TC02738

Appeal number: TC/2012/05349

VAT – Flat Rate Scheme – Appeal against HMRC refusal to allow retrospective application

FIRST-TIER TRIBUNAL
TAX CHAMBER

GEOFFREY SEEFF **Appellant**
t/a TPL ASSOCIATES

- and -

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

TRIBUNAL: JUDGE CHRISTOPHER STAKER
CAROLINE DE ALBUQUERQUE

Sitting in public at London on 17 May 2013

Mr L Bingham for the Appellant

The Appellant in person

DECISION

Introduction

1. The Appellant appeals against a decision of HMRC dated 12 February 2012, affirmed on review on 4 April 2012, refusing the Appellant's request dated 31 January 2012 to convert his VAT registration retrospectively to the flat-rate scheme ("**FRS**").

2. At the end of the hearing of this appeal on 17 May 2012, the Tribunal gave an oral determination allowing the appeal. Mr Bingham requested full written reasons for the Tribunal's decision, which are now provided.

The facts

3. The background facts of the case have been set out by the Appellant in his correspondence with HMRC in relation to his request for retrospective application of the FRS, and in relation to his appeal against the HMRC decision to refuse that request. HMRC have not sought to dispute the backgrounds facts. On its consideration of the evidence, the Tribunal finds the following facts to be established on a balance of probability.

4. The Appellant is a Fellow of the Chartered Institute of Accountants in England and Wales and has a PhD from the University of Birmingham. He has practised for over 35 years as a management consultant. In 2007, he resigned from his then employer to set up a management consultancy as an unincorporated sole practitioner. Based on discussions with prospective clients and his previous experience, he forecast that his turnover would exceed by a considerable margin the threshold for registration for VAT, and he therefore registered for VAT with effect from 2 January 2007.

5. At the time that he registered for VAT, he would have been entitled to apply to use the FRS if his expected turnover was less than £150,000. The FRS is provided for in s 26B of the Value Added Tax Act 1994 ("**VATA**"). Under the FRS, VAT is calculated as a percentage of sales, without the need to calculate input tax and the corresponding need to keep receipts for purchases. Throughout the period of his VAT registration, the Appellant was aware of the availability of the FRS, but he did not apply to use it as he thought that his turnover would exceed the £150,000 threshold.

6. Unfortunately for the Appellant, matters did not work out as he had hoped, in part due to the general economic situation from 2008. His turnover during his first year of registration was some £44,000. During the second year of registration it was some £49,000. In the third year, it was some £36,000. In the fourth year it was less than £1,000. In the fifth year it was some £23,000. Thus, in fact, at no point did the turnover reach anywhere near the threshold for VAT registration.

7. Throughout the period of his VAT registration, the Appellant had expectations that the situation would improve. Eventually, he came to accept that there was no prospect of this happening. On 31 January 2012, he wrote to HMRC, noting that he

had never reached the threshold for mandatory VAT registration, and requesting that he be deregistered with effect from 31 December 2011.

8. That 31 January 2012 letter also requested that the period of his VAT registration from 2 January 2007 to 31 December 2011 be converted retrospectively to the FRS. In support of this request, the representations made in the letter included the following:

(1) At no time during the period of VAT registration had his turnover reached the mandatory threshold for registration.

(2) The Appellant's management consultancy business was severely affected by the financial crisis of 2008.

(3) The failure to secure the expected turnover and the economic downturn has caused immense financial difficulty to the Appellant personally.

(4) The Appellant disadvantaged himself and exacerbated his financial difficulties by not converting his registration to the FRS.

9. These representations were expanded upon in subsequent correspondence with HMRC. In a letter dated 7 March 2012, after the original HMRC decision but before the review decision, the Appellant set out why he considered that his case was exceptional. He said that throughout the period of his registration, he expected an upturn, and therefore did not apply to deregister for VAT or apply for the FRS. Then in early 2009 his income plummeted catastrophically. By the time that he realised that the FRS would be appropriate, it was too late to gain anything by making an application. He stated that "the sudden and total disappearance of my business ... makes my situation ... exceptional".

10. The Appellant's total VAT liability for the whole period of his VAT registration using the standard basis of accounting is £23,997. His total liability under the FRS would be £21,846, a difference of £2,151.

Applicable law and guidance

11. HMRC has the power under regulation 55B(1)(b) of the VAT Regulations 1995 to allow a retrospective start date for the FRS. In the present case, HMRC has accepted that it had the power to grant the Appellant's request to have the whole of his period of VAT registration retrospectively placed under the FRS, and that the Appellant qualified for the FRS for the whole of that period.

12. HMRC has guidance on how to deal with applications for the retrospective application of the FRS. FRS3200 provides that the power to allow retrospective applications is one that HMRC must "use reasonably in the circumstances of each case", that the decision maker must "consider all the relevant facts", and must explain the main reasons and indicate the main factors taken into account if the decision is to refuse. FRS3300 lists factors to be taken into account by the decision maker under four bullet points. The first bullet point states again that "Each case should be considered on its own merits". It states that the fact that less tax would be paid under

the FRS is not "sufficient" reason to authorise use of the scheme retrospectively, but it does not state that this is a wholly irrelevant consideration. The second bullet point states that authorisation may be refused if this would present a revenue risk. HMRC have not suggested that this is a consideration in the present case. The third bullet point states that because the purpose of the FRS is to simplify VAT accounting, "The policy is to refuse retrospection where the business has already calculated its VAT liability ... using a different accounting method", subject to the fourth bullet point. The fourth bullet point states that there may be "exceptional circumstances" where this policy should not apply, and that such cases are "likely to involve compassionate circumstances, or the survival of the business". It is added that HMRC "have not identified to date any case where such circumstances justify a departure from the normal policy".

13. Section 83(1)(fza) VATA provides for an appeal to the Tribunal against a decision of HMRC refusing or withdrawing authorisation to use the FRS.

14. Section 84(4ZA) VATA provides that "the tribunal shall not allow the appeal unless it considers that [HMRC] could not reasonably have been satisfied that there were grounds for the decision". Mr Bingham accepted on behalf of HMRC that if the Tribunal considered that HMRC could not reasonably have been satisfied that there were grounds for the HMRC decision, the Tribunal could substitute its own decision on the Appellant's application for retrospective application of the FRS.

The HMRC decision

15. The HMRC decision of 10 February 2012 referred to FRS3300, and said simply that "Where a trader has already calculated their VAT liability using normal accounting, retrospective use of the Flat Rate Scheme would be authorised only where justified by exceptional circumstances".

16. The Tribunal notes that this decision does not consider in terms whether or not there are exceptional circumstances in the present case. In particular, it does not address the representations made by the Appellant, and reach a conclusion on whether these representations amount to exceptional circumstances.

17. The HMRC review decision of 4 April 2012 refers to the applicable legislation and guidance. It then notes that under the guidance, "survival of a business may be an exceptional circumstance", but concludes that: "*In order for retrospective entry due to exceptional circumstances to apply there would need to be firm evidence that a trader would be put out of business as a direct result of a decision to refuse retrospection. In your case it appears the business has already ceased to trade and retrospection cannot be allowed simply to reduce any outstanding tax due*".

Arguments of the parties

18. The Appellant's grounds are set out in his notice of appeal, a reply to the statement of case, and his oral submissions at the hearing. Various of his points reflect his earlier correspondence with HMRC. His main grounds are as follows:

(1) HMRC has not considered the points made the Appellant in his application for retrospectivity.

(2) The HMRC finding that "survival of the business" is not at stake because he has ceased trading is wrong. He has not ceased trading (although he has minimal turnover), but has merely deregistered for VAT.

(3) HMRC have a duty to advise taxpayers of their options, in particular of the availability of the FRS, where it is apparent from returns that it would apply, or when a business is no longer required to be registered for VAT at all.

(4) It is not equitable that two businesses with the same turnover trading in the same circumstances could be liable to different amounts of tax, merely as a consequence of their different expectations at a given point in time as to what may happen in the future.

(5) If a business registered for the FRS exceeded the threshold for the scheme, HMRC would seek to claw back the additional tax liability. HMRC should be required, conversely, to repay the additional VAT in cases where a business did not register because it thought it would exceed the threshold, but then ultimately did not.

(6) Although HMRC state that the FRS was introduced to ease the administrative burden placed on small traders, in fact it does not achieve this purpose, and the scheme is perceived by the general business community as a tax incentive for small businesses which is only ever used when it is financially advantageous to the business.

(7) The Appellant relied on *Anderson v Revenue & Customs* [2007] UKVAT V20255 at [29]-[30] as an example of a case where the Tribunal allowed an appeal where the HMRC decision "over-simplified the Appellant's case".

(8) The Appellant also relied on *AC Wadlewski* [LON 94/1849], quoted in Anderson at [20], for the proposition that the fact that he would have paid less under the FRS is a relevant consideration.

19. The HMRC position is, in essence, that the HMRC decision did consider all of the circumstances relied upon by the Appellant, that the decision was in accordance with HMRC policy, that the Appellant's only reason for wanting retrospective application of the FRS was that it would reduce his VAT liability, that there were no exceptional circumstances, and that HMRC is under no obligation to give the individualised advice suggested by the Appellant. It is said that therefore, for purposes of s 84(4ZA) VATA, HMRC was entitled to be satisfied that there were grounds for its decision. HMRC relied on *Burke v Revenue & Customs* [2008] UKVAT V20881, *HM Revenue and Customs v Burke* [2009] EWHC 2587 (Ch), *Skinner (t/a DLS Packaging) v Revenue & Customs* [2010] UKFTT 64 (TC), *SD Solutions Ltd v Revenue & Customs* [2010] UKFTT 228 (TC) and *Anycom Ltd v Revenue & Customs* [2011] UKFTT 654 (TC).

The Tribunal's findings

20. The Tribunal finds that the HMRC decision did not in terms consider the specific circumstances invoked by the Appellant, referred to in paragraph 8 above, nor did the review decision consider the submissions referred to in paragraph 9 above.

21. On its reading of those decision letters, the Tribunal is satisfied that they did not consider those specific circumstances at all. Mr Bingham suggested that it could be inferred that the decision maker considered everything advanced by the Appellant, and that the decision did not need to refer to every consideration individually. However, the Tribunal considers that the decision needs to show at least that the core elements of the Appellant's case were considered. The Appellant was not simply saying that the FRS would be more advantageous to him, and that he was suffering financially. His point was that this was not a case of a business not knowing in advance whether or not the FRS would be more advantageous, and then applying for the scheme retrospectively when it was established with hindsight that it would have been more advantageous. Rather, his case was, in essence, as follows. He had had good reason at the outset for thinking that his turnover would be above the threshold for VAT registration and above the threshold making him ineligible for the FRS. His expectations turned out to be catastrophically wrong, which he could not have foreseen. Nonetheless he did not apply for the FRS earlier because he still had expectations that the situation would improve, which also proved to be wrong. So catastrophically wrong were his expectations that he need never have registered for VAT at all, and he is currently suffering considerable financial hardship.

22. The HMRC decisions do not consider whether this peculiar combination of circumstances amounts to exceptional circumstances that would justify granting retrospective application of the FRS. The guidance makes clear that "Each case should be considered on its own merits" and that "all relevant facts" must be considered. The guidance is expressed in non-mandatory language. In referring to exceptional circumstances that might justify retrospectivity, the policy states, in an open-ended way, what "in principle" such circumstances are "likely" to involve. The guidance does not lay down any hard and fast rules. In contrast, the 4 April 2012 HMRC review decision states for instance that "there would need to be firm evidence that a trader would be put out of business as a *direct* result of a decision to refuse retrospection". Not only does the decision suggest that this is a hard and fast rule, but the language used here does not itself even appear in the guidance.

23. The Tribunal therefore considers not only that the HMRC decision maker has not considered all of the circumstances advanced by the Appellant, but also has not properly applied the guidance. For this reason, the Tribunal finds under s 84(4ZA) VATA that HMRC could not reasonably have been satisfied that there were grounds for the decision" (compare *Anderson* at [29]-[30]).

24. The Tribunal therefore proceeds to make its own decision on the Appellant's application for retrospective application of the FRS.

25. Because each case must be considered on its own particular merits, the cases relied on by HMRC afford little assistance. In *Burke*, the Chancery Division

ultimately held that HMRC were entitled to make the original decision that they did, and that HMRC were under no duty to raise the FRS with the appellant in that case. In *Skinner*, *SD Solutions* and *Anycom*, the circumstances were not identical to the present case, and in any event, as noted in *SD Solutions* at [25], "Similarities in the factual position will not necessarily result in similar outcomes".

26. In making its own decision, the Tribunal has regard to the HMRC Guidelines. The guidelines state that the fact that less tax would be paid under the FRS is "not sufficient reason" to authorise retrospectivity, but do not suggest that this is a wholly irrelevant consideration (compare *Wadlewski* referred to above). The Tribunal is satisfied that in the present case there are exceptional circumstances justifying retrospectivity. It is not a simple case of a business being unaware of the FRS, or simply realising after the event that less tax would have been paid under the FRS. It is a case where reasonable expectations proved unforeseeably to be catastrophically wrong, to the extent that the Appellant fell far short of the threshold for registering for VAT at all, and where the Appellant is now suffering considerable financial hardship.

27. For the above reasons, the Tribunal allows the appeal. In the circumstances it is unnecessary to address the Appellant's other arguments referred to at paragraph 18(3)-(6) above, other than to note that the Tribunal did not find them persuasive.

28. 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.

DR CHRISTOPHER STAKER
TRIBUNAL JUDGE

RELEASE DATE: 5 June 2013