[2016] UKFTT 385 (TC)

TC05139

Appeal number: TC/2015/06231

INCOME TAX –PAYE – new employee- no P45- employer used tax code from old employment – error in tax code-tax under deducted-Regulation 80 determination-whether employer liable-whether operated PAYE correctly-whether employee should pay tax.

FIRST-TIER TRIBUNAL
TAX CHAMBER

THE ATHENAEUM CLUB LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE MARILYN MCKEEVER
MR RICHARD LAW

Sitting in public at Fox Court, London on 4 May 2016

Mrs M Jones, a director of the Appellant for the Appellant

Ms Hellie Lai, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. *Introduction*

2. This case concerns an appeal against a determination under Regulation 80 of the Income Tax (Pay As You Earn) Regulations 2003 ("the Regulations") for the tax year 2011-12. The determination required the Appellant to pay £2,525.80 income tax under-deducted from the salary of Mr Shadbolt, a former employee of the Appellant.

3. *The facts*

4. The Athenaeum Club Ltd ("the Club") is a member's club in Essex with 700 members. The Club has 20 to 25 employees.

5. On 12 September 2011, Mr Shadbolt commenced employment at the Club. When he began his employment, he failed to produce a P45 but said that his previous employer would provide one before the end of September. This did not materialise, but Mr Shadbolt did produce a form P11 which set out his PAYE position for the tax year up to 19 August 2011 and a payslip from his previous employer. These documents showed Mr Shadbolt's tax code as "W1747L". Mrs Jones, a director of the Appellant, who dealt with matters at the time and gave evidence at the hearing, said that, in the absence of the P45, she telephoned the previous employer, who confirmed that they had been operating the tax code W1747L in relation to Mr Shadbolt's salary. They also informed Mrs Jones that they had been using the code for two years without query from HMRC. The correct code was, in fact, 474L Week 1, but the way it was printed on the P11 misled Mrs Jones. The code 1474L produces a much higher weekly tax free amount than the correct code.

6. Mrs Jones used the code 1747L in September which resulted in a repayment to Mr Shadbolt.

7. She wrote to HMRC to check if the code was correct, but received no response. She also attempted to telephone the HMRC helpline on numerous occasions between September and December. On each occasion, she heard a recorded message informing her that the helpline was experiencing a very high volume of calls and inviting her to call back later. She never actually got to speak to anyone at HMRC.

8. The Appellant continued to use the same code for the next couple of months but in December, asked Mr Shadbolt to complete form P46 "Employee without a Form P45". Mr Shadbolt returned the completed form after Christmas in January 2012 and it was duly sent to HMRC. Part 1 of the P46 is to be completed by the employee and the employee must tick one of three boxes setting out his current circumstances. Mr Shadbolt ticked Box C which stated "I have another job or receive a state or occupational pension". Part 2 of the form must be completed by the employer. The form states that employers must normally file employee starter information online and gives the appropriate web address. It also states where online guidance may be found.

9. The bottom part of the form is headed "Tax Code Used" and requires the employer to mark "X" in the appropriate box. There are three boxes corresponding to the three boxes on the employee's side of the form and a further section where the actual tax code used may be inserted. The instructions at Box C state "Code BR unless the employee fails to complete section one…" Mr Shadbolt did complete section one. The Appellant inserted code W1747L in the additional space as the tax code used.

10. Mr Shadbolt contacted HMRC in January 2012 to query the 1474L tax code. .

11. On 28 February, the Appellant received a communication from HMRC instructing it to apply the tax code BR to Mr Shadbolt's salary. This meant that the Appellant should have deducted tax at the basic rate from the employee's salary. Had the Appellant applied that code, it would have meant that Mr Shadbolt would have received no pay that month. Indeed, there would have been a deficit. Mrs Jones therefore wrote to HMRC to check their instructions and also attempted to telephone them, without success. In the meantime, she continued to use code 1747L.

12. On 8 March, HMRC confirmed the BR code and the Appellant began to operate that code from 12 April.

13. Mr Shadbolt left the Appellant's employment in August 2012.

14. HMRC wrote to Mr Shadbolt on 8 November 2012 to inform him that he had not paid enough tax for the tax year 2011-12 and requesting payment. This was passed to Mrs Jones.

15. On 24 February 2014, HMRC wrote to the Appellant to say that it had not deducted enough PAYE tax from Mr Shadbolt's earnings and requesting it to pay the tax owed. That letter stated that the tax was £1,901.64. This figure had been calculated on the, incorrect, basis that Mr Shadbolt had provided a P45 showing a tax code of 747L week1/month 1. In fact, Mr Shadbolt had produced only the P11 and payslip from the previous employer. A letter was issued on 25 June 2014 showing the correct tax due of £2,525.80.

16. The February letter stated "If you agree you made a mistake but think that the employee should pay the tax, then please send us an explanation in writing telling us how the error was made… .Your explanation should show how you took reasonable care to operate PAYE and made the error in good faith". This is directed to Regulation 72 which we discuss below.

17. Mrs Jones replied on 24 May 2014, setting out what had happened and her efforts to contact HMRC but no information about how she had taken reasonable care to operate PAYE.

18. There was further correspondence on 4 July 2014 in which Mrs Jones set out the enquiries she had made to try and obtain the correct tax code for Mr Shadbolt. She added "we feel that if you wish to recover these monies, it should be through Mr Shadbolt as he clearly benefited from the situation".

19. HMRC'S next letter, on 20 August 2014 said that HMRC would consider making a Regulation 80 determination which would prevent them from considering any claim that Mr Shadbolt should pay the tax.

20. There were further exchanges of correspondence along the same lines and on 23 April 2015, HMRC issued a Regulation 80 determination requiring the Appellant to pay the £2,525.80 PAYE tax under-deducted from Mr Shadbolt's salary.

21. *The Law*

22. The law is not in dispute and it is set out in the Regulations.

23. Regulation 21 imposes an obligation on an employer to deduct or repay tax on payments made to an employee by reference to an employee's code even if the code is the subject of an objection or appeal.

24. Regulation 46 requires an employee to provide specified information on Form P46 where he commences employment and does not have a Form P45. HMRC's guidance, as it applied at the time, enabled an employer to obtain the specified information otherwise than by using a Form P46, but the information required was the same in each case. This information was not contained in Form P11 or Mr Shadbolt's payslip. The Form P46 requires the employee to tick one of three boxes setting out his current situation and Regulations 47 to 49 set out what code the employer is to apply depending on which box is ticked. Where Box C is ticked, the employer must operate a BR week 1/month1 code.

25. Regulation 72 confers a discretionary power on HMRC to recover under-deducted tax from the employee instead of the employer and Regulation 72A sets out the procedure to be followed. These Regulations provide as follows.

72 (1) This regulation applies if—

(a) it appears to the Inland Revenue that the deductible amount exceeds the amount actually deducted, and

(b) condition A or B is met.

(2) In this regulation [and regulations 72A and 72B]—

"the deductible amount" is the amount which an employer was liable to deduct from relevant payments made to an employee in a tax period;

"the amount actually deducted" is the amount actually deducted by the employer from relevant payments made to that employee during that tax period;

"the excess" means the amount by which the deductible amount exceeds the amount actually deducted.

(3) Condition A is that the employer satisfies the Inland Revenue—

(a) that the employer took reasonable care to comply with these Regulations, and

(b) that the failure to deduct the excess was due to an error made in good faith.

(4) …

(5) The Inland Revenue may direct that the employer is not liable to pay the excess to the Inland Revenue.

[(5A) Any direction under paragraph (5) must be made by notice ("the direction notice"), stating the date the notice was issued, to—

(a) the employer and the employee if condition A is met;

(b) …

(5B) A notice need not be issued to the employee under paragraph (5A)(a) if neither the Inland Revenue nor the employer are aware of the employee's address or last known address.]

(6) If a direction is made, the excess must not be added under regulation 185(5) or 188(3)(a) (adjustments to total net tax deducted for self-assessments and other assessments) in relation to the employee.

72A (1) In relation to condition A in regulation 72(3), the employer may by notice to the Inland Revenue ("the notice of request") request that the Inland Revenue make a direction under regulation 72(5).

(2) The notice of request must—

(a) state—

(i) how the employer took reasonable care to comply with these Regulations; and

(ii) how the error resulting in the failure to deduct the excess occurred;

(b) specify the relevant payments to which the request relates;

(c) specify the employee or employees to whom those relevant payments were made; and

(d) state the excess in relation to each employee.

(3) The Inland Revenue may refuse the employer's request under paragraph (1) by notice to the employer ("the refusal notice") stating—

(a) the grounds for the refusal, and

(b) the date on which the refusal notice was issued.

(4) The employer may appeal against the refusal notice—

(a) by notice to the Inland Revenue,

(b) within 30 days of the issue of the refusal notice,

(c) specifying the grounds of the appeal.

(5) For the purpose of paragraph (4) the grounds of appeal are that—

(a) the employer did take reasonable care to comply with these Regulations, and

(b) the failure to deduct the excess was due to an error made in good faith.

(6) If on appeal under paragraph (4) [that is notified to the tribunal] it appears to the [tribunal] that the refusal notice should not have been issued [the tribunal] may direct that the Inland Revenue make a direction under regulation 72(5) in an amount the [tribunal determines] is the excess for one or more tax periods falling within the relevant tax year.]

26. Regulation 80 applies where PAYE tax should have been deducted by the employer, but remains payable. HMRC may determine the amount of tax to be paid and serve notice of their determination on the employer. In full:

80 (1) This regulation applies if it appears to [HMRC] that there may be tax payable for a tax year under regulation [67G[, as adjusted by regulation 67H(2) where appropriate,] or] 68 by an employer which has neither been—

(a) paid to [HMRC], nor

(b) certified by [HMRC] under regulation [75A,] 76, 77, 78 or 79.

[(1A) In paragraph (1), the reference to tax payable for a tax year under regulation 67G includes a reference to any amount the employer was liable to deduct from employees during the tax year whether or not that amount was included in any return under regulation 67B (real time returns of information about relevant payments) or 67D (exceptions to regulation 67B).]

(2) [HMRC] may determine the amount of that tax to the best of their judgment, and serve notice of their determination on the employer.

(3) A determination under this regulation must not include tax in respect of which a direction under regulation 72(5) has been made; and directions under that regulation do not apply to tax determined under this regulation.

[(3A) A determination under this regulation must not include tax in respect of which a direction under regulation 72F has been made.

(4) A determination under this regulation may—

(a) cover the tax payable by the employer under regulation [67G[, as adjusted by regulation 67H(2) where appropriate,] or] 68 for any one or more tax periods in a tax year, and

(b) extend to the whole of that tax, or to such part of it as is payable in respect of—

(i) a class or classes of employees specified in the notice of determination (without naming the individual employees), or

(ii) one or more named employees specified in the notice.

(5) A determination under this regulation is subject to Parts 4, 5[, 5A] . . .and 6 of TMA (assessment, appeals, collection and recovery) as if—

(a) the determination were an assessment, and

(b) the amount of tax determined were income tax charged on the employer,

and those Parts of that Act apply accordingly with any necessary modifications.

27. A determination is treated as an assessment under the Taxes Management Act 1970 (TMA) for the purposes of procedure and appeals. Section 50(6) of that Act provides:

"(6) [If, on an appeal notified to the tribunal, the tribunal decides—]

(a) that, . . ., the appellant is overcharged by a self-assessment;

(b) that, . . ., any amounts contained in a partnership statement are excessive; or

(c) that the appellant is overcharged by an assessment other than a self-assessment,

the assessment or amounts shall be reduced accordingly, but otherwise the assessment or statement shall stand good."

28. So our powers in this appeal against the Regulation 80 determination are to consider whether the amount of the determination is excessive or not. However, we must also consider the relationship between Regulation 80 and Regulation 72 and whether there is any room for Regulation 72 to apply in this case.

29. *The Appellant's submissions*

30. The Appellant submits that it operated PAYE correctly in relation to Mr Shadbolt and that, in the absence of the P45 they applied the code which had been used by his previous employer and which had not been queried by HMRC.

31. Mrs Jones contends the Appellant acted in good faith.

32. She further argues that she did everything she could to check the code and ascertain the correct code and that the Appellant was let down by HMRC who failed to answer telephone calls or respond to correspondence and that this failure by HMRC led to the current situation.

33. *The Respondent's submissions*

34. The Respondent submits that if a new employee does not provide a Form P45, the employer must obtain a Form P46 from the employee and operate the code stated on that form, depending on the box ticked by the employee.

35. Form P46 itself tells the employer to operate the BR code where the employee ticks Box C.

36. HMRC issued manual coding notices to the Appellant on 14 February 2012 (though it appears the Appellant received this on 28 February) and on 8 March 2012 which instructed the Appellant to operate the BR code.

37. Code 1474L resulted in a weekly tax free allowance of £335.96 but Mr Shadbolt's payslip showed a tax free amount of £143.80 a week so the Appellant should have realised that the code it used was wrong.

38. The determination under Regulation 80 assessed the correct amount of underpaid tax, that is £2,525.80 and the determination should be upheld.

39. *Discussion*

40. If the Tribunal is satisfied that the determination has been validly made and the amount of tax sought is correct, then it must, under section 50(6) TMA, order that the determination stand good.

41. As set out in HMRC's letters of 24 February 2014 and 20 August 2014, once they make a Regulation 80 determination, they are precluded from seeking the tax from Mr Shadbolt. That is the effect of the second part of Regulation 80(3) which states that "*a determination under this regulation must not include tax in respect of which a direction under regulation 72(5) has been made; and directions under that regulation*

do not apply to tax determined under this regulation." Regulation 80 imposes the tax on the employer and Regulation 72 imposes it on the employee. The two regulations are mutually exclusive.

42. Regulation 72 applies if either Condition A or Condition B applies. Condition B is not relevant. Condition A requires that the employer must satisfy HMRC that it took reasonable care to comply with the Regulations and that the under-deduction of tax was due to "an error made in good faith". Where the employer so satisfies HMRC, Regulation 72(5) enables HMRC (on a discretionary basis) to direct that the employer is not liable to pay the tax.

43. In order for HMRC to consider exercising its discretion to make a determination under Regulation 72(5), the employer must make a notice of request which must contain specified information, namely:

(a) how the employer took reasonable care to comply with the Regulations; and

(b) how the error resulting in the failure to deduct the excess occurred;

(b) specifying the relevant payments to which the request relates;

(c) specifying the employee or employees to whom those relevant payments were made; and

(d) stating the excess in relation to each employee.

44. Mrs Jones' letters of 24 May and 4 July 2014 and the other letters which preceded the Regulation 80 determination did not set out this information and cannot have amounted to a notice of request. In particular, the correspondence did not set out how the Appellant took reasonable care to comply with the Regulations and how the error resulted in the failure to deduct the right amount of tax.

45. In any event, we do not consider that both limbs of Condition A were satisfied.

46. We entirely accept that Mrs Jones acted in good faith at all times and that she made genuine efforts to try and find out the correct tax code to apply to Mr Shadbolt's pay.

47. However, the first part of condition A requires the Appellant to have taken reasonable care to comply with the PAYE Regulations. This the Appellant did not do. As set out in *Poole Leisure Ltd v HMRC* [2015] UKFTT 0109 (TC), applying *Wald v Revenue and Customs Commissioner*s [2011] UKFTT 183(TC), the responsibility for compliance with the PAYE regulations rests on the employer.

48. The Appellant is an experienced employer with over 20 employees. It is aware of its obligations in relation to PAYE and it was aware of the existence of Form P46

and that it should be used if the employee had not produced a P45. HMRC argue that Part Two of Form P46 itself tells the employer to operate the BR code if the employee ticks box C. We find Form P46 ambiguous in that it requires the employer to tick the code used by reference to the Box ticked by the employee, rather than instructing the employer to use the relevant code depending on the Box ticked. However, an experienced employer like the Appellant might have been expected to infer that Part Two of the Form set out the code which they should use rather than merely asking them what code they in fact used. In addition, the form sets out where an employer could find online guidance if they were not sure of the correct code. The on-line guidance has an extensive section about what to do if an employee does not have a P45. It states that an employee must complete Form P46 (or provide the same information in another format) and clearly sets out that if an employee ticks Box C, the employer must operate code BR.

49. This information was available to the Appellant, but it chose to use the tax code from the former employment which was not in accordance with the Regulations.

50. Further, HMRC issued a BR code to the Appellant in February and March 2014 but the Appellant continued to use the wrong code until April 2014.

51. Part of the problem arose from an error in interpreting the code shown on the Form P11. That form showed the code as "W1474L". The actual code was 474L to be operated on a week 1 basis. The Appellant interpreted this to be code 1474L. This meant they allowed Mr Shadbolt a much higher tax free allowance than he should have had which resulted in an initial repayment of tax. This meant that when the BR code issued by HMRC in February was applied it resulted in a very high tax charge for that month, leaving Mr Shadbolt with no pay, because there was a clawback of the amount wrongly refunded. Mrs Jones could not believe that this was right and so continued to operate the erroneous code.

52. However, it cannot be said in these circumstances that the Appellant took reasonable care to comply with the Regulations, so Condition A in Regulation 72(3) would not have been satisfied, even if it was open to HMRC to make a Regulation 72(5) Direction, which it could not do. Once the Regulation 80 direction was made, it was no longer possible for them to seek to recover the tax from Mr Shadbolt.

53. Having said that, we acknowledge that Mrs Jones made genuine efforts to contact HMRC to clarify the correct code with them. As Mrs Jones observed at the hearing, had someone from HMRC picked up the telephone on one of the many occasions when she had called the HMRC helpline between September and December 2012, the current situation would never have arisen. We would add our criticism of HMRC's customer service to the many other criticisms which have been made of it and we hope that in the future, people in Mrs Jones' position will find it easier to obtain the help they seek from HMRC to pay the right amount of tax.

54. *Decision*

55. For the reasons set out above, we find that the Regulation 80 determination in the sum of £2,525.80 made on the Appellant was validly made and should stand good.

56. Accordingly, we dismiss the appeal.

57. 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.

MARILYN MCKEEVER
TRIBUNAL JUDGE

RELEASE DATE: 2 JUNE 2016