TC02721

Appeal number: TC/2012/09157

VAT – penalty for failure to register – Schedule 41 Finance Act 2008 – whether reasonable excuse or breach of human rights – no – whether penalty qualified for mitigation down to 0% under paragraph 13(5)(a) – meaning of "time when tax first becomes unpaid by reason of the failure" – whether disclosure made within 12 months of that date – whether relevant date was first day of compulsory registration period or date on which first payment of VAT would have been made – held the latter – penalty therefore qualified for potential mitigation to 0% – HMRC had already accepted quality of disclosure merited 100% mitigation within available range – in view of quality of disclosure, penalty should be reduced to nil – appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

TASTE OF THAI LIMITED **Appellant**

-and-

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

TRIBUNAL: **JUDGE KEVIN POOLE**
PAUL ADAMS FCA

Sitting in public in Vintry House, Wine Street, Bristol on 15 March 2013

Robin Carey FCA for the Appellant

Les Bingham, Presenting Officer of HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This appeal concerns a penalty of £904 imposed under schedule 41 Finance Act 2008 ("FA 08") for failure to notify liability to register for VAT.

2. The novel point it considers is "when tax first becomes unpaid by reason of the failure" to notify liability for VAT registration. HMRC argued it was on the date from which the taxpayer was obliged to be registered (in which case the Appellant's unprompted notification of its non-deliberate failure to notify its liability to VAT registration was made more than 12 months later, resulting in a minimum 10% penalty); the Appellant argued it was the date on which it would have first been obliged to pay VAT if it had been duly registered (in which case such notification was made less than 12 months after such date, resulting in a minimum 0% penalty).

3. HMRC accepted that the failure to notify was not deliberate, and that the Appellant had made an unprompted disclosure of it. They took the view that the quality of the Appellant's disclosure justified the maximum mitigation and accordingly they mitigated the penalty down to 10% of the "potential lost revenue" (which they regarded as the minimum penalty permitted as a result of the timing of the disclosure).

4. The Appellant initially appealed on the grounds that it had tried to be compliant but had failed to register for VAT at the correct time due to a simple arithmetical error in calculating its rolling annual turnover figure; if HMRC had made available on their website the automated checking spreadsheet which they used internally then the error would not have been made. In effect, this was a "reasonable excuse" argument.

5. The Tribunal considered there was doubt about whether the error was notified to HMRC within 12 months after tax first became unpaid by reason of the failure to notify, and invited further submissions from the parties on this point following the hearing. The Appellant took that opportunity to argue also that HMRC's failure to make available on their website the relevant software was also discriminatory, in that it discriminated against taxpayers who did not have the necessary skills to create a similar software tool for themselves.

The facts

6. The Appellant carried on business as a restaurant in Gloucester. It had previously been registered for VAT from 3 April 2006 to 5 August 2008. That registration had been cancelled on the grounds that the Appellant's turnover had fallen below the relevant threshold.

7. In April 2011 the Appellant gave its records for the year ended 31 March 2011 to its accountant (Mr Carey) for the purposes of drawing up its annual accounts. Mr Carey started work on the records and on 19 October 2011 he came to the conclusion that the Appellant had exceeded the VAT registration threshold in March 2011, thus

prima facie becoming liable for registration from 1 May 2011 under paragraph 1(1)(a) Schedule 1 Value Added Tax Act 1994 ("VATA 94").

8. Mr Carey sought further turnover information from the Appellant for the period commencing 1 April 2011, with a view to ascertaining whether an exception to compulsory registration could be justified under paragraph 1(3) Schedule 1 VATA 94. Having obtained turnover figures from the Appellant up to 13 November 2011, he wrote to HMRC on 17 November 2011 (received by HMRC on 18 November 2011), giving them the weekly turnover figures from 1 April 2010 to 13 November 2011, informing them of the failure to register but pointing out that it was the Appellant's intention to close for three weeks in January 2012 if necessary in order to ensure that its turnover for the year ended 31 March 2012 would fall below the de-registration threshold. He thus hoped to obtain an exemption from compulsory registration from 1 May 2011.

9. On 29 November 2011 HMRC wrote back, asking for (amongst other things) the 36 months' turnover figures prior to March 2011 so they could verify the Appellant's position.

10. On 5 December 2011, Mr Carey faxed the monthly turnover figures for the relevant period to HMRC. They inputted the figures into their own spreadsheet and established that in fact the rolling turnover threshold for compulsory VAT registration had been exceeded in September 2010, thus rendering the Appellant liable to compulsory VAT registration from 1 November 2010. The turnover figures for the year commencing on that date were slightly above the de-registration threshold and therefore there was no question of an exception to compulsory registration under paragraph 1(3) Schedule 1 VATA 94. These facts are not disputed by the Appellant.

11. In a letter dated 12 December 2011, HMRC indicated they were not in a position to grant a retrospective exemption from the obligation to register with effect from 1 November 2010. This was because they were "unable to accept that at the appropriate time they could have been satisfied that the value of your taxable supplies in the period of one year then beginning would not exceed £68,000".

12. HMRC therefore required the Appellant to register for VAT with effect from 1 November 2010 (which it duly did) and make a return accounting for VAT on its turnover since that time. They issued the VAT registration on 16 December 2011 and required the Appellant to deliver a return for the extended period from 1 November 2010 to 29 February 2012.

13. On 13 February 2012, Mr Carey submitted an application for de-registration on behalf of the Appellant. HMRC initially refused the application on the grounds that no return had been submitted or other turnover figures supplied and they were therefore unable to satisfy themselves that the Appellant was indeed trading below the de-registration threshold. Mr Carey wrote again on 7 March 2012 with updated turnover figures, showing the Appellant had fallen below the de-registration threshold in January 2012. HMRC cancelled the Appellant's VAT registration with effect from 14 March 2012.

14. HMRC then considered the question of penalties for late notification of liability to register. They wrote to the Appellant on 23 March 2012 warning it of prospective penalties, sending it relevant fact sheets and asking for a note of the net tax liability for the period 1 November 2010 to 15 December 2011. They were informed that the relevant figure was £9,661.

15. On 27 April 2012 HMRC sent a "pre-decision letter" to the Appellant, warning it of the penalty they intended to charge and setting out their reasoning and calculations.

16. In that letter, they accepted that the omission to notify liability to VAT registration was "non-deliberate" and that the disclosure of that omission was "unprompted", but they stated their view that the disclosure was made "more than 12 months after the tax becomes unpaid" and therefore the penalty range was between 10% and 30% of the "potential lost revenue".

17. They also accepted that the quality of the disclosure allowed for the full 100% mitigation within this range, thus resulting in a final penalty of £966, being 10% of the potential lost revenue. They issued a notice of penalty assessment in that amount dated 12 June 2012.

18. There was a subsequent amendment to the penalty, when HMRC agreed that the calculation of the "potential lost revenue" should only cover the period up to 17 November 2011 (when the original notification was first sent to them) rather than 15 December 2011 (the day before the effective date of registration). This resulted in a small agreed reduction in the potential lost revenue from £9,661 to £9,045 and a consequent reduction in the penalty from £966 to £904. HMRC issued an amended pre-decision letter on 11 July 2012 and an amended notice of penalty assessment on 8 August 2012. This is the penalty which is currently under appeal.

19. None of the calculations are in dispute between the parties, save as to the percentage mitigation allowable in calculating the penalty.

The law

20. There is no dispute as to the effect of the provisions of Schedule 1 VATA 94 concerning the obligation to register, so we do not set those provisions out in full.

21. At the relevant time, the relevant provisions of Schedule 41 FA 08 were as set out in the Appendix to this decision.

Submissions of the parties

Submissions on reasonable excuse and Human Rights Act

22. Mr Carey argued that it was unreasonable of HMRC to keep to themselves the means of easily testing for compliance with the turnover thresholds. He contrasted their apparent secretiveness in this regard with their other well-used tools available on their website, such as the normal online self-assessment tax return.

23. We see nothing in this submission, even when supported by Mr Carey's later assertion that it was in some way discriminatory of HMRC to act in this way. The responsibility lies on the taxpayer to monitor his own compliance with the turnover thresholds and the rules are not unduly complicated or difficult to understand. When a taxpayer is effectively flirting knowingly with the limit on an ongoing basis, he should be even more alert to ensure that he does not exceed it and it will be difficult for him to establish that he has a reasonable excuse for having failed to monitor his turnover and act appropriately when it exceeded the threshold. We do not consider that Mr Carey's arithmetical error can afford the Appellant a reasonable excuse in the circumstances of this case, the Appellant having taken no steps itself of which we were informed to ensure that it did not exceed the turnover threshold.

24. Mr Carey also made a vague and unsubstantiated allegation that HMRC had failed to comply with the appropriate procedures under the Human Rights Act before imposing the penalties. We see nothing in the procedure they followed which could properly be criticised in this way.

Submissions on potential availability of 0% penalty rate

25. At the hearing, the Tribunal asked the parties to address the question of whether it could be said that HMRC had, in terms of paragraph 13(5)(a) of Schedule 41 FA 08:

> "become aware of the failure less than 12 months after the time when tax first becomes unpaid by reason of the failure"

26. The background to this request was as follows:

(1) The parties were agreed that the Appellant had passed the rolling twelve month turnover threshold for compulsory VAT registration during September 2010.

(2) It therefore became liable to compulsory VAT registration at the end of September 2010 under paragraph 1(1)(a) Schedule 1 VATA 94 and it was required, under paragraph 5(1) Schedule 1 VATA 94, to notify HMRC no later than 30 October 2010 of its liability to registration.

(3) It was the Appellant's failure to give such notification until 18 November 2011 that had triggered the penalty under appeal.

(4) When considering what minimum penalty should apply to such failure, the question to consider was whether HMRC had "become aware of the failure less than 12 months after the time when tax first becomes unpaid by reason of the failure". If they had become aware of that failure within the 12 month period in question, then a 0% penalty was potentially available, subject to the quality of the disclosure.

(5) If the Appellant had notified its liability to registration on time, HMRC would then have been required under paragraph 5(2) Schedule 1 VATA 94 to

register the Appellant for VAT with effect from 1 November 2010 (as, indeed, they subsequently did) unless an earlier date was agreed between the parties.

(6) The earliest time at which the Appellant would have been liable to pay any VAT following such registration would have been 31 December 2010 (if HMRC had registered the Appellant for VAT with accounting periods ending at the end of February, May, August and November in each year).

(7) Given that HMRC have accepted that they became aware of the Appellant's failure to register on 18 November 2011, when they received Mr Carey's first letter, it appeared to the Tribunal to be arguable that the Appellant would potentially qualify for a 0% minimum penalty by reason of paragraph 13(5)(a) of Schedule 41 FA 08.

27. We gave the parties the opportunity to produce written submissions after the hearing on the point.

28. The submissions received from Mr Carey on behalf of the Appellant added nothing new to the analysis, simply observing that if HMRC had applied a normal three month accounting period, the first return would have been made in respect of the period 1 November 2010 to 31 January 2011, the return would have been due by 28 February 2011 and payment could have been made up to 7 March 2011. Thus, he submitted, the disclosure was made to HMRC well under twelve months after tax first became unpaid by reason of the failure and a 0% penalty should be available.

29. It is worth setting out Mr Bingham's submissions in full:

> "1. It is the Respondents' contention that the tax first becomes unpaid on the first day of the period over which the potential lost revenue is calculated. In making this contention the Respondents would refer the Tribunal to Paragraph 6 *[note: should be 7(6)]* of Schedule 41 FA2008 which states:
>
> "In the case of any other relevant obligation relating to value added tax, the potential lost revenue is the amount of value added tax (if any) for which P is, or but for any exemption from registration would be, liable for the relevant period (see sub-paragraph (7)) but subject to sub-paragraph (8)."
>
> The 'relevant period' as far as this appeal is concerned is defined at paragraph (7)(b) of Schedule 41 FA2008 as:
>
> "in relation to a failure to comply with an obligation under any other provision, the period beginning on the date with effect from which P is required in accordance with that provision to be registered and ending on the date on which HMRC received notification of, or otherwise became fully aware of, P's liability to be registered."
>
> In this case the Respondents therefore contend that the tax first becomes unpaid by virtue of the failure on the first day of the period over which

the potential lost revenue is calculated i.e. 1 November 2010. As the Appellant first contacted the Respondents on 17 November 2011 the minimum penalty by virtue of paragraph 13(5) of Schedule 41 FA2008 is 10%.

2. The Tribunal's analysis of paragraph 13(5) of Schedule 41 FA2008 is misplaced in that it would frustrate Parliament's intention that only those persons who, within 12 months of failing to notify that they should be registered for VAT (in this case), come forward unprompted and tell HMRC about their (non-deliberate) failure should have 0% penalty as a possibility. The logical conclusion of the Tribunal's analysis is that all unprompted (non-deliberate) disclosures would have a 0% penalty available to them.

3. The Tribunal appears to be of the view that the debt to the Respondents is established and due either through an assessment or by the rendering of a return when interpreting the term 'unpaid' in relation to paragraph 13(5) of Schedule 41 FA2008. However, the Respondents would refer the Tribunal to Section1(2) of the Value Added Tax Act 1994 (VATA 1994) which says that "*VAT on any supply of goods or services is a liability of the person making the supply and (subject to provisions about accounting and payment) becomes due at the time of supply.*" The VAT charged on a supply made under Section 1(2) of the VATA 1994 will therefore always be unpaid until it is paid either through payment of an assessment, return or other formal demand. The tax unpaid under paragraph 13(5) of Schedule 41 FA2008 must therefore be the amount of tax due from the Appellant from their effective date of registration.

4. Paragraph 1 Schedule 41 FA2008 provides for failures to meet obligations to notify HRMC. Penalties for failure to render and pay tax returns lie elsewhere – these failures are not pivotal to an analysis of Paragraph 1 Schedule 41 FA2008. Penalties under Schedule 41 FA2008 are calculated as a percentage of the potential lost revenue which is the amount that is liable to be paid and not the amount that is unpaid."

30. With reference to paragraph 1 of the submissions, we have the following comments. We are unable to discern any logical link between the contention stated at the outset of it and the statutory provisions which are said to support that contention. We fully accept that the "potential lost revenue" includes all VAT ultimately becoming due in respect of the period starting with the date with effect from which the taxpayer is required to be registered. However we do not see how this should satisfy us that "tax first becomes unpaid" on the effective registration date.

31. With reference to paragraph 2 of the submissions, we regard it as essentially flawed in that it asserts that Parliament's intention was that the twelve month period should start from the date of failure to notify and says that any other interpretation is "misplaced". The only basis which is given for the assertion appears to be that the alternative suggestion put forward is absurd because, taken to its logical conclusion, it would make a 0% penalty available to all unprompted non-deliberate disclosures

(whenever made). If this were the logical conclusion of the alternative suggestion, we might have some sympathy with the argument. But we do not consider that it is. For example, in the present case on our analysis, if the Appellant had notified its liability to registration after mid-March 2012, it would certainly have lost the opportunity of a 0% penalty.

32. With reference to paragraph 3 of the submissions, we consider it addresses the wrong question. Paragraph 13(5) of Schedule 41 FA 08 is not concerned with when a VAT debt is "established and due", it is concerned with "the time when tax first becomes unpaid by reason of the failure". That is the phrase which we must interpret, and we take it at face value (see [41] to [43] below).

33. The argument in paragraph 3 of the submissions appears to be based on section 1(2) VATA 94. The reference in that sub-section to the date of supply being the date on which tax "becomes due" is clearly and expressly made subject to the provisions about accounting and payment and does nothing, in our view, to demonstrate that tax "becomes unpaid" on any particular date. It is of course quite possible, for example, that no tax will ever become payable by reference to a particular standard rated supply, due to the availability of input tax to set against the output tax liability. And of course Mr Bingham's submission, if it is to be applied properly, requires an investigation to be made as to the first date on or after 1 November 2010 when the Appellant actually made taxable supplies, rather than assuming (as he tacitly does) that it did so on that date.

34. Finally, whilst we do not disagree with the statement contained in paragraph 4 of the submissions, we do not see its relevance. We fully accept that under Schedule 41 FA 08, penalties are payable by reference to potential lost revenue rather than any "amount that is unpaid". But there is no dispute about the level of potential lost revenue in this case, all we are concerned with is whether the disclosure was made early enough to qualify for a potential 0% penalty rate.

Discussion and conclusion

35. We have reached the conclusion, without difficulty, that the Appellant had no reasonable excuse for its failure to notify its liability to registration and that the procedure followed by HMRC is unimpeachable on Human Rights grounds (see [23] and [24] above).

36. We were however not persuaded by Mr Bingham's submissions on Paragraph 13(5)(a) of Schedule 41 FA 08. Our views on that provision are as follows.

37. Paragraph 13(5)(a) of Schedule 41 FA 08 effectively requires us to identify two dates:

(1) the date when tax first became unpaid by reason of the Appellant's failure ("Date 1"); and

(2) the date when HMRC became aware of the Appellant's failure to notify its liability to register for VAT ("Date 2").

38. If Date 2 is less than twelve months after Date 1, then a 0% penalty is potentially available for an unprompted disclosure of adequate quality if the failure was not deliberate.

39. In the present case, Date 2 was 18 November 2011 (though HMRC appeared ready to accept that it was 17 November 2011).

40. Therefore if Date 1 was after 19 (or possibly 18) November 2010, a 0% penalty would potentially be available.

41. We are not persuaded by Mr Bingham's submissions as to the correct way of identifying Date 1. It would have been a very simple matter, if Parliament had intended Date 1 to be (as Mr Bingham contends) the effective date of compulsory registration, for it to say so. It would have been even simpler for it to have designated the day by which the taxpayer should have notified his liability to register. But it did neither. It chose to designate "the time when tax first becomes unpaid by reason of the failure" and we see no reason not to take these words at face value.

42. There is logic to this. If, for example, a taxpayer is obliged to register for VAT but is in a repayment situation for say his first six or nine months, Parliament has decided that he should not be deprived of the opportunity of a 0% non-notification penalty until, broadly, 12 months after he becomes a "payment" trader. There is a link between the twelve month period starting to run and the start of the potential loss to the public purse.

43. We consider the correct approach to identifying Date 1 is first to identify the failure. Here, it is the failure to notify liability to compulsory VAT registration. The next step is to identify when tax first became unpaid by reason of that failure. That should be done by identifying what would have happened if the failure had not taken place, and when the first payment of VAT would have been due.

44. In the present case, if the Appellant had notified its liability at the right time, it would have been registered in the normal way for VAT in late 2010.

45. It may well be that the Appellant would have been registered with a first VAT accounting period from 1 November 2010 to 31 January 2011 (with a resulting obligation to pay VAT by 28 February 2011 or, in case of electronic payment, by 7 March 2011). However, there was no evidence before us of the VAT accounting period that would have been allocated to the Appellant by HMRC, so we need to consider all the possibilities. Even if it had been registered with the shortest possible first VAT accounting period (from 1 to 30 November 2010), the earliest it would have been obliged to pay VAT was 31 December 2010 (or 7 January 2011 in case of electronic payment).

46. Thus, the "worst case" for the Appellant would have been that it would have been obliged to make its first payment of VAT by 31 December 2010. We consider therefore that Date 1 for this Appellant in this case would not have been earlier than 31 December 2010.

47. Since Date 2 is 17 or 18 November 2011 and Date 1 is no earlier than 31 December 2010, it follows that the period of time between them must be less than 12 months and therefore the Appellant's situation falls within Paragraph 13(5)(a) FA 08. As such, the range of potential penalty falls in the 0% to 30% range of potential lost revenue.

48. In the circumstances, we see no reason to interfere with HMRC's view that the quality of the disclosure merited a 100% mitigation within the available range.

49. We therefore cancel HMRC's decision to impose a penalty. The appeal is allowed.

50. We should mention that if the disclosure had been made later (e.g. in January 2012), we would have required evidence as to the length of the first VAT accounting period which would have been allocated to the Appellant on registration, in order to clarify the actual first due payment date of VAT. We understand HMRC follow a general policy in allocating accounting periods to traders on registration, and evidence of that policy would normally be required. This was not necessary in this case only because the disclosure was made within twelve months even in the worst possible scenario from the Appellant's point of view.

51. 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.

KEVIN POOLE
TRIBUNAL JUDGE

RELEASE DATE: 22 May 2013

APPENDIX

Relevant extracts from Schedule 41 Finance Act 2008

(as applying in respect of tax periods commencing on or before 5 April 2011 or other relevant obligations arising on or before that date)

"**1** A penalty is payable by a person (P) where P fails to comply with an obligation specified in the Table below (a "relevant obligation").

Tax to which obligation relates	Obligation
…..	…..
Value added tax	Obligations under paragraphs 5 …. of Schedule 1 to VATA 1994 (obligations to notify liability to register ….)

….

6 (1) The penalty payable under any of paragraphs 1…. is –

(a) for a deliberate and concealed act or failure, 100% of the potential lost revenue,

(b) for a deliberate but not concealed act or failure, 70% of the potential lost revenue, and

(c) for any other case, 30% of the potential lost revenue.

(2) ….

(3) Paragraphs 7 to 11 define "the potential lost revenue".

….

7 (1) "The potential lost revenue" in respect of a failure to comply with a relevant obligation is as follows.

….

(6) In the case of any other relevant obligation relating to value added tax, the potential lost revenue is the amount of the value added tax (if any) for which P is, or but for any exemption from registration would be, liable for the relevant period (see sub-paragraph (7))…

(7) "The relevant period" is –

(a) ….

(b) in relation to a failure to comply with an obligation under any other provision, the period beginning on the date with effect from which P is required in accordance with that provision to be registered and ending on the date on which HMRC received notification of, or otherwise became fully aware of, P's liability to be registered.

….

12 (1) Paragraph 13 provides for reductions in penalties under paragraphs 1 to 4 where P discloses a relevant act or failure.

(2) P discloses a relevant act or failure by –

(a) telling HMRC about it,

(b) giving HMRC reasonable help in quantifying the tax unpaid by reason of it, and

(c) allowing HMRC access to records for the purpose of checking how much tax is so unpaid.

(3) Disclosure of a relevant act or failure –

(a) 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 relevant act or failure, and

(b) otherwise, is "prompted".

(4) In relation to disclosure, "quality" includes timing, nature and extent.

13 (1) ….

….

(5) Where a person who would otherwise be liable to a 30% penalty has made an unprompted disclosure, HMRC shall reduce the 30% –

(a) if the penalty is under paragraph 1 and HMRC become aware of the failure less than 12 months after the time when tax first becomes unpaid by reason of the failure, to a percentage (which may be 0%), or

(b) in any other case, to a percentage not below 10%,

which reflects the quality of the disclosure.

….

17 (1) P may appeal against a decision of HMRC that a penalty is payable by P.

(2) P may appeal against a decision of HMRC as to the amount of a penalty payable by P.

….

19 (1) On an appeal under paragraph 17(1) the tribunal may affirm or cancel HMRC's decision.

(2) On an appeal under paragraph 17(2) the tribunal may –

(a) affirm HMRC's decision, or

(b) substitute for HMRC's decision another decision that HMRC had power to make.

….

20 (1) Liability to a penalty under any of paragraphs 1…. does not arise in relation to an act or failure which is not deliberate if P satisfies HMRC or (on an appeal notified to the tribunal) the tribunal that there is a reasonable excuse for the act or failure.

(2) For the purposes of sub-paragraph (1) –

(a) an insufficiency of funds is not a reasonable excuse unless attributable to events outside P's control,

(b) where P relies on any other person to do anything, that is not a reasonable excuse unless P took reasonable care to avoid the relevant act or failure, and

(c) where P had a reasonable excuse for the relevant act or failure but the excuse has ceased, P is to be treated as having continued to have the excuse if the relevant act or failure is remedied without unreasonable delay after the excuse ceased.

….

21 (1) In paragraph 1 the reference to a failure by P includes a failure by a person who acts on P's behalf; but P is not liable to a penalty in respect of any failure by P's agent where P satisfies HMRC or (on an appeal notified to the tribunal) the tribunal that P took reasonable care to avoid the failure."