indeed it became almost impossible to contact their finance departments, as their staff left to shield and/or work from home.

38. Despite this, the NHS Health Boards, for whom the appellant company was still working, carrying out often essential and highly specialised works for the benefit of the public, still expected the appellant company to fulfil its part of the framework agreements, not least in delivering its VAT invoices timeously.

39. Mr Snodgrass explained that these delays caused huge cash-flow difficulties for the company, which were exacerbated as staff output fell considerably, as a result of staff having to travel in separate vehicles, having to socially distance (2 metres) in the workplace and having to wear both masks and PPE, which were cumbersome. In general staff productivity fell from around 8 hours per day, to closer to 5 hours a day. This resulted in work which had been priced pre-pandemic costing the appellant company a lot more to actually undertake.

40. One particular contract undertaken by the company during the pandemic, at the Queen Elizabeth University Hospital in Glasgow had originally been estimated and priced to take 32 weeks, but actually took 110 weeks to complete.

41. Mr Snodgrass provided examples of several other major contracts, all of which had been plagued by the same problems.

42. Finally Mr Snodgrass explained, in addition to the enormous problem of actually obtaining payment timeously from the NHS and in addition to the large percentage reduction in staff productivity, that there were also large increases in material costs and material shortages during the pandemic, both of which the company had to “swallow” in financial terms.

43. Regardless of these enormous financial burdens and constraints the company had to pay its staff and suppliers through the pandemic, otherwise it could not have continued trading.

44. Overall, we accepted the picture Mr Snodgrass painted of the company being let down seriously by the NHS Health Boards for which it was contracting and carrying out both essential and highly specialised public work, under circumstances that were completely unforeseeable.

45. Mr Snodgrass suggested, and we accepted, that it was unreasonable and entirely unforeseeable that one government organisation (the NHS) would fail to honour its contractual obligations, for 100% of the value due to the appellant company, whilst another government department (HMRC) levied 15% surcharges on the late payment to it of the 20% VAT element, on those same unpaid contractual obligations.

46. Mr Snodgrass confirmed and we had no reason to doubt him that the continuing delays in payment by the NHS, the reduced labour efficiencies/increased labour costs, and increased materials costs had a cumulative effect on the appellant company’s cash flow, which increased through 2020 into and through 2021, hitting a peak, of around £500,000 owed, on top of increased labour and material costs.

47. Finally Mr Snodgrass gave evidence about the contact he and his office manager had had with HMRC throughout 2021, as the appellant company’s VAT defaults were accruing, trying to explain to them that his company’s cash flow difficulties were being caused entirely as a result of the NHS, itself a government body, not making timely payments, as it was contracted to do.

48. This contact and explanation we accept seemed to “fall on deaf ears”.

49. It was, in our view, entirely appropriate for Mr Snodgrass to assume (given the extenuating circumstances, which he could not have predicted) that his company had a

reasonable excuse for late payment during and in the months after the COVID 19 pandemic for those periods itemised in paragraph 6 above and that his company would not therefore be penalised for late payment.

50. We found Mr Snodgrass to be an honest and truthful witness, we accepted his evidence and had great sympathy for the way in which described his company, as apparently having been treated, by several NHS Health Boards.

THE LAW ON REASONABLE EXCUSE AND ITS APPLICATION TO THE FACTS

51. There is no statutory definition of what constitutes a reasonable excuse.

52. 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” Rowland v HMRC [2006] SPC548/06 (at paragraph 19).

53. The test as to whether the Appellant has a reasonable excuse is as set out by Judge Medd QC, in *The Clean Car Company v C&E Commissioners* [1991] VATTR 234:

“The test of whether or not there is a reasonable excuse is objective one. In my judgement it is an objective test in this sense. One must ask oneself: was what the taxpayer did a reasonable thing for a responsible taxpayer 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?”

54. We accept, following Judge Medd’s reasoning in *The Clean Car Co Ltd v C&E Commissioners* [1991] VATTR 234, that the appellant company, having the experience and other relevant attributes it clearly had, when placed in this situation at this time acted reasonably as any responsible trader, conscious of and intending to comply with its tax obligations, would or indeed, should have done.

55. 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.

56. We find it difficult to imagine how any responsible trader (as described in paragraph ?? above, faced with the particular circumstances with which the appellant company was faced, would have behaved any differently. The company worked exclusively for the NHS during a national health emergency, COVID 19 and even before the pandemic, around 75% of its work was for the NHS. The company considered it had a duty to the public to continue supplying its services to the NHS. However because the NHS contracts formed up to 100% of the company’s business, it was not able to overcome the cash flow difficulties it was faced with as a result of the increasing delays in receiving payment from the NHS.

57. For the reasons provided, we accept, given that the underlying circumstances, that neither the appellant company, nor objectively any other reasonable taxpayer imbued with the appellant company’s attributes, could have predicted, foreseen, or for that matter avoided the factors which resulted in it ultimately defaulting on paying its VAT on time for the periods set out in paragraph 6 above.

58. The respondents submit, that section 71(1)(a) of the VAT Act 1994 specifically excludes insufficiency of funds from being a reasonable excuse for the late payment of VAT.

59. That submission, in our opinion, fails to acknowledge that the underlying reasons causing the appellant to have a shortage of funds, which in turn result in the late payment, may in some circumstances amount to the appellant having a reasonable excuse.

60. This Tribunal is required to approach the question of a reasonable excuse in line with the Upper Tribunal decision in *Perrin v HMRC* [2018] UKUT 156 TCC at paragraph 81:

“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?”

(NB The fourth step in *Perrin* contains an extra requirement that does not apply to the default surcharge).

61. Thus, in regard to steps 1 and 2 above, we accept the detailed explanation which Mr Snodgrass has provided in his evidence as to the several unplanned, unexpected and unpredictable factors (as set out in paragraphs 36 to 45 above) which together contributed to the unavoidable shortage of funds.

62. We also accept, when viewed objectively, that what Mr Snodgrass has said does indeed amount to an objectively reasonable excuse for the default and the time when that objectively reasonable excuse ceased.

63. The appellant company was, as Mr Snodgrass confirmed in his evidence, a business which during the COVID 19 pandemic, traded exclusively with the NHS and derived 100% of its income therefrom and for whom, seemingly, regardless of timely payment it was expected to continue to perform what were vital and essential works for the public good.

64. Payments to the company from the NHS were unexpectedly and unreasonably substantially delayed and its labour and materials costs increased substantially, again unexpectedly. In our view, not even the most diligent and responsible taxpayer, intending to comply with its tax obligations could have predicted or planned for these issues.

65. Short of ceasing to trade, there was little else the appellant company could do, other than pay its VAT late.

66. The appellant company was not, in our view, a company which suffered only general unspecified cash flow problems as a result of the COVID 19 pandemic. It was affected exceptionally and specifically because of its 100% reliance on NHS contracts.

67. The respondents submit that whether a taxpayer has a reasonable excuse will depend on the particular circumstances in which the failure occurred and the abilities of the taxpayer who has failed. What is a reasonable excuse for one person may not be a reasonable excuse for another.

68. We find, on the evidence as provided by Mr Snodgrass, that that the appellant company's unique and particular circumstances pass this test.
69. The respondents contend that even if the facts asserted by the appellant are true, they do not objectively constitute a reasonable excuse.
70. We find however that the facts, as stated by Mr Snodgrass, are true and that they collectively do amount (as above) objectively to a reasonable excuse.
71. HMRC further assert that COVID 19-related business disruption has affected many businesses in the United Kingdom in different ways and that whilst they sympathise with this business, they do not accept that the circumstances attributable to this business do amount to a reasonable excuse, such that the VAT default surcharges under appeal should be remitted.
72. We disagree. The appellant company was not in our view, a general "run of the mill" business which was affected, to the same degree as many other businesses, by general problems associated with trading through the COVID 19 pandemic.
73. On the contrary, we find, on the evidence provided by Mr Snodgrass, that the company was largely unique in the way in which it relied entirely on NHS contracts and payments throughout the relevant period.
74. The Respondents contend that as the first UK COVID-related lockdown was entered in March 2020, and that the default surcharges under appeal arose from February 2021 to February 2022 then it would be reasonable to expect that the appellant company would have had contingency plans in place to deal with these measures by then, whilst still being able to meet their VAT obligations under the law.
75. Mr Snodgrass however explained the cumulative effect through the period of the delayed payments and increased costs and we accept why it was that to some extent there was a "delayed reaction".
76. It is correct for HMRC to point out that the appellant had a poor VAT compliance record (beginning at the end of the VAT period 11/17) long before the COVID 19 pandemic and indeed failed to comply with its VAT obligations on time, for three months during 2020.
77. However, to their credit, the company has not tried to appeal those surcharges but only those surcharges itemised in paragraph 6 above.
78. In our view this lends support and gravitas to the appellant Company only appealing those surcharges against which it believes it has a reasonable excuse.
79. We do not accept, that because the appellant company had an historically poor compliance record (for whatever reason(s)) that the evidence put forward by Mr Snodgrass, as to why there is a reasonable excuse for the periods under appeal, should be given any less weight.
80. Indeed, to some extent, the fact that the previous defaults have not been appealed adds greater weight to the validity of the reasons which support those defaults that are being appealed.
81. For all the above reasons we find that the appellant has established, on the balance of probabilities, an objectively reasonable excuse for late payment of its VAT for the periods under appeal and which are set out in paragraph 6 above.

DECISION

82. In the circumstances we allow the appeal on the grounds of the appellant company's objectively reasonable excuse and dismiss the default surcharges, in the sum of £247,151.18.

83. 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.

**G. NOEL BARRETT
TRIBUNAL PRESIDING MEMBER**

RELEASE DATE:

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