

Disproportionate penalty – Default surcharge

[Trinity Mirror Ltd](#)

The taxpayer is on calendar VAT quarters and in the payments on account scheme. Trinity Mirror Ltd (Trinity) was initially late in paying the balancing VAT payment for the quarter ending 06/07. The amount was paid in full one day late. HMRC issued a surcharge liability notice and specified a surcharge period from 31 August 2007 to 1 July 2008. This expressly notified Trinity that that it may be liable to a surcharge if it defaulted in respect of a VAT period ending within that time. Two returns later, the taxpayer was again 1 day late in making its balancing VAT payment. HMRC issued a default surcharge at 2%. This was originally based on an underpayment of £3,545,324, producing a surcharge amount of £95,500. Following a voluntary disclosure, this was reduced to £70,906.44. The taxpayer appealed to the FTT which found that the surcharge was disproportionate. HMRC then appealed to the UT.

Held

The UT Tribunal began by considering whether the FTT applied the correct legal tests. In supporting the view that the surcharge was disproportionate the FTT used two comparisons. First, it compared the current case to the Enersys FTT, which involved a 5% default surcharge of £131,881 on a fifth default. The UT concluded the FTT's reliance on Enersys was misguided, that it was wrong to extrapolate from a different case and started from the incorrect basis that the gravity of the offence is exclusively dictated by the number of defaults and not the amount of unpaid VAT. Secondly, the FTT used the UT decision in Total Technology to support the benchmark figure of £50,000 for a third default (second within the surcharge period). The current UT considered the FTT had misunderstood Total Technology. Its £50,000 example was an illustrative example to show how a fixed flat rate penalty, could be disproportionate based on the size of the taxpayer. This was enough for the UT to conclude the FTT had erred in law and it was appropriate to remake the decision.

Turning to its own decision on proportionality. The UT noted Total Technology rightly focused on the aim of the default surcharge regime. However, the UT considered it did not examine in detail the more fundamental objective of the underlying aim of the Directive. Under this, it is necessary for Member States to provide a system of deduction and collection of tax at each stage in the process, that tax should be accounted for, and paid, on a timely basis. The correct approach is to determine whether a penalty goes beyond this and whether the penalty is so is so disproportionate to the gravity of the infringement that it becomes an obstacle to fiscal

WE HOPE YOU FIND THIS NEWS ARTICLE HELPFUL. IF YOU WOULD LIKE TO REGISTER TO RECEIVE FUTURE UPDATES BY EMAIL THEN PLEASE SEND A REQUEST TO

info@4eyesltd.co.uk

This VAT update is published for the general information of 4 Eyes Ltd personnel, clients and contacts. It provides only an overview of the rules and regulations in force at the date of publication, and no action should be taken without consulting the detailed legislation or seeking professional advice. Therefore no responsibility for loss occasioned by any person acting or refraining from action as a result of the material contained in this e-mail will be accepted by the authors or the firm.

neutrality. Applying this to the default surcharge in the current case, the UT concluded that a penalty of 2% cannot be regarded as so disproportionate to the seriousness of the infringement as to constitute an obstacle to the underlying aim of the directive. The UT adds that the surcharge cannot also be regarded as disproportionate by reference to the Convention on the basis that it has been arrived at by the application of a rational scheme that cannot be characterised as devoid of all reasonable foundation. Whilst admitting the penalty may be considered harsh, it cannot be regarded as plainly unfair.

Comment

Following Total Technology, this is now the second higher court decision which has found against the taxpayer on proportionality. These cases provide a high bar to a penalty being considered disproportionate and are clearly of the view that the default surcharge regime is not disproportionate per se. The only concern raised in these cases is the absence of a maximum penalty, but for a penalty to be considered disproportionate this is considered only likely to occur in 'a wholly exceptional case'.

When this article appears in the latest news section on our website then the [website disclaimer](#) applies. See also full disclaimer on PDF in document archive which also applies

WE HOPE YOU FIND THIS NEWS ARTICLE HELPFUL. IF YOU WOULD LIKE TO REGISTER TO RECEIVE FUTURE UPDATES BY EMAIL THEN PLEASE SEND A REQUEST TO

info@4eyesltd.co.uk

This VAT update is published for the general information of 4 Eyes Ltd personnel, clients and contacts. It provides only an overview of the rules and regulations in force at the date of publication, and no action should be taken without consulting the detailed legislation or seeking professional advice. Therefore no responsibility for loss occasioned by any person acting or refraining from action as a result of the material contained in this e-mail will be accepted by the authors or the firm.