



TC05463

Appeal number: TC/2016/01053

NATIONAL INSURANCE – whether failure to pay Class 2 NIC was due to lack of due care and diligence – whether entitled to make (and be credited for) late payment of Class 2 NIC

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

RICHARD THOMAS

Appellant

- and -

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

**TRIBUNAL: JUDGE VICTORIA NICHOLL
MR CHRISTOPHER JENKINS**

Sitting in public at Brighton on 28 September 2016

The Appellant in person

Mrs Ramsay (HMRC Presenting Officer) for the Respondents

DECISION

Introduction

1. This appeal is against the decision of the Respondents (“HMRC”) to treat any
5 class 2 national insurance contributions (“Class 2 NICs”) paid by the Appellant (“Mr
Thomas”) for the period from the 1967-68 contribution year to 5 April 2008 as not
having been paid for the purposes of any contributory benefit. The decision-maker
found on 6 November 2015 that Mr Thomas’s failure to pay the NICs within the
prescribed time limits was attributable to his ignorance or error, and that the ignorance
10 or error was the result of his failure to exercise due care and diligence.

2. HMRC issued a varied notice of decision on 21 April 2016, after Mr Thomas
had made his appeal to HM Courts and Tribunal Service by reference to the decision
dated 6 November 2015. This varied decision accepted that class 1 national insurance
contributions (“Class 1 NICs”) had been paid in 1971-72, but did not change the
15 decision as regards the carry back of Class 2 NICs claimed by Mr Thomas which is
the subject of this appeal.

Background and facts found

3. We found the following facts from the evidence in the tribunal bundle and the
oral evidence from Mr Thomas and HMRC’s witness, Mrs L A Crawford.

4. Mrs Crawford is the officer in HMRC who reviewed the decision dated 6
20 November 2015. Mrs Crawford has dealt with the collection of Class 2 NICs and
associated issues since January 2000 and so was able to provide us with helpful
information on the chronology of changes in National Insurance Contributions
(“NIC”) and the agency responsible for NIC, the significance of manual entries on a
25 permanent NIC record for an individual and the procedures for the collection,
granting exceptions and waivers of Class 2 NICs liabilities.

5. Mr Thomas presented his case clearly and frankly, confirming the evidence that
he could recall and advising us of events and information which, not surprisingly after
some 50 years, he could not recall.

6. Mr Thomas is a musician. He left school in 1966 and was employed as a
30 computer clerk in Birmingham for some two years. Mrs Crawford explained, and we
accepted, that prior to commencing employment Mr Thomas would have visited his
local NIC office to register for NIC and obtain his first contribution card. Class 1
NICs were paid for Mr Thomas as his employer would have stamped the card and
35 returned it once completed. Mr Thomas does not recall this visit or the arrangements
with his employer.

7. In 1968 Mr Thomas joined a group called ‘Breakthru’ and became a self-
employed musician. The group disbanded and he moved to London in 1970 to play
with a group in pubs and clubs, earning very little income and moving address
40 frequently. He did not have a telephone.

8. Mrs Crawford advised us that the entries on the agency's permanent NIC record for Mr Thomas show that he paid 18 Class 2 NICs in 1968/69, although interestingly these were originally recorded as Class 1 NICs and crossed through. Mrs Crawford was also able to advise us that the faint manuscript entries on Mr Thomas's permanent
5 NIC record show that he was sent correspondence about his failure to return his contribution card on 26 February 1969, that he had received letters about provisional and absolute waivers of NIC liabilities (that would typically have followed investigations and meetings to establish the level of his low earnings) and that he had been sent statements. Copies of this correspondence are no longer available but Mrs
10 Crawford referred to sample letters in the tribunal bundle. Mr Thomas has no recollection of visiting, being interviewed by or receiving letters from a NIC agency during this period.

9. In 1970 Mr Thomas worked as a stage hand for some 9 months. Mrs Crawford was able to find a record showing that the Shaftesbury Theatre had operated a 'Tax
15 Deduction Card' for him and so accepted that a further 38 Class 1 NICs should be added to Mr Thomas' record notwithstanding that there was no record of the employment on his permanent NIC record.

10. From 1973 until 1975 Mr Thomas was self-employed as a touring musician. He was living on a low subsistence income until 1975 when he had a period in which he
20 had no work at all. As he could no longer make ends meet, he sought to claim benefits in July 1975. He was informed that his NIC record was not sufficient to claim unemployment benefit but that he was entitled to social security payments.

11. Mrs Crawford provided us with the following background to the reconstruction and computerisation of NIC in 1975 and later significant changes. The introduction of
25 class 4 national insurance contributions ("Class 4 NICs") was a consequence of the introduction of earnings related contributions for employed workers. It was decided that the flat rate of Class 2 NICs should continue as the basis for entitlement to benefits for self-employed workers but, in order to take account of the impact of the self-employed being able to claim certain benefits and the new earnings related
30 contributions for employed earners, Class 4 NICs were introduced as profits based charge for the self-employed. The charge is described as an additional class of contribution and contributions are paid into the National Insurance Fund in the same way as other contributions, but payments are not linked to individual contribution records.

35 12. National insurance records were computerised in 1975. Class 1 NICs moved from a stamp based system to collection through PAYE and Class 4 NICs were to be collected with income tax from January 1976 by Inland Revenue (subsequently HMRC). Mrs Crawford noted that the agency collecting Class 2 NICs changed over the years from the Department of Social Security (DSS and then DHSS) to the
40 Contributions Agency. The Contributions Agency merged with Inland Revenue in 1999 and steps were taken to ensure that all computers were updated, but there were no checks of previous systems or transfers of this information. The merger allowed workers to make a joint registration for tax and all NIC. At this time Mr Thomas was

registered for income tax and Class 4 NICs. The National Insurance Act 2015 now provides for the collection of Class 2 NICs with Class 4 NICs under self-assessment.

13. The tribunal bundle includes post 6 April 1975 computer records for Mr Thomas, referred to RD18s and RD19s. The RD19 shows a notification of a change
5 in Mr Thomas' address on 29 November 1981, but Mrs Ramsay explained that this showed that a previous address was on Mr Thomas' 1975/76 schedule and that no further address had been notified.

14. By 1976 Mr Thomas's new group had some commercial success. He stopped
10 claiming the benefit and resumed his work as a self-employed musician. At some time between 1976 and 1978 Mr Thomas received a publishing advance and his income rose incrementally with the success of TV jingles and other work.

15. In 1978 Mr Thomas appointed Bryce Hanmer of Piccadilly in London as his accountants to prepare his tax returns for the years commencing 1977/78. Mr Thomas used an accountant as he is nervous of paperwork and was concerned that his financial
15 affairs should be in order as he had met his future wife. Mr Thomas recalls that "I do remember asking them about the Class 4 NICs on my return and being told that they were my self-employed National Insurance contribution. (It was certainly not explained that this was a tax on self-employed profits or that I should also pay Class 2 NICs)".

20 16. In 1982 Bryce Hanmer advised Mr Thomas that his earnings had exceeded the VAT threshold. Mr Thomas took the necessary action to register for VAT as a self-employed trader. It was found that the threshold had in fact been exceeded in the previous year and Mr Thomas made the additional payments due. Mr Thomas believes that Bryce Hanmer ceased trading some time in 1984 and so he appointed
25 another firm of accountants in Brighton to prepare his tax returns. From 2008/09 Mr Thomas submitted his self-assessment returns online as his income had dropped and no longer warranted the cost of using an accountant.

17. Between 1978 and 2014 Mr Thomas did not receive any correspondence about
30 his failure to pay Class 2 NICs when he was paying Class 4 NICs. Mrs Crawford advised that information about the payment of Class 2 NICs would have been included with his tax returns. Mr Thomas explained that as these were prepared by his accountant he did not see this information. Mrs Crawford also explained that the NIC agencies had run two publicity campaigns from January to February 2001 and from
35 July to August 2005 in newspapers and on local radio stations. Mr Thomas does not recall seeing or hearing these campaigns and he noted that he does not take a newspaper or listen to local radio.

18. Shortly after his 65th birthday Mr Thomas called the Pensions Office to ask
40 about his pension. He was informed that there was no record of his self-employment and that he was last recorded as unemployed in 1976. Mr Thomas was advised to send in a form CWF 1 to notify his self-employment and he completed it to notify his self-employment from 1 January 1976. He then entered into correspondence with HMRC about paying Class 2 NICs for the period 1 January 1976 to his retirement

5 date to restore his NIC record. This was allowed for a period of six years from 6 April 2008 to 5 April 2014, but HMRC told Mr Thomas on 18 December 2014 that he would not be given any credits for the period prior to 6 April 2008. HMRC also decided that in these circumstances it would not require Mr Thomas to pay the Class 2 NICs due for the period prior to 6 April 2008.

10 19. Mr Thomas queried this decision and a varied decision was issued on 6 November 2015. Mr Thomas requested a review of the decision of 6 November 2015. Mrs Crawford reviewed the decision, but confirmed in her letter of 27 January 2016 that she upheld the decision. Mr Thomas appealed against this review decision. As noted in paragraph 2 above, the decision was later varied on 21 April 2016.

15 20. HMRC's later decisions refer to contributions from the 1967-68 contribution year to 5 April 2008, but Mr Thomas's appeal reflects the information on his form CWF1 application dated 15 December 2014 as he only claims the right to pay Class 2 NICs from 1976. As this is consistent with the form RD 18 that shows that Mr Thomas stopped receiving credited contributions for unemployment at the beginning of the 1976/77 tax year, we have treated his claim as relating to Class 2 NICs for the period 6 April 1976 to 5 April 2008 ("the Class 2 NICs liability period"). Mr Thomas does not seek to carry back Class 2 NICs in respect of any earlier period of self-employment.

20 **The law**

21. The law relating to liability for NIC and to its collection, the exceptions, time limits and decisions has changed a number of times over the period from 1966 when Mr Thomas first registered for NIC to his retirement in 2014.

25 22. It is agreed by the parties that Mr Thomas has a liability to account for Class 2 NICs in respect of the Class 2 NICs liability period. It is agreed by the parties that Mr Thomas had a liability during the Class 2 NICs liability period to notify his changes of address. It is agreed by the parties that the time limits for making the payments relating to the Class 2 NICs liability period have passed. This appeal relates to Mr Thomas's request to make the payments late under the following provisions that applied sequentially over the Class 2 NICs liability period:

23.1 regulation 36 of the Social Security (Contributions) Regulations 1975;

23.2 regulation 41 of the Social Security (Contributions) regulations 1979; and

35 23.3 regulation 6 of the Social Security (Crediting and Treatment of Contributions and National Insurance Numbers) Regulations 2001.

40 These regulations provide that NICs that have been paid late may be treated as having been paid on an earlier date if it can be shown to HMRC's (or the predecessor agencies') satisfaction that the failure to pay on time is because of ignorance or error, and that the ignorance or error was not due to a failure, on behalf of the contributor, to exercise due care and diligence.

23. Section 8(1)(m) of the Social Security Contributions (Transfer of Functions, etc) Act 1999 provides that it shall be for an officer of the Board to decide such issues relating to contributions as may be prescribed by regulations. Regulation 155A(2)(j) provides that the decisions that the Board can make includes:

5 “whether, in the case of a Class 2 contribution remaining unpaid by the due date, the reason for the non-payment is the contributor’s ignorance or error, and, if so, whether that ignorance or error was due to his failure to exercise due care and diligence...”.

24. Regulation 10 of the Social Security (Decisions and appeals) Regulations 1999 provides that if it appears to the tribunal that the decision of the officer of the Board under appeal should be varied, “the decision shall be varied in that manner, but otherwise shall stand good”.

Submissions

25. Mr Thomas submits that he should be allowed to make and carry back late payment for the Class 2 NICs liability period. He accepts that the reason for the non-payment during the Class 2 NICs liability period was his ignorance or error, but he claims that this was not due to his failure to exercise due care and diligence. He was registered as self-employed from 1968 and sought to keep his affairs in order as soon as his earnings increased above low subsistence income when he resumed self-employment in 1976. He appointed an accountant in 1978 and asked about the Class 4 NICs he was paying. He accepted the answer that this was his NIC contribution to his pension and had no reason to believe that further enquiry should be made of the NICs agency or a financial adviser about any further NICs liability.

26. Mr Thomas submits that the NICs collection agencies over the years also failed in that they did not contact him between 1978 and 2014, despite his payment of Class 4 contributions throughout this period. He did not receive any deficiency notices. Mr Thomas notes that the NICs agency merged with HMRC in 1999 and that the failure to contact him is particularly surprising after that date.

27. Mr Thomas notes that he sought to pay all of his tax and contributions liabilities in the Class 2 NICs liability period in a timely fashion, and should not be treated as if he sought to delay or chose not to pay Class 2 NICs. Given the very low cost of the fixed rate Class 2 NICs compared to the earnings based Class 4 NICs he was paying, it is clear that he would have paid them if he had known that were they payable. His intention and actions to keep his affairs in order are demonstrated by the fact that his accountant notified him that his earnings had exceeded the VAT threshold in 1981, and he then registered for VAT and has since managed his VAT personally.

28. HMRC submit that Mr Thomas was required to become an insured person according to his classification as a self-employed person in the 1967-68 contribution year (section 1 National Insurance Act 1965) and he remained responsible for ensuring that he was paying his Class 2 NICs. Mr Thomas’s permanent NIC record shows that although he first paid Class 2 NICs in 1968, he did not meet his Class 2 NIC liability. HMRC hold no evidence to show Mr Thomas remained compliant after

the contribution year 1969-70, which was the last year his NI record shows he paid Class 2 NICs. A letter in March 1973 requesting the return of his contribution card came back undelivered. Mr Thomas failed to inform the NIC agency of his new address and no further contribution cards were sent to or received from him.

5 29. HMRC submit that when considering how the legislation affects this case, it is
necessary to look at all of the circumstances surrounding the non-payment of the
contributions in question and the steps that Mr Thomas took to make sure that his
affairs were in order. In this context HMRC consider that Mr Thomas was aware of
his NICs liability. Mrs Ramsay noted the information that was sent to Mr Thomas
10 over the years, including notification of the award of both a provisional waiver of
NICs and an absolute waiver for periods of time in 1968/1969 and 1970/1971. These
notifications would have advised Mr Thomas that he was still liable to pay the arrears
and given him information that explained the effects of non-payment of NICs on
future entitlement to benefit. HMRC also note the two publicity campaigns referred to
15 in paragraph 17 above and the information in the notes and guidance provided with
tax returns. Mr Thomas relied on the word of his accountant that Class 4 NICs
contributed towards his state pension and assumed that he was paying the correct
NICs. HMRC do not consider that making such enquiry was acting with due care and
diligence.

20 30. HMRC note that if Mr Thomas had “paid his Class 2 (self-employed) NICs,
then the Department would have continued to receive contribution cards from him
until 1974-75 then his NI record would have been noted with his SE liability when the
records were computerised.” Instead, in the year when the reconstructed NI scheme
began and all records became computerised in 1975 Mr Thomas claimed
25 unemployment benefit and notified his address but, by the time that he was sent a
statement of the shortfall in his contributions, he had moved address and failed to
notify his new address. He did not notify his post 1975 self-employment until 2014.

Discussion

31. We noted that the onus of proof in the appeal is for Mr Thomas to show that, on
30 the balance of probabilities, his ignorance or error in failing to make the payments of
Class NICs in the Class 2 NIC liability period was not due to his failure to exercise
due care and diligence.

32. Mrs Ramsay referred us to three cases in support of HMRC’s case, *Walsh v*
Secretary of State (High Court, 28 March 1994) (“*Walsh*”), *Adojutelegan v Clark*
35 [2004] STC (SCD) 524 (SpC430) (“*Adojutelegan*”) and *Rose v HMRC* [2007] STC
(SCD) 129 (SpC574) (“*Dr Rose*”). Mrs Crawford had also referred to the leading
case of *RCC v John Joseph Kearney* [2010] STC 1137 (“*Kearney*”) in her review
letter of 27 January 2016. The Court of Appeal decision in *Kearney* provided us with
guidance on what “care and diligence” mean in the context of this statutory test.

40 33. We noted that the passage from *Kearney* that is cited in Mrs Crawford’s letter as
Lady Justice Arden’s conclusion in the Court of Appeal is in fact taken from the High
Court decision. In the passage quoted, the Judge states that “to rely on an assumption,

which has not been shown to have been positively induced, and without making any further enquiries cannot amount to the exercise of due care and diligence...” In the Court of Appeal Lady Justice Arden considered the question of enquiries further and commented (at paragraph 29) that “the statutory question assumes that there is at least
5 in general a duty to make some enquiries and in appropriate circumstances to follow them up. I agree with the Judge that those enquiries need not necessarily be made of NICO. The enquiries might be sufficiently made if they were made of the employer or trade union”.

34. Lady Justice Arden’s decision then considers what approach should be adopted to determine the presence or absence of due care and diligence and concludes [at
10 paragraph 34]:

“...the correct approach, [which] is to treat all relevant circumstances as factors which have to be balanced together to reach an assessment or evaluation on a case-by-case basis as to whether due care and diligence
15 was exercised and, if not, whether the failure was the cause of the contributor’s ignorance of his obligation to pay contributions when he was bound or entitled to pay them.” ...

“... I do not think it is possible to produce a definitive list of relevant factors. However, they would include the contributor’s age and any relevant physical disability or incapacitation. ... Knowledge of the NIC
20 scheme is also likely to be a very important factor.”

“Moreover, there cannot logically be an absolute rule that, if the contributor has knowledge of the existence of some aspect of the NIC scheme, he can never show that he exercised due care and diligence
25 unless he made further enquiries about his rights or obligations.”

35. We considered Mr Thomas’s enquiries and knowledge of the NIC scheme and the other factors as in this case in accordance with Lady Justice Arden’s guidance in *Kearney*. HMRC have sought to compare Mr Thomas’s circumstances to those in
30 *Walsh*. Mr Walsh was a self-employed barrister who had paid Class 2 NICs using a contribution card until he went away on his family holiday in September 1974. The contribution card fell to the back of his desk drawers and he forgot to resume paying his Class 2 contributions on his return from holiday. Mr Walsh did not use or make enquiry of an accountant but began paying Class 4 NICs with effect from 1 January
35 1976 with his income tax. He assumed from the fact that he was not pursued for the post September 1974 NICs and that he was paying Class 4 NICs, that he had nothing further to pay.

36. In contrast, Mr Thomas had only paid 18 Class 2 NICs in 1968-69, and interestingly these were originally noted as Class 1 NICs on his permanent NIC
40 record. His remaining pre 1976 NIC payments were Class 1 NICs by his employer or credited. We found from this that Mr Thomas was not familiar with the Class 2 NICs system notwithstanding the payments in 1968-69. After Mr Thomas resumed his self-employment in 1976 he wanted to make sure that his affairs were in order and he asked about the Class 4 NICs. He accepted his accountant’s response that it was his

NICs contribution as a registered self-employed person. Mr Thomas states in his appeal that he was “always aware that one must contribute to receive a State Pension [but] I have no memory of being told about or ever understanding different classes of NIC contributions”. We found that Mr Thomas is uncomfortable but cautious with paperwork and therefore seeks help. He appointed an accountant as he was concerned to do the right things in order to keep his affairs in order and diligent to comply with what he understood to be all of his obligations.

37. HMRC argue that even if Mr Thomas had made this error at the outset, he should have been alerted by the HMRC literature referred to in paragraph 17 above. Mrs Ramsay referred us to a passage in the case of *Dr Rose* that “he was aware at the time of his choices [to pay voluntary contributions], or at least he would have been aware of them had he read the leaflets he was sent and had he made the reasonable enquires that those leaflets should have prompted.” It was found in that case that Dr Rose “decided not to pay because he could not afford to do so. Alternatively, he was in error – he was wrong so to decide that as he now sees it.”

38. We considered this but found that, in contrast to Dr Rose, Mr Thomas is not relying on hindsight to support his claim as he would have paid his Class 2 NICs if he had known that they were payable (see paragraph 26 above). We found that Mr Thomas’ behaviour with regard to his other tax affairs during the Class 2 NICs liability period supports his claim. Mr Thomas did not receive see or hear the publicity campaigns and he left his tax returns with his accountant.

39. We considered that another relevant factor in this case is the timing of the relevant events. The timing of the reconstruction of the NIC scheme and the introduction of Class 4 contributions coincided with Mr Thomas resuming self-employment. HMRC’s statement that “if it had continued to receive contribution cards from Mr Thomas until 1974-75 then his NI record would have been noted with his self-employed liability when the records were computerised” is one indication of the effect of the specific timing of the events in this case.

40. Another indication of the effect of this timing is that paying two classes of contribution under two collection methods was an “unfamiliar concept” in 1976, much like the introduction of NICs in 1948 as referred to in *Kearney* (at paragraph 52). Mr Thomas was not aware of the different classes of NIC or that paying Class 4 NICs did not contribute to his pension. Mr Thomas therefore expected to pay one class of contribution when he resumed self-employment and, while HMRC’s statement of case refers to Class 4 NICs as “an additional tax on self-employed profits above a certain threshold”, it is a contribution. The difficulties in structure and collection of Class 2 NICs which give entitlement to benefits, as compared to Class 4 NICs, have been commented on in consultation papers over the years, but it was some forty years before the National Insurance Act 2015 provided for the collection of Class 2 NICs under self-assessment with Class 4 NICs. This came too late for Mr Thomas but it is interesting to note that notwithstanding this long period of separate collection, the Financial Secretary to the Treasury (Mr David Gauke) described the policy reason for the change as follows:

“Having two separate collection methods for Class 2 and Class NICs causes confusion...”

41. We found that the fact that Mr Thomas resumed self-employment at the same time as the reconstruction of NICs and introduction of the new Class 4 NICs (to be collected under a separate method from Class 2 NICs) could well have contributed to both his misunderstanding that payment of the new Class 4 NICs was his pension contributions payment and his contribution record falling between the two collection agencies, and these factors reinforced the assumption that he made based on his accountant’s response to his enquiry.

42. Accordingly, on the basis of the specific factors in his case, Mr Thomas has discharged the onus of proof that his ignorance or error was not due to a failure on his part to exercise due care and diligence. In the terms used by Lady Justice Arden in *Kearney*, lack of due care and diligence by Mr Thomas “can be eliminated as a cause of his ignorance” about his liability or need to pay Class 2 NICs.

Decision

43. The appeal is allowed and Mr Thomas is entitled to make late payments of Class 2 NICs that can be carried back and treated as paid in the Class 2 NICs liability period.

44. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to “Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)” which accompanies and forms part of this decision notice.

**VICTORIA NICHOLL
TRIBUNAL JUDGE**

RELEASE DATE: 31 OCTOBER 2016