[2016] UKFTT 0400 (TC)

TC05154
Appeal number:TC/2015/04130

VAT – penalty – Schedule 24 Finance Act 2007 – inaccuracy in VAT returns – whether deliberate – special circumstances – proportionality – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

SOLAR POWER PV LIMITED	**Appellant**
- and -	
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS	**Respondents**

TRIBUNAL: JUDGE JONATHAN CANNAN
MRS GAY WEBB

Sitting in public in Manchester on 28 January 2016

Mr Andrew Ronnan, director for the Appellant

Mr John Nicholson of HM Revenue & Customs for the Respondents

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DECISION

Background

1. The Appellant was in business selling and installing photovoltaic solar panel systems at commercial and residential premises. It has been VAT registered since 21 October 2010. Following a VAT audit visit on 1 December 2014 the Respondents considered that the Appellant had understated the VAT due on its VAT returns for periods 06/11, 09/11, 12/11 and 09/12. The total amount of VAT said to have been understated on those returns was £145,019.

2. On 20 February 2015 the Respondents made a penalty assessment against the Appellant pursuant to Schedule 24 Finance Act 2007 ("the Penalty"). The Penalty was in the sum of £50,756 and was made on the basis that the Appellant had deliberately understated its liability to VAT although it had not sought to conceal the understatement. The Appellant appeals against the Penalty.

3. We set out in detail below the circumstances in which the Appellant came to understate its VAT liability and why Mr Andrew Ronnan, the director of the Appellant who appeared before us, says that it should not be liable to a penalty. In broad terms the Appellant contends in its notice of appeal dated 1 July 2015 as follows:

(1) The liability to VAT arose in extraordinary circumstances involving an unlawful Government proposal to regulate the market for supply and installation of solar panels.

(2) There was no deliberate understatement of VAT and all the VAT due was paid.

(3) The Penalty failed to take into account health issues suffered by Mr Ronnan's family.

(4) The Penalty failed to take into account that the Appellant was utilising a form of cash accounting which also gave raise to overpayments in some periods.

(5) The Penalty is unfair and disproportionate.

4. We set out below the relevant statutory provisions governing penalties for inaccuracies in VAT returns. We then make findings of fact relevant to the issues in the appeal. In setting out reasons for our decision we consider the arguments raised by the parties.

Statutory Provisions - Penalties

5. The following references are to the penalty regime in place in 2011 and 2012 when the relevant returns were made. Save where otherwise noted references are to *Schedule 24 Finance Act 2007.*

6. Paragraph 1(1)(a) provides that a penalty is payable where a taxpayer gives HMRC a document including a VAT return and two conditions are satisfied. The first

condition for present purposes is that the document contains an inaccuracy which leads to an understatement of liability to VAT. The second condition is that the inaccuracy was careless or deliberate.

7. Paragraph 3(1)(a) provides that an inaccuracy in a document is "careless" if "*the inaccuracy is due to failure by [the taxpayer] to take reasonable care*". Paragraph 3 also distinguishes inaccuracies which are "*deliberate but not concealed*" from those which are "*deliberate and concealed*". It is not suggested by HMRC that the inaccuracy in the present case was concealed but they do contend that it was deliberate.

8. Paragraph 4 makes provision for the standard amount of penalties. The standard penalty for careless action is 30% of the potential lost revenue ("PLR"). The standard penalty for deliberate but not concealed action is 70% of the PLR.

9. Paragraph 5 defines the PLR as follows:

> "*(1) The potential lost revenue in respect of an inaccuracy in a document … is the additional amount due or payable in respect of tax as a result of correcting the inaccuracy ….*"

10. Paragraphs 9 and 10 provide for reductions in the standard penalties where a person discloses an inaccuracy. Disclosure in this context is defined as:

> "*(a) telling HMRC about it,*
>
> *(b) giving HMRC reasonable help in quantifying the inaccuracy…, and*
>
> *(c) allowing HMRC access to records for the purpose of ensuring that the inaccuracy … is fully corrected.*"

11. There is a distinction for these purposes between an "unprompted" disclosure and a "prompted" disclosure. Paragraph 9(2) provides that a disclosure is unprompted if made at a time when the person making it has no reason to believe that HMRC have discovered or are about to discover the inaccuracy. Otherwise a disclosure is prompted.

12. Paragraph 10 sets out the reductions for disclosure which HMRC must apply to a penalty. Those reductions depend on whether any penalty is a 30% penalty for a careless inaccuracy or a 70% penalty for a deliberate but not concealed inaccuracy. The reduction which HMRC must apply will depend on whether the disclosure was prompted or unprompted. It must also reflect the "*quality*" of the disclosure. Paragraph 9 defines the quality of a disclosure as including "*timing, nature and extent*".

13. The reductions in the standard penalty by reference to the quality of disclosure give a range of potential penalties. For example the standard penalty for a deliberate but not concealed inaccuracy is 70% of the PLR. Where there is prompted disclosure the penalty must be reduced but the minimum penalty is 35% of the PLR. In the

present case the Penalty has been applied at 35% of the PLR so that the maximum reduction for disclosure has been given on the basis that the inaccuracy was deliberate but not concealed and that the Appellant's disclosure was prompted.

14. Paragraph 11 permits HMRC to reduce a penalty generally "*if they think it right because of special circumstances*", but special circumstances does not include inability to pay. Paragraph 11 provides as follows:

> "*(1) If they think it right because of special circumstances, HMRC may reduce a penalty under paragraph 1….*
>
> *(2) In sub-paragraph (1) "special circumstances" does not include—*
>
> > *(a) ability to pay, or*
> >
> > *(b) the fact that a potential loss of revenue from one taxpayer is balanced by a potential over-payment by another.*"

15. There is no general discretion to reduce a penalty simply because there are mitigating circumstances.

16. Paragraphs 15 to 17 set out the rights of appeal in respect of penalties. The tribunal has jurisdiction to affirm or cancel HMRC's decision that a penalty is payable. It may also affirm HMRC's decision as to the amount of any penalty payable, or substitute another decision which HMRC would have had power to make. The tribunal's jurisdiction to reduce a penalty because of special circumstances is restricted to cases where HMRC's decision in relation to special circumstances is "flawed" in light of the principles applicable in proceedings for judicial review.

Findings of Fact

17. On behalf of the Respondents we heard evidence from Mrs Susan Walters who is a VAT assurance officer of HMRC. She made a witness statement and gave oral evidence. On behalf of the Appellant we heard evidence from Mr Ronnan who gave oral evidence. Based on that evidence and the documentary evidence before us we make the following findings of fact on the balance of probabilities.

18. The issues in this appeal are closely connected with the market for the installation of solar panels, taking advantage of what is known as the system for "Feed-in Tariffs" ("FITs"). The FIT scheme enabled electricity supply companies to make payments to small-scale producers of low carbon electricity, which includes electricity generated by solar photovoltaic cells. As such it encouraged members of the public and businesses to install solar panels. The Appellant's business model relied to a great extent on the amount of the FITs received by its customers.

19. The FITs are set by the Department for Energy and Climate Change ("DECC"). Rates were set by statutory instrument with effect from 1 April 2010. They included a "generation tariff" and an "export tariff". The generation tariff was calculated by reference to the electricity generated by a small-scale producer, including electricity

generated for own use. The export tariff was calculated by reference to the electricity supplied by a small-scale producer to an electricity supplier. Once a solar panel installation was installed and commissioned the generation tariff was fixed for 25 years subject only to an indexation allowance for inflation.

20. Much of the background which follows is taken from the Court of Appeal decision in *Department for Energy and Climate Change v Breyer Group plc and Others [2015] EWCA Civ 408*.

21. DECC had originally stated that FITs would remain unchanged over the 25 year period for new installations commissioned between April 2010 and April 2012 so as to provide certainty for the purposes of investment by small-scale producers. FITs were set so as to deliver a rate of return of approximately 5% of investment for well-sited solar installations. DECC repeatedly stated that it would not act retrospectively to change FITs. It was anticipated that after April 2012 FITs would reduce for new installations to reflect reductions in technology costs but so as to broadly maintain the same rate of return.

22. In February 2011 DECC announced that there would be a comprehensive review of the scheme. On 31 October 2011 it published a consultation document as part of that review. One proposal was for a reduction in the generation tariff with effect from 1 April 2012 by reference to installations which became eligible for FITs on or after 12 December 2011. Those installations would be eligible only for the reduced rate generation tariff after 1 April 2012. In effect DECC was proposing to bring forward from 1 April 2012 to 12 December 2011 the date by which installations had to be commissioned in order to qualify for the original tariffs for the life of the installation. If implemented this would have saved DECC some £1.6 billion.

23. The effect of publication of the proposal by DECC was to deter the vast majority of solar panel businesses from proceeding with installations, save in relation to installations which could be commissioned by 12 December 2011, a period of 6 weeks.

24. Friends of the Earth and others commenced judicial review proceedings against DECC in which they challenged the proposal. On 21 December 2011 Mitting J held that the proposal, if implemented, would be unlawful. On 25 January 2012 the Court of Appeal dismissed DECC's appeal.

25. DECC never implemented the proposal. Instead on 19 January 2012 the Secretary of State pursuant to powers in the Energy Act 2008 laid before Parliament a licence modification which had the effect of reducing the generation tariff with effect from 1 April 2012 in relation to solar panel installations commissioned on or after 3 March 2012. That modification was not challenged in the courts.

26. Thereafter a number of solar panel businesses including Breyer Group plc and the Appellant commenced a group action seeking damages against DECC. Collectively they claimed damages of approximately £195 million. Their complaint was that by the time the courts had ruled that the proposal was unlawful many

installations that would otherwise have been commissioned by 1 April 2012 had been abandoned as a direct result of the proposal. Initially the Appellant's claim was for damages of £243,000 but we understand that it has since been reduced to some £180,000. The Appellant's contribution to the costs of that group action was some £120,000 although a proportion of those costs were recovered.

27. The Appellant's business concentrated on installations up to 50 kWh, that is up to approximately 200 panels. The sales value of installations at the higher level would typically be in excess of £100,000 plus VAT. Smaller installations were for residential customers, typically retired persons who would receive a better rate of return than putting cash on deposit. The value of those installations would typically be in the region of £10-12,000 plus VAT. VAT on solar panel installations is charged at 5% on residential installations and 20% on commercial installations. Installations were required to be certificated before being commissioned and customers were invoiced once the installation was certificated.

28. On 24 October 2011, prior to the DECC proposal, the Appellant had ordered £500,000 worth of stock. Stock was purchased from a German supplier which offered the Appellant flexible credit terms. The Appellant offered similarly flexible credit terms to its customers giving them the opportunity to pay over a period of time. In the period following the DECC proposal the Appellant used quite a lot of the stock but as at 12 December 2011 it still had approximately £200,000 of stock and effectively no market.

29. VAT period 06/11 was the Appellant's first VAT return period. The Appellant completed and invoiced 18 installations in the period, which included 5 commercial installations. 4 of the 5 commercial installations were supplied to The Sidings (Whalley) Limited totalling £173,000 plus VAT. That was a company which had been owned by Mr Ronnan for many years. It owned a business park, receiving rental income and it had a steady cashflow. It would have a VAT inspection every 3 or 4 years.

30. In VAT period 09/11 the Appellant completed and invoiced 31 installations. All bar one were residential installations.

31. In VAT period 12/11 the Appellant completed and invoiced 55 installations. This included 10 commercial installations, of which 5 were 50 kWh installations.

32. No installations were invoiced between 8 December 2011 and 18 January 2012. In VAT period 03/12 as a whole there were 28 installations, of which 5 were relatively small commercial installations. Most were done before 3 March 2012 which was the cut-off date for the new generation tariff, effective on 1 April 2012. February 2012 was a particularly busy month when the Appellant was trying to move stock.

33. Mr Ronnan described the situation in late 2011 and early 2012 as something of a maelstrom of fast moving events, but said that he always wanted to pay the VAT falling due. We accept that was the position.

34. All the Appellant's VAT returns were submitted on time with full payment of the amounts shown on the returns as being due to HMRC. Mr Ronnan maintained the Appellant's books and records himself. He did not seek any advice in relation to VAT, although a professional firm of accountants prepared the Appellant's annual accounts.

35. Mr Ronnan maintained a sales ledger spreadsheet for the Appellant with invoices in date order, the first invoice being dated 31 December 2010. The sales ledger identified details in relation to each invoice including the name of the customer, whether it was a residential or commercial installation, the amount charged to customers and the relevant amount of VAT chargeable. There were totals for each VAT quarter.

36. The sales ledger also included a column headed "VAT Cash Flow Accounting". We can give an example of how Mr Ronnan used the spreadsheet. In period ending 06/11 the Appellant invoiced a customer for a commercial installation. The net contract price was £135,000. The sale appeared in row 16 of the spreadsheet and was dated 19 May 2011. However the entry appearing in the VAT column of the spreadsheet was left blank. The VAT Cash Flow Accounting column had a narrative which must have been entered at a later date stating "See Row 168".

37. Row 168 fell in period 06/12 in the sales ledger. It showed the name of the customer with the date 1 April 2012 and the narrative "(From Row 16)". It was not part of the Appellant's case that this was the date on which payment was received from the customer. The VAT Cash Flow Accounting column for Row 168 had an entry of £27,000, which was the VAT on the sale. The effect of this was that the Appellant accounted for output tax on the sale in period 06/12 when it could afford to pay the VAT rather than in period 06/11 when the tax was due.

38. By 2013 the Appellant had effectively ceased trading, but there was a VAT liability which had not been accounted for or paid. During the course of 2013 the Appellant accounted for and paid what VAT it could. For example in period 06/13 the Appellant effectively overstated its liability to VAT by £19,200. At this stage the adjustments being made by Mr Ronnan were not related to specific invoices but simply by reference to what the Appellant could afford. He was keeping track of the amount of VAT which he owed. The Appellant had never been in a position to borrow money from banks, instead cashflow shortages were funded by borrowings from Mr Ronnan. The VAT that was accounted for and paid was calculated by reference to a system of invoice accounting, but subject to what Mr Ronnan could afford to lend to the Appellant.

39. Mr Ronnan said in his evidence that he believed he had been operating cashflow accounting, albeit carelessly. He had heard the term "cash accounting scheme" for VAT and he thought it was there to help small businesses with their cashflow. He did not recall seeing any HMRC notice about the scheme. We consider this evidence further below.

40. The Appellant’s approach to accounting for VAT gave rise to understatements of VAT due in some periods and overstatements in other periods as follows:

Period	**VAT Properly Due £**	**VAT Declared £**	**Understatement/ (Overstatement) £**
06/11	70,999	30,999	40,000
09/11	24,122	23,648	474
12/11	150,985	54,322	96,663
03/12	35,500	35,500	0
06/12	2,926	29,576	(26,650)
09/12	13,021	5,139	7,882
12/12	27,899	27,899	0
03/13	0	9,554	(9,554)
06/13	327	19,527	(19,200)
09/13	232	3,526	(3,294)
12/13	0	9,035	(9,035)
03/14	0	8,000	(8,000)
06/14	0	3,426	(3,426)
09/14	0	0	0
Total:			**£ 65,860**

41. The overall effect was that as at 30 September 2014 there was a sum of approximately £65,000 in VAT which had not been accounted for or paid.

42. The evidence before us also included the Appellant’s balance sheets which showed net assets as follows:

Year Ended 30 September	**Net Assets £**
2011	(1,919)
2012	27,778
2013	(214,756)
2014	(256,657)

43. On 17 October 2014 HMRC wrote to the Appellant to arrange a VAT compliance visit. A factsheet accompanying the letter stated that if a trader knows or suspects something is wrong then it should tell HMRC what is wrong as soon as the compliance check starts.

44. On 1 December 2014 Mrs Walters conducted the visit at the premises of the Appellant in Whalley, Lancashire. She met with and interviewed Mr Ronnan. During the course of the visit they moved to Mr Ronnan's home address which was nearby. This was the Appellant's first VAT visit.

45. Mr Ronnan told Mrs Walters that output tax was accounted for when sales were invoiced. Early on in the visit he told Mrs Walters that VAT of approximately £62-64,000 was due. He produced a copy of the sales ledger spreadsheet. Mr Ronnan also referred during the visit to "cash accounting issues" and to the litigation the Appellant was involved in arising from DECC changes to FITs described above. He stated that as a result the Appellant had only declared the VAT it could afford to pay and that the business was now winding down. Mr Ronnan also described certain personal issues involving his son.

46. It was suggested to Mr Ronnan in cross examination that the reason he referred to the liability of £62-64,000 so early on in the visit was because he knew his VAT returns had been incorrect and he had been following the advice in the factsheet. Initially Mr Ronnan maintained in his evidence that he had understood his method of accounting for VAT was acceptable. He was unaware that there was any turnover limit for using the cash accounting scheme and he had always understood that VAT cash accounting was available to be utilised by small businesses not to avoid paying VAT but to assist in their cashflow. Later in his evidence he stated that as a businessman he didn't think he was "doing it [ie the cash accounting] right" but that there was a lot going on.

47. We find that Mr Ronnan was not doing anything like cash accounting. He was not accounting for output tax by reference to payments received for sales but simply by reference to cash available in the business. A quick perusal of HMRC Notice 731 "Cash Accounting Scheme" would have identified that the scheme permitted businesses to account for output tax by reference to payments received rather then VAT invoices issued. It would also have shown that the scheme was subject to conditions and that it could not be operated if taxable supplies in the next year were expected to be more than £1,350,000. The Appellant did not seek to suggest that it would have satisfied that condition. We accept that Mr Ronnan had not looked at the Notice and that he was unaware of the turnover limit.

48. Mrs Walters made an assessment to VAT in December 2014 in the sum of £65,824 for periods 06/11 to 09/14. That figure was agreed by Mr Ronnan and it was paid by the Appellant in February 2015. Shortly before February 2015 Mr Ronnan had sold The Sidings (Whalley) Ltd and lent part of the proceeds to the Appellant to pay the liability.

49. Mrs Walters considered the understatements of VAT by the Appellant were deliberate but not concealed. She gave the maximum possible reduction for disclosure so that the Penalty was calculated at the rate of 35% of the PLR as follows:

VAT Period	PLR £	Penalty £
06/11	40,000	14,000
09/11	474	166
12/11	96,663	33,832
09/12	7,882	2,758
Total:	**£ 145,019**	**£ 50,756**

50. The PLR in the above table is the output tax which the Appellant did not declare in the relevant VAT periods. In period 06/11 it can be traced to two specific invoices identified in the sales ledge, including the one referred to in detail above. In the other periods specific invoices were not identified in the sales ledger, there is simply a global reduction identified.

51. The Penalty was assessed on the basis of Mrs Walter's recommendation. She did not consider that there were any special circumstances to justify any further reduction in the Penalty. In particular she did not consider that the litigation with DECC and the need to fund that litigation amounted to special circumstances. She considered that the Appellant ought to have declared the correct amount of VAT and sought a time to pay arrangement with HMRC.

52. We understand that interest on the VAT assessed amounted to £8,824 by December 2014. The Appellant has questioned that interest but there is no right of appeal in relation thereto. It was not suggested that the mathematical calculation of interest was incorrect.

53. Mr Ronnan also mentioned in his evidence certain personal difficulties suffered by his son in 2012 which he said he did not want to dwell on. He later described those difficulties, which were particularly acute in August 2012, and the effect they had on his family. We see no reason to elaborate here, but we have taken them into account in our decision.

54. We do not accept that Mr Ronnan could honestly have believed he was entitled simply to declare the VAT which the Appellant could afford to pay. He is an intelligent and experienced businessman. VAT can be a complicated tax, but it strains credibility to think that he honestly believed the Appellant was entitled to account for VAT in this way.

55. It was put to Mr Ronnan in cross-examination that he had deliberately understated the VAT liability. He responded by saying that the Appellant found itself in exceptional circumstances. That is true for the period after 31 October 2011. However it does not explain why Mr Ronnan accounted for VAT in the way he did. He started accounting for VAT in this way in the Appellant's first VAT return for period 06/11. Mr Ronnan's response was not consistent with his case that he believed the Appellant was entitled to account for VAT in the way it did. Mr Ronnan was unable to give any satisfactory explanation as to why he started understating the

Appellant's liability in June 2011. We infer that the Appellant was suffering cashflow difficulties prior to the DECC proposal and that is why the Appellant understated the VAT liability.

56. At one stage Mr Ronnan said in his evidence "*it appeared to me that I was acting within the law, but at risk of HMRC taking a view that it could attract penalties*". That does not sit easily with his case that he believed he was entitled to account for VAT in the way he did. If Mr Ronnan really thought that there was such a risk then he would have realised that he should check the position with the Appellant's accountants or with HMRC.

57. In the light of all the evidence we are satisfied that Mr Ronnan was aware that the VAT returns he was submitting from 06/11 onwards were inaccurate. He deliberately understated the Appellant's VAT liability in periods 06/11, 09/11, 12/11 and 09/12. In other periods identified above he deliberately overstated the Appellant's VAT liability. We are satisfied that Mr Ronnan always intended that the Appellant would settle its VAT liabilities. However he knew he ought to have been declaring output tax in the period the invoices were issued.

58. Mr Ronnan stated that he was unaware that it was possible to make time to pay arrangements with HMRC. If that is true it is unfortunate, because that would have been the proper thing to do. It may be that Mr Ronnan did not fully focus on what he was doing because of difficulties in his family life. However we do not consider that those difficulties would have clouded his judgment to such an extent that he did not realise at the time that what he was doing was wrong.

Reasons

59. It is for the Respondents to establish that the Appellant deliberately lodged VAT returns which understated its liability to VAT. Mr Nicholson for the Respondents submitted that the Appellant, through Mr Ronnan, knew full well that the VAT returns being lodged were incorrect. HMRC accepted that the Appellant had not sought to conceal the understatements and they gave the maximum reduction for disclosure.

60. Mr Nicholson submitted that HMRC had been right to conclude that there were no circumstances to justify a special reduction. In particular the following matters did not amount to special circumstances:

(1) The fact that the Appellant always intended to pay its VAT liabilities.

(2) Mr Ronnan's family circumstances.

61. Mr Nicholson further submitted that there was nothing disproportionate about the Penalty. Full mitigation had been given for disclosure. This was a serious offence and justified a substantial penalty which had been calculated in accordance with the provisions of Schedule 24.

62. Mr Ronnan submitted that he had carelessly understated VAT on the Appellant's returns, rather than deliberately. His carelessness was in failing to realise

that he had operated cash accounting incorrectly. For the reasons given above in our findings of fact we do not accept that submission.

63. Mr Ronnan relied on a decision of Flaux J in *Bank Mellat v HM Treasury [2015] EWHC 1258 (Comm)*, in particular part of the judgment dealing with whether a shareholder can recover damages for losses which are merely reflective of losses suffered by a company. With respect to Mr Ronnan, who presented the Appellant's arguments carefully and cogently, that case has no relevance or application in the present appeal.

64. Mr Ronnan also relied on an argument that the Penalty was disproportionate. He relied on a decision of the European Court of Justice in *Louloudakis v Elliniko Dimosio Case C-262/99* to support of his argument that a penalty under Schedule 24 is subject to principles of proportionality.

65. Mr Ronnan's case was essentially that in assessing proportionality, HMRC and this Tribunal should take into account the financial position of the Appellant, including the damage to the Appellant caused by the DECC's unlawful actions. Further, it was unfair to apply a penalty based on the PLR when the VAT was always going to be paid.

66. In the light of our findings of fact the conditions for a penalty under Schedule 24 are satisfied. We must however consider the following issues dealt with by the parties in their submissions:

(1) Whether the Respondents' decision on special circumstances was flawed;

(2) Whether the Penalty is disproportionate in the Appellant's case.

67. When the Respondents issued the Penalty they decided that there were no special circumstances. In particular Mrs Walters considered that the litigation with DECC including the need to fund that litigation did not amount to special circumstances. She considered that the Appellant ought to have declared the correct amount of VAT and sought to agree a time to pay arrangement.

68. The Court of Appeal decision in *Clarks of Hove v Bakers' Union* [1978] 1 WLR 1207 at p1216 held that in the context of special circumstances, the word 'special' means "something out of the ordinary, something uncommon". In *Crabtree v Hinchcliffe* [1971] 3 All ER 967 Lord Reid stated at p976 that "'special' must mean unusual or uncommon – perhaps the nearest word to it in this context is 'abnormal.'" In the same case, Viscount Dilhorne said at p983 that "for circumstances to be special they must be exceptional, abnormal or unusual…".

69. The tribunal has generally accepted these meanings and we propose to do the same. We would add that the special circumstances must in our view also go some way to excusing or mitigating the conduct which has given rise to the Penalty, whilst at the same time recognising that there is no general power to mitigate. It appears to us that our jurisdiction involves considering HMRC's decision as to whether there are special circumstances. If there are special circumstances then HMRC has a discretion to reduce a penalty. It is only if we consider that HMRC's decision in relation to the

application of paragraph 11 Schedule 24 is flawed that we can reduce the Penalty on the basis of special circumstances. The approach was summarised by the F-tT in *Collis v HMRC* [2011] UKFTT 588(TC):

> *"[36] … Judicial review may be pursued in relation to decisions of public bodies on a number of grounds. Included amongst these are the grounds of illegality and fairness. In the context of a decision of HMRC as to whether a reduction in a penalty should be made on account of special circumstances, the general test will be whether the decision is so demonstrably unreasonable as to be irrational or perverse, such that no reasonable authority could ever have come to it (Associated Provincial Picture Houses Ltd v Wednesbury Corporation [1948] 1 KB 223, HL).*
>
> *[37] …The tribunal should also consider whether HMRC have erred on a point of law (see Customs & Excise Commissioners v J H Corbitt (Numismatists) Ltd [1980] STC 231; John Dee Ltd v Customs & Excise Commissioners [1995] STC 941). This will also include considering whether any internal HMRC policy on the application of the special circumstances rule is being applied too rigidly so as to amount to a fetter on HMRC's discretion."*

70. We must first consider whether there were special circumstances to excuse or mitigate the conduct which gave rise to the Penalty. Schedule 24 directs that inability to pay does not amount to special circumstances. However in our view we can still consider whether the circumstances which gave rise to the Appellant's inability to pay amount to special circumstances.

71. The Appellant's cashflow difficulties in period 06/11 were nothing to do with the announcements by DECC in relation FITs. The significant announcement was made on 31 October 2011. Mr Ronnan's evidence was that where there was a cashflow difficulty VAT was paid when he could afford to lend money to the Appellant. We had no evidence as to the cause of the cashflow difficulty in 06/11.

72. The other period in which there was a significant understatement was period 12/11. That was the largest understatement and we are satisfied that the cashflow difficulty was caused at least in part by the issues with FITs and the DECC proposal announced on 31 October 2011.

73. Paragraph 11(2)(b) provides that special circumstances does not include the fact that a potential loss of revenue from one taxpayer is balanced by a potential overpayment by another. That is not the situation in the present case, but it is the case that the PLR in the four periods on which the Penalty was calculated was partly balanced by overpayments in other periods.

74. We are not satisfied that financial difficulties arising from the DECC proposal or the circumstances in which Mr Ronnan overstated the Appellant's liability to VAT in later periods justify a special reduction, still less that Mrs Walters decision not to give a special reduction was perverse or irrational. The proper response to cashflow difficulties is to negotiate a payment schedule. The circumstances did not excuse or

mitigate Mr Ronnan's decision to put in an inaccurate return. Mr Ronnan's intention to pay the VAT which was not declared at a later date does not in our view excuse his conduct. It might mitigate the seriousness of his conduct but the question we must ask is whether it is a special circumstance which ought to be reflected in a reduction in the Penalty over and above the reduction given for disclosure. It is difficult to see that it should amount to a special circumstance in the light of paragraph 11(2)(b).

75. In our experience of cases coming before this tribunal it is common that traders who fail to put in returns or to pay their VAT on time are not intending to evade VAT completely. They fall within a different penalty regime in the form of the default surcharge. By submitting incorrect returns the Appellant effectively avoided paying the VAT due, avoided recovery action by HMRC and avoided the default surcharge regime. We accept that the penalties under that regime at a maximum of 15% would have been significantly less than under Schedule 24 although no calculation to that effect was provided. It may be unusual for a trader to put in incorrect returns with the intention of making good the understatement in a later return, but we cannot say that the decision not to treat that as a special circumstance and reduce the Penalty was perverse or irrational.

76. We do not consider that Mr Ronnan's family difficulties excused or mitigated his conduct. To be fair to Mr Ronnan he did not strenuously argue that they did.

77. We have also considered whether the circumstances as a whole might be regarded as special circumstances. Again, we are not satisfied in the light of the circumstances as a whole that the Respondents' decision was perverse or irrational.

78. Finally we must consider the issue of proportionality raised by Mr Ronnan. He did not suggest that the penalty regime was inherently disproportionate, rather that it gave rise to a disproportionate penalty in the light of all the circumstances of the Appellant's case.

79. The factors relied upon by Mr Ronnan in arguing that the Penalty was disproportionate were effectively the same as those we have considered above in the context of special circumstances. In addition, we accept that on the occasion of Mrs Walters' audit visit Mr Ronnan was completely open about the existence of the VAT liability. He did not seek to hide it in any way and the Appellant has since paid the liability in full.

80. We have had regard to the full and detailed analysis of the principle of proportionality by the Upper Tribunal in the context of VAT default surcharges in *Commissioners for HM Revenue & Customs v Total Technology (Engineering) Limited [2012] UKUT 418 (TCC)* and *HM Revenue & Customs v Trinity Mirror plc [2015] UKUT 421 (TCC)*. Neither case was cited to us, but both referred to the European Court of Justice decision in *Louloudakis v Elliniko Dimosio Case C-262/99* which the Appellant relied on. In the context of VAT, penalties must not go beyond what is strictly necessary for the objectives pursued, and a penalty must not be so disproportionate to the gravity of the infringement that it becomes an obstacle to the underlying aims of the VAT directive. However a court or tribunal must be astute not

to substitute its own view of what is fair for the penalty which Parliament has imposed. Further, as appears from the Court of Appeal in *International Transport Roth GmbH v Secretary of State for the Home Dept* [2003] *QB 728* it must be asked whether the penalty is "not merely harsh but plainly unfair".

81. We have also found helpful the analysis of proportionality by the F-tT in *Bluu Solutions Ltd v HM Revenue & Customs [2015] UKFTT 0095 (TC)* at [161] to [179], including its reference to the Supreme Court decision in *Bank Mellat v HM Treasury (No 2) [2013] UKSC 39*.

82. In our view the Penalty is not disproportionate. Some may consider it harsh on the particular facts of this case, but in our view it is not unfair. It reflects the seriousness of the Appellant's conduct whereby Mr Ronnan deliberately submitted false returns over an extended period in order to gain a cashflow advantage.

Conclusion

83. For the reasons given above we must dismiss the appeal.

84. 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.

JONATHAN CANNAN
TRIBUNAL JUDGE

RELEASE DATE: 7 JUNE 2016