[2017] UKFTT 0374 (TC)

TC05839

Appeal number: TC/2015/06693

VAT – failure to notify obligation to register – reliance on third party – absence abroad – whether special circumstances – no – whether penalty should be reduced - yes

FIRST-TIER TRIBUNAL
TAX CHAMBER

DANCE WITH MR D LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE ANNE FAIRPO
MR NICHOLAS DEE

Sitting in public at Birmingham on 3 August 2016

Mrs N Preston, Counsel for the Appellant

Mr D Ryder, presenting officer, for the Respondents

DECISION

Introduction

1. This is an appeal against a penalty of £41,666.00 issued by HMRC on 17 November 2014 to the appellant in relation to the appellant's failure to notify HMRC of its compulsory obligation to register for VAT.

2. It is agreed between the parties that the due date for notification was 30 January 2012 and that the date of notification was 13 May 2014.

3. The appeal was made 28 days late but HMRC raised no objection to the late appeal and the matter was allowed to proceed.

4. The question to be resolved is whether the level of the penalty is appropriate and, in particular, whether special circumstances should have been taken into account to reduce the level of the penalty to nil.

Background

5. The appellant carries on a business of theatrical production. In early 2014 it became clear that the business had exceeded the VAT threshold in December 2011 and a form VAT1 was submitted to HMRC on 13 May 2014, requesting VAT registration from the earlier date of 1 December 2011. The application was accepted and the appellant was registered for VAT with effect from 1 December 2011.

6. HMRC subsequently determined that the appellant had exceeded the VAT threshold (then £73,000) on 31 December 2011 so that the compulsory notification date for registration was 30 January 2012 under Schedule 1 Value Added Tax Act ('VATA') 1994.

7. On 2 June 2014, HMRC wrote to the appellant to notify it of a potential liability under Schedule 41 of Finance Act 2008 as a consequence of the failure to notify liability to register for VAT on time. The letter asked for an explanation of the late registration and for confirmation of the net tax liability for the period 1 February 2012 to 12 May 2014.

8. On 18 August 2014, the appellant's representative replied to HMRC's notification letter and advised that it had not been appreciated that the VAT registration threshold had been exceeded because of "the involvement of connected parties in the supplies and receipt of income from overseas". The net tax liability was confirmed to be £347,221.72.

9. On 9 September 2014, HMRC advised the appellant that they intended to charge a penalty, with a calculation of the amount due.

10. On 10 October 2014 the appellant's representative wrote to HMRC, requesting that the penalty be removed and citing *James Hillis* [2013] UKFTT 196 (TC) as authority for the request.

11. On 17 November 2014, HMRC issued a Notice of Penalty Assessment to the appellant ni the amount of £41,666.00.

12. The appellant requested a formal independent review of the matter; the review conclusion of 27 March 2015 upheld the decision to impose a penalty.

13. On 25 June 2015, the appellant appealed to this Tribunal.

Appellant's evidence and submissions

14. The appellant's grounds of appeal state that the reason for the delay is that the appellant "is in the entertainment industry and travels around the globe so he does not have access to snail mail if its arrives in his absence … it is absurd to expect a business to employ someone just to open HMRC's snail mail and forward it when he is the other side of the world. We dispute that [the appellant] did not action this in a timely manner given his circumstances with his work". The grounds of appeal also states that "If the error has arisen due to non-deliberate behaviour and the appellant has made an unprompted disclosure … it is all about action and behaviour and … as soon as he knew about the requirement to be VAT registered action was taken to rectify his tax affairs".

15. The appellant's appeal is therefore made on the basis that special circumstances should apply to reduce the penalty as the appellant acted as soon as it was aware that it should have been registered and there had been no intention to fail to comply with the law.

16. It was confirmed for the appellant that the appeal was not being made on the basis of reasonable excuse, as it was accepted that incorrect advice did not amount to a reasonable excuse. It was noted that, nevertheless, HMRC had – and continued – to focus on the reasonableness of the appellant's case.

17. The appellant relies in this on the decision in the case of *James Hillis* [2013] UKFTT 196 (TC), in which the Tribunal held that special circumstances applied (as provided for in paragraph 14 of Schedule 41 of Finance Act 2008) and justified a special reduction of penalty for late notification to nil. The case related to a solicitor who had, in setting up a new practice, made a genuine mistake in relation to his obligation to register for VAT and so had registered late.

18. The appellant submits that the case is comparable because, as in *James Hillis*, the failure to notify had not been deliberate or concealed. The appellant had made a genuine mistake, relying on information from his accountants at the relevant time. It was only when the appellant changed accountants that he realised that the previous accountants' advice had been incorrect. Having obtained advice from the first accounts, the appellant had no reason to question that advice or otherwise verify it.

Part of the reason for engaging accountants is to eliminate the need to deal with tax issues directly, although it was accepted that the onus remains on the taxpayer to ensure that tax affairs are dealt with. Nevertheless, the policy underlying the penalty regime in Schedule 41 is clearly intended to ensure that the rules are not too rigidly applied.

19. Further, in contrast with *James Hillis*, the appellant in this matter had acted immediately on becoming aware of the liability to be registered. In the case of *James Hillis*, the taxpayer had delayed several months in notifying HMRC after becoming aware of the need to register.

20. The Tribunal in the *James Hillis* case noted that special circumstances should be considered where, inter alia, "the strict application of the penalty law produces a result that is contrary to the clear compliance intention of the law" and that "the penalty regime under schedule 41 is primarily aimed at tax payers who deliberately avoid their responsibilities to notify HMRC of their obligation to pay tax [and not] …for tax payers who make a genuine mistake on their liability and disclose their mistake to HMRC".

21. Accordingly, it was submitted that the penalty should be reduced to nil on the basis of special circumstances, in accordance with the decision in *James Hillis*, as the appellant had made a genuine mistake and had disclosed the mistake to HMRC. HMRC's refusal to accept that special circumstances apply in this case ignores the intention behind the penalty regime.

22. It was noted that HMRC dispute the application of the *James Hillis* case to this matter on the basis that the delay here was longer, and that the amount of tax was greater.

23. It was submitted that both points are flawed: firstly, although the delay in this case was longer than in the *James Hillis* case, the appellant had acted as soon as it became aware of the failure to notify. In contrast, in the *James Hillis* case, the taxpayer had delayed further after becoming aware of the failure, although the overall delay was shorter.

24. Secondly, the amount of tax involved is not relevant to the question of whether special circumstances apply. The penalties are not charged on a sliding scale as to how much is due. It was noted that Schedule 41 allows a reduction in penalty to 10% where an unprompted disclosure is made and the delay is over 12 months but provides no sliding scale. Given that the appellant had engaged accountants, the level of turnover would not have made him any more aware that there could be a liability to register for VAT where the accountants had not informed him. Further, given the complexities of connected parties and overseas income, it was not straightforward to determine the VAT position. A focus on the turnover alone gives too narrow a view of the position.

25. Accordingly, it was submitted that the question to be considered is whether the appellant had special circumstances, not whether there was a reasonable excuse. The

appellant's business circumstances, involving significant overseas activity and income, and dealings with inter-related companies, and the fast expansion of the business meant that he had to rely on his accountancy advice. It was noted that HMRC had not rejected the explanations given by the appellant for the delay in notification. Therefore it was submitted that this was a genuine mistake in line with *James Hillis* regardless of the amount at stake, and that the penalty should be eliminated as special circumstances applied.

26. In the alternative, it was submitted that the penalty reduction should be increased to 90%. HMRC had not given full discounts for "telling" and "helping" as they had had to send a reminder letter.

27. For the appellant, it was explained that one letter from HMRC dated 2 June 2014 had not been received, but the appellant's representative had contacted HMRC as soon as they received the subsequent letter dated 23 July 2014. As the appellant is a "one man band" there is no one to deal with post if he is not available and so some delay also arises there.

28. It was submitted that, as HMRC had accepted the explanation for the delay in replying, a greater discount to the penalty should be given if the Tribunal does not find that the penalty should be reduced to nil given the application of special circumstances.

HMRC evidence and submissions

29. For HMRC, it was noted and accepted that the onus of proof is on HMRC to establish that the penalty charged has been applied correctly. It was agreed that the standard of proof is the ordinary civil standard of the balance of probabilities.

30. HMRC submitted that the onus is, however, on the taxpayer to be aware of potential tax liabilities at all times and to ensure that they do the necessary research to ensure compliance with the VAT regime. In this case, the appellant has not provided any evidence that they made reasonable efforts to confirm whether they should have been registered or to confirm the Vat liability of their supplies.

31. It was noted that the appellant is, as previously described, a "one man band" and travels extensively and so it would have been expected that the appellant would have had made provision to deal with correspondence in his absence. It was remarkable that no such processes were in place.

32. HMRC noted that the notification for registration in this case was made two years and four months late; the turnover during the period of default was almost £2.2 million, an average annual turnover of approximately £960,000 more than ten times the registration threshold. It was submitted that it was remarkable that the liability to register was unnoticed for such a length of time.

33. HMRC submits that the case of *James Hillis* is not binding on this Tribunal as the decision is one of the First Tier, and so is not binding on other Tribunals including this one. This case therefore needs to be considered on its own facts and merits.

34. It was submitted that the facts in this case are very different to those in the *James Hillis* case. In particular, firstly, the delay in notification in *James Hillis* was only one month outside the twelve month threshold for consideration of a nil penalty and within the "margin of appreciation" as described by the Tribunal. In this matter, the delay in notification was twenty-eight months.

35. Secondly, the potential lost revenue in the *James Hillis* case was substantially lower than that involved in this case. The level of turnover in this case was such that it should have been clear to the appellant that VAT registration was required earlier.

36. It was submitted that the appellant has not demonstrated that any special circumstances apply. The overseas nature of the business and the involvement of related parties is not unique to the appellant, and no details have been provided to explain why there is anything special in respect of the circumstances in this case.

37. It was submitted that no grounds have been identified that would warrant further reduction or elimination of the penalty. Accordingly, the appeal should be dismissed.

Relevant law

38. Schedule 41 of the Finance Act 2008 provides a penalty regime for failures to comply with obligations to notify liability in respect of various taxes, including notification of liability to register for VAT.

39. Paragraph 6 of Schedule 41 sets outs the penalties for failures to notify. These depend upon the degrees of culpability defined in paragraph 5. For a failure to notify liability for VAT registration the penalties are:

> (1) 100 per cent of the potential lost revenue for a deliberate and concealed act or failure.
>
> (2) 70 per cent of the potential lost revenue for a deliberate but not concealed act or failure.
>
> (3) 30 per cent of the potential lost revenue for any other case.

40. Paragraphs 12 and 13 of Schedule 41 provide for reduction of the penalty where the tax payer discloses a relevant act or failure. Paragraph 12 distinguishes between unprompted and prompted disclosures.

41. Paragraphs 13(3)(a) and 13(3)(b) give a discretion to reduce the 30 per cent penalty for any other case (in paragraph 6(3)) to a specified minimum depending on the type of disclosure. Where HMRC becomes aware of the failure to notify VAT registration less than 12 months after when the tax first becomes unpaid by reason of the failure, the specified minimum is ten per cent for prompted disclosure and nil per

cent for unprompted disclosure. Where HMRC becomes aware of the failure 12 months or after when the tax first becomes unpaid the specified minimum is increased to 20 per cent for prompted disclosure and 10 per cent for unprompted disclosure.

42. Paragraph 14 of schedule 41 enables HMRC to reduce a penalty generally if HMRC thinks it right because of special circumstances. Paragraph 14(2) states that special circumstances do not include ability to pay or the fact that a potential loss of revenue from one tax payer is balanced by a potential over payment by another.

43. Paragraph 19(2) permits the Tribunal on an appeal against the amount of a penalty to affirm HMRC's decision or substitute for HMRC's decision another decision that HMRC had power to make. In respect of the substitution the Tribunal may rely on special circumstances but only if the Tribunal thinks that HMRC's decision on the application of special circumstances is flawed. Paragraph 19(4) defines flawed as flawed when considered in the light of the principles applicable in proceedings for judicial review.

Decision

44. We note that it is agreed that the appellant's failure to register for VAT was non-deliberate and the disclosure was unprompted.

45. The penalty for an unprompted disclosure made more than twelve months after the tax became due is 30%, which may be reduced by the quality of disclosure to no less than 10%. In this case, the penalty was reduced by HMRC to 12%.

46. The question being considered, therefore, is whether special circumstances or a reasonable excuse apply to justify a reduction in the penalty. The appellant has not argued that any reasonable excuse applies, and the grounds of appeal are that a genuine mistake was made. As it is well-established that a mistake alone is not sufficient grounds for reasonable excuse, the only issue remaining is whether there were special circumstances which justify a reduction in the penalty.

47. Schedule 41 of Finance Act 2008 does not define "special circumstances", although it does state that ability to pay and the fact that a potential loss of revenue from one person is balanced by a potential overpayment to another cannot amount to special circumstances. Neither is in point here.

48. As noted in *James Hillis* (at 23), "HMRC's policy defines special circumstances as either uncommon or exceptional or where the strict application of the penalty law produces a result that is contrary to the clear compliance intention of the law. The Tribunal in *Collis v HMRC* [2011] UKFTT 588 (TC) ruled that the circumstance in question must operate on the particular individual, and not be a mere general circumstance that applies to many taxpayers by virtue of the scheme of the provisions themselves".

49. We note the decision in *James Hillis* but also note that the decision is not binding on this Tribunal; indeed, as stated in *James Hillis* (at 24) the question must be considered with regard to the appellant's individual circumstances.

50. We consider that the essence of the appellant's case is that special circumstances should be considered to apply because his business involves overseas activities and income, and involves related parties and so he had to rely upon his original accountants' advice as to whether he should be registered for VAT.

51. We consider that in the time period involved there is no automatic unusual complexity in a business which as overseas activities and income, and involves related parties. No evidence was presented to us to explain why the appellant's business had particular difficulties with regard to identifying its VAT liability that would not have applied to other taxpayers in a similar position.

52. In the absence of any such evidence, we do not consider that the nature of the appellant's business amounts to special circumstances. All that remains of the contention therefore is reliance on a third party, the original accountants. It is well-established that reliance on a third party cannot amount to a reasonable excuse; we consider therefore that it cannot amount to special circumstances either as that would render redundant the principle in respect of reasonable excuse.

53. Accordingly, we find that there are no "uncommon or exceptional" circumstances which amount to special circumstances.

54. We have also considered the alternative, that "the strict application of the penalty law produces a result that is contrary to the clear compliance intention of the law". In this case, the delay in notifying HMRC was twenty-eight months, and the level of turnover was almost ten times the level of the VAT registration threshold. In the circumstances, we consider that this is not a marginal failure to realise that VAT registration applied.

55. Whilst there is a compliance intention to the law, we consider that the law is not intended only to discourage deliberate non-compliance but is also intended to discourage a relaxed approach to compliance. A taxpayer cannot escape a penalty through special circumstances simply because they did not deliberately intend to fail to notify registration; if that was the case, there would be no policy reason for the legislation to set a minimum penalty for an unprompted disclosure of liability which is made more than twelve months late. As there is such a minimum penalty, we consider that it must be the case that, for special circumstances to apply, those circumstances must involve something more than a non-deliberate failure to notify particularly where the delay is more than twelve months.

56. We therefore find that the fact that the appellant did not intend to deliberately fail to notify his liability does not mean that the penalty law produces a result that is contrary to the clear compliance intention of the law. As such, the appellant's lack of deliberate intention does not amount to special circumstances. As we have already found that the nature of the appellant's business and his reliance on his original

accountants do not amount to special circumstances, we find therefore that there are no special circumstances which apply to reduce the penalty in this case.

57. Turning therefore to the amount of the penalty, we note that HMRC gave only a 25% reduction for "Telling", rather than the full 30% reduction possible. The reason for this was stated to be delays in correspondence, but HMRC have also accepted the appellant's explanation for the delay in correspondence.

58. On that basis, and in exercise of our powers under paragraph 19(2) of Schedule 41, Finance Act 2008, we find that the reduction for "Telling" should be increased to 30% from 25%.

59. We do not consider that the reduction for "Helping" should be increased further, however, as we consider that the appellant failed to make proper provision for correspondence in his absence, particularly once correspondence with HMRC on these matters had begun.

60. Accordingly, we find that the penalty reduction should be 95%. When applied to the difference between the maximum penalty rate of 30% and the minimum penalty rate of 10%, that gives a revised penalty rate of 11% in place of the 12% calculated by HMRC.

61. The Tribunal therefore dismisses the appeal as to special circumstances but substitutes the penalty of £41,666.00 with a penalty of £38,194.

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

ANNE FAIRPO

TRIBUNAL JUDGE
RELEASE DATE: 4 MAY 2017