[2015] UKFTT 0690 (TC)

TC04808

Appeal number: TC/2015/03278

VALUE ADDED TAX – Flat-rate scheme – assessment to recover VAT where trader does not implement increase in percentage – appellant claiming correct percentage for actual business used instead of incorrect percentage for business category applied for – whether s 84(4ZA) VATA (supervisory review) applies – no – assessment cancelled – decision not to allow appellant to retrospectively use percentage for actual business – HMRC decision held unreasonable – decision cancelled.

FIRST-TIER TRIBUNAL
TAX CHAMBER

KDT MANAGEMENT LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE RICHARD THOMAS
NIGEL COLLARD

Sitting in public at 1 Edward St, Brighton on 10 December 2015

Mr Keith Talbot, director, for the Appellant

Mrs Rita Pavely, Presenting Officer, for the Respondents

DECISION

1. This was an appeal by KDT Management Ltd ("the appellant") against assessments to VAT and interest for the prescribed accounting periods and of the amounts set out in Column 1 and 2 respectively of this table:

Period*	Amount £
09/10	244
12/10	750
03/11	1,835
06/11	1,494
09/11	2,122
12/11	2,558
03/12	619
06/12	1,439
09/12	1,588
12/12	793
03/13	363
06/13	1,211
09/13	1,240
12/13	738
03/14	1,066

The notice of assessment showing the amounts and periods listed also contained an assessment to interest of £1130.84.

*A period designated XX/YY in the first column is a period of three months ending on the last day of the month (XX) of the year (20YY).

2. The assessments were made to recover VAT alleged to have been omitted from the appellant's returns because it did not apply certain increases of rate to its turnover under the Flat-rate Scheme ("FRS") of accounting for VAT

3. This is also an appeal against a decision by HMRC not to allow the appellant to retrospectively apply the percentage of turnover it says was appropriate to its business under the FRS instead of the one it says it mistakenly chose.

Evidence

4. We had a bundle of documents from HMRC. Mr Talbot for the appellant also produced documents, being screen prints of the pages of the appellant's website which set out what the appellant's business was and the services it offered. We thank both Mr Talbot for the appellant and Mrs Pavely for the Commissioners for Her Majesty's Revenue and Customs ("HMRC") for their well-structured and succinct submissions and for letting us have a copy of their speaking notes.

5. Mr Talbot, in making his submissions to us, was in part giving evidence, and he was questioned by Mrs Pavely and by the Tribunal.

6. We found Mr Talbot be an honest and credible witness and we accept his evidence.

Law

7. Article 281 of the Principal VAT Directive (EC/2006/112) ("PVD") says:

> "Member States which might encounter difficulties in applying the normal VAT arrangements to small enterprises, by reason of the activities or structure of such enterprises, may, subject to such conditions and limits as they may set, and after consulting the VAT Committee, apply simplified procedures, such as flat-rate schemes, for charging and collecting VAT provided that they do not lead to a reduction thereof."

Art. 281 is in a Section headed "Simplified procedures for charging and collection" and is in a Chapter headed "Special scheme for small enterprises".

8. The United Kingdom has taken up the option of applying a flat-rate scheme and in s 26B Value Added Tax Act 1994 ("VATA") it is provided (relevantly) that:

> "(1) The Commissioners may by regulations make provision under which, where a taxable person so elects, the amount of his liability to VAT in respect of his relevant supplies in any prescribed accounting period shall be the appropriate percentage of his relevant turnover for that period.
>
> A person whose liability to VAT is to any extent determined as mentioned above is referred to in this section as participating in the flat-rate scheme.
>
> (2) For the purposes of this section—
>
> > (a) a person's "relevant supplies" are all supplies made by him except supplies made at such times or of such descriptions as may be specified in the regulations;

(b) the "appropriate percentage" is the percentage so specified for the category of business carried on by the person in question;

(c) a person's "relevant turnover" is the total of—

(i) the value of those of his relevant supplies that are taxable supplies, together with the VAT chargeable on them, and

(ii) the value of those of his relevant supplies that are exempt supplies.

(3) The regulations may designate certain categories of business as categories in relation to which the references in subsection (1) above to liability to VAT are to be read as references to entitlement to credit for VAT.

(4) The regulations may provide for persons to be eligible to participate in the flat-rate scheme only in such cases and subject to such conditions and exceptions as may be specified in, or determined by or under, the regulations.

(5) Subject to such exceptions as the regulations may provide for, a participant in the flat-rate scheme shall not be entitled to credit for input tax.

This is without prejudice to subsection (3) above.

(6) The regulations may—

(a) provide for the appropriate percentage to be determined by reference to the category of business that a person is expected, on reasonable grounds, to carry on in a particular period;

(b) provide, in such circumstances as may be prescribed, for different percentages to apply in relation to different parts of the same prescribed accounting period;

(c) make provision for determining the category of business to be regarded as carried on by a person carrying on businesses in more than one category.

(7) The regulations may provide for the following matters to be determined in accordance with notices published by the Commissioners—

(a) when supplies are to be treated as taking place for the purposes of ascertaining a person's relevant turnover for a particular period;

(b) the method of calculating any adjustments that fall to be made in accordance with the regulations in a case where a person begins or ceases to participate in the flat-rate scheme.

(8) The regulations may make provision enabling the Commissioners—

(a) to authorise a person to participate in the flat-rate scheme with effect from—

(i) a day before the date of his election to participate, or

(ii) a day that is not earlier than that date but is before the date of the authorisation;

(b) to direct that a person shall cease to be a participant in the scheme with effect from a day before the date of the direction.

The day mentioned in paragraph (a)(i) above may be a day before the date on which the regulations come into force.

(9) Regulations under this section—

(a) may make different provision for different circumstances;

(b) may make such incidental, supplemental, consequential or transitional provision as the Commissioners think fit, including provision disapplying or applying with modifications any provision contained in or made under this Act."

9. The regulations for which s 26B VATA gives the vires are in Part VIIA of the Value Added Tax Regulations 1995 (SI 1995/2812) ("the Regulations"), the relevant regulations of which are:

"**55A Interpretation of Part VIIA**

(1) In this Part—

"EDR" means the day with effect from which a person is registered under the Act;

…

"flat-rate trader" means a person who is, for the time being, authorised by the Commissioners in accordance with regulation 55B(1);

…

"start date" has the meaning given in regulation 55B(2);

"the scheme" means the flat-rate scheme for small businesses established by this Part;

"the Table" means the table set out in regulation 55K.

(3) For the purposes of this Part, "relevant date", in relation to a flat-rate trader, means any of the following--

(a) his start date;

(b) the first day of the prescribed accounting period current at any anniversary of his start date;

…

(e) any day with effect from which the Table is amended in relation to him;

(f) where regulation 55JB (reduced rate for newly registered period) applies—

(i) the day that his newly registered period begins, and

(ii) the first anniversary of his EDR.

55B Flat-rate scheme for small businesses

(1) The Commissioners may, subject to the requirements of this Part, authorise a taxable person to account for and pay VAT in respect of his relevant supplies in accordance with the scheme with effect from—

(a) the beginning of his next prescribed accounting period after the date on which the Commissioners are notified ... of his desire to be so authorised, or

(b) such earlier or later date as may be agreed between him and the Commissioners.

(2) The date with effect from which a person is so authorised shall be known as his start date.

(3) The Commissioners may refuse to so authorise a person if they consider it is necessary for the protection of the revenue that he is not so authorised.

(4) A flat-rate trader shall continue to account for VAT in accordance with the scheme until his end date.

55D Method of accounting

Subject to regulations 55H and 55JB below, for any prescribed accounting period of a flat-rate trader, the output tax due from him in respect of his relevant supplies shall be deemed to be the appropriate percentage of his relevant turnover for that period

55H

(1) The appropriate percentage to be applied by a flat-rate trader for any prescribed accounting period, or part of a prescribed accounting period (as the case may be), shall be determined in accordance with this regulation and regulations 55JB and 55K.

(2) For any prescribed accounting period—

(a) beginning with a relevant date, the appropriate percentage shall be that specified in the Table for the category of business that he is expected, at the relevant date, on reasonable grounds, to carry on in that period;

(b) current at his start date but not beginning with his start date, the appropriate percentage shall be that specified in the Table for the category of business that he is expected, at his start date, on reasonable grounds, to carry on in the remainder of the period;

(c) not falling within (a) or (b), the appropriate percentage shall be that applicable to his relevant turnover at the end of the previous prescribed accounting period.

(3) Except that, where a relevant date other than his start date occurs on a day other than the first day of a prescribed accounting period, the following rules shall apply for the remainder of that prescribed accounting period—

(a) for the remaining portion, the appropriate percentage shall be that specified in the Table for the category of business that he is expected, at the relevant date, on reasonable grounds, to carry on in that period;

(b) "remaining portion" means that part of the prescribed accounting period in which the relevant date occurs—

(i) starting with the relevant date, and

(ii) ending on the last day of that prescribed accounting period;

(c) the appropriate percentage specified in sub-paragraph (a) shall be applied to his relevant turnover in the remaining portion described;

(d) if the rules set out in paragraphs (a) to (c) apply and then another relevant date occurs in the same prescribed accounting period, then—

(i) the existing remaining portion ends on the day before the latest relevant date,

(ii) another remaining portion begins on the latest relevant date, and

(iii) the rules in paragraph (a) to (c) shall be applied again in respect of the latest remaining portion.

55JB Reduced appropriate percentage for newly registered period

(1) This regulation applies where a flat-rate trader's start date falls within one year of his EDR.

…

(3) At any relevant date on or after 1st January 2004 falling within his newly registered period, the Table shall be read as if each percentage specified in the right-hand column were reduced by one.

(4) A flat-rate trader's "newly registered period" is the period—

(a) beginning with the later of—

(i) his start date; and

(ii) the day the Commissioners received notification of, or otherwise became fully aware of, his liability to be registered under the Act, and

(b) ending on the day before the first anniversary of his EDR.

55K Category of business

(1) Where, at a relevant date, a flat-rate trader is expected, on reasonable grounds, to carry on business in more than one category in the period concerned, paragraph (3) below shall apply.

(3) He shall be regarded as being expected, on reasonable grounds, to carry on that category of business which is expected, on reasonable grounds, to be his main business activity in that period.

(4) In paragraph (3) above, his main business activity in a period is to be determined by reference to the respective proportions of his relevant turnover expected, on reasonable grounds, to be generated by each business activity expected, on reasonable grounds, to be carried on in the period.

Table[1]

Category of business	**Appropriate percentage**
…	…
Advertising	11
…	…
Management consultancy	14
…	…

Tribunal's Note: This Table was substituted by regulation 4 of the Value Added Tax (Amendment) (No 3) Regulations, SI 2010/2940 with effect from 4 January 2011. Before then (and on or after 1 January 2010) the percentages were (by virtue of regulation 9 of the Value Added Tax (Amendment) (No. 5) Regulations 2009 (SI 2009/3241)) as follows:

Category of business	**Appropriate percentage**
…	…
Advertising	10
…	…
Management consultancy	12.5
…	…

But before 1 January 2010 the percentages were (by virtue of regulation 4 of the Value Added Tax (Amendment) (No. 2) Regulations 2008 (SI 2008/3021)) as follows:

Category of business	**Appropriate percentage**
…	…
Advertising	8.5
…	…
Management consultancy	11
…	…

55N Notification

(1) Where—

(a) at the first day of the prescribed accounting period current at any anniversary of his start date,

(b) the appropriate percentage to be applied by a flat-rate trader in accordance with regulation 55H(2)(a) for the prescribed accounting period just beginning differs from that

[1] It is difficult to see what the Table is doing in regulation 55K. The preceding paragraphs of that regulation do not relate, or refer, to the Table. The Table *is* referred to in regulations 55H(2) and (3) and 55JB(3) but they do not indicate where the Table is to be found.

applicable to his relevant turnover at the end of the previous prescribed accounting period,

he must notify the Commissioners of that fact within 30 days of the first day of the prescribed accounting period current at the anniversary of his start date.

(2) Where a flat-rate trader begins to carry on a new business activity or ceases to carry on an existing business activity, he must notify the Commissioners of—

(a) that fact,

(b) the date that is the relevant date described by regulation 55A(3)(c) or (d) (as the case may be), and

(c) the appropriate percentage to be applied to the period immediately before that relevant date and immediately after it,

within 30 days of that relevant date.

(3) Where any of sub-paragraphs (a) to (g) of regulation 55M(1) apply, the flat-rate trader shall notify the Commissioners of that fact within 30 days.

(4) Any notification required by this regulation shall be given in writing."

10. Although not law there is one HMRC document that both parties relied on. HMRC's Manual on the FRS at paragraph FRS7300 sets out its view of what activities fall within each of the categories in the table in regulation 55K of the Regulations. The entries for the two categories in question are:

Advertising	Advertising consultants Advertising space providers Advertising services such as billposting
Management consultancy	Business consultancy Financial consultancy Management consultancy Public relations

The facts

11. From the documents in the bundle and from the evidence of Mr Turner we find the following facts, none of which was in dispute. We make further findings of fact below in relation to the one matter about which there was a possible dispute as to the inferences to be drawn from the facts.

12. The appellant was registered for VAT with effect from 3 June 2009.

13. In the application for registration under the heading "Description of your current and/or intended business activities" the entry was "Consultant for advertising industry". Under the heading "categorisation of your current and/or intended business activities" the entry was "Management consultancy activities (other than financial management) (main activity)".

14. On 15 July 2009 the appellant's accountants, Hilton Sharp and Clarke ("HSC") submitted an application on Form VAT 600FRS to join the FRS. At Section B under the heading "My main business activity is:" the form said "Management Consulting". The Form was signed by Mr Talbot (as he admitted at the hearing), though completed by HSC.

15. On 21 July 2009 HMRC notified the appellant of confirmation that it was authorised to use the FRS with effect from 3 June 2009. The letter asked the appellant to ensure that "your chosen trade sector accurately reflects your business activities" and said "remember to notify us if your business changes so that it falls within a different flat rate sector …". It also advised the appellant that "[f]or guidance on using the flat rate scheme, including choosing your flat rate percentage and filling in your VAT return, please see Notice 733 …"

16. On 4 July 2014 HMRC confirmed that the appellant had been withdrawn from the FRS at its request.

17. On 29 August 2014 HMRC, having made an assurance visit following the appellant's first return under the normal rules which showed a repayment as due, informed the appellant that it had not implemented the increases in the appropriate percentage for management consultancy, informing it that the rate had changed from 11% to 12.5% (for 2010) then to 14% (for 2011 onwards). The letter went on to say that an assessment of £18,060 plus interest would be raised, and enclosed, it said, a schedule of calculations. In our bundle we had "Details of the assessment" but these merely show for each prescribed accounting period the amount of the assessment being the tax underdeclared for the period. The details do not show how the amounts were calculated. The first prescribed accounting period assessed was the 09/10 one (1 July to 30 September 2010). The appellant was informed on 29 August and again on 23 September 2014 that if it disagreed with HMRC's decision it had 30 days to let them know.

18. On 2 October 2014 HSC wrote to HMRC on behalf of the appellant. They said they had reviewed the FRS criteria and believed the company had been applying the correct rate as it should fall under "advertising" where the current rate was 11%. They added that they appreciated that on the application to join the FRS the "management consultancy" category was mistakenly used and the company should have applied to change the category. It asked that the advertising rate could be applied throughout the period.

19. On 7 October 2014 HMRC wrote refusing to consider a retrospective change of category, pointing to Notice 733 paragraph 4.2 which, they said, "clearly states that

HMRC will not retrospectively change the flat rate sector that the business has chosen". Again the appellant was told it had 30 days to appeal against the decision.

20. On 11 May 2015 an appeal was made to the Tribunal.

21. The matter we refer to in §11 is what the appellant's business actually was. Mr Talbot said he *was* the business – it is a one man band. He produced the printouts of pages from the appellant's website, the front page of which had text as follows:

> "**KDT outdoor advertising services**
>
> KDT Management Ltd (KDT) is a specialist consultancy delivering income to landlords from all forms of outdoor advertising ranging from large format roadside banner displays to traditional digital and billboard media.
>
> **Services**
>
> - Independent site evaluation
> - Full or partial project management
> - Planning services
> - Printing services
>
> The downturn in the outdoor advertising market in 2009 saw revenue spend drop by more than 20%: this has made portfolio value maximisation even more essential as sites can no longer be assumed to be profitable.
>
> Cutting through the claims from the plethora of sales houses, building contractors and planning consultants, as well as agents of every nature offering to unlock the potential dormant in your portfolio is crucial in determining which sites should be developed into advertising locations and how they should be brought to market.
>
> The key to unlocking the value of a site varies location by location and also with the owner's specific requirements.
>
> With over 20 years experience of hands-on delivery and success in all aspects of generating income from outdoor advertising assets, KDT offers site owners a truly comprehensive service, commencing from the initial stage of visual conception through to site delivery with all intermediate steps covered in-house."

The heading at the top and the heading "Services" are in a larger font than, and a different colour from, the rest of the text, and the items bulleted are in a different colour.

22. A page headed "KDT Management Services" explains the appellant's "Independent site evaluation service" as enabling the client to make a fully informed choice as to what advertising services they wish to undertake in-house or have managed externally. "Project management" services are offered where the appellant will carry out one or more of the "three pillars upon which site value rests - Planning, Operation and Sales."

23. "Planning" here means obtaining etc planning consent and advising on planning issues and the site refers to the Town and Country (Control of Advertisements) Regulations 2007: the appellant says it offers a complete planning service "for your site".

24. As to "Operations" the appellant offers full site management including "liaising with all matters in conjunction with Health & Safety, Method & Risk Assessments, Installation Technicians, Contractors, Installers and Project management teams". The page goes on to set out the size of advertisements ranging from 3m x 3m to 18.3m x 4.6m, but also that it covers "wraps" usually attached to scaffolding whose size is determined by the specific site dimensions. These "wraps" may advertise the site owners' message or be used by others.

25. As to "Sales" the appellant says that having been on both the buying and selling side of contracts, it offers unparalleled expertise and expert knowledge of how "you can optimise your returns".

26. In his evidence in chief and in cross-examination by Mrs Pavely, Mr Talbot reiterated the point that he was "in the advertising business". He also said, in response to a question from Mrs Pavely whether the appellant's income comes from advertising that in some cases he takes "a piece of the action", in that the appellant may itself own or have an interest in a site or be entitled to some of the earnings from the site.

27. We accept Mr Talbot's evidence, both oral and in the form of the website pages, of what the appellant does, and that what it does is what it claims to do in those pages. (We should of course not be taken to be endorsing any claims made on the website as to how successful the appellant is at what it does or the quality of its services). And it is clear to us and we so find that by and large the appellant's clients are the owners of the site and not the potential advertisers.

Submissions

28. We need to relate the way the appellant's case has been put at various stages because it has varied and HMRC have tailored their submissions to meet the variations.

29. When HMRC first told Mr Talbot that an assessment charging over £18,000 would be made, Mr Talbot explained in an email of 11 September 2014 that he had no idea, and was not notified, of any changes in the appropriate percentage of turnover that the appellant should be paying by way of VAT under the FRS, and that he would have expected the VAT office to have made him aware. He referred to the appellant's "mistake".

30. On 2 October 2014 HSC wrote to HMRC on behalf of the appellant. In this letter they maintained that the appellant had been applying the correct rate "as it should fall under the Advertising category at 11% current rate …We appreciate that on the original application to join the flat rate scheme the Management Consultancy

category was mistakenly used and the company should have applied to change the category".

31. In the grounds of appeal section in the Notice of Appeal to this tribunal, the appellant said:

> "The company used the VAT flat rate percentage for advertising services because it purchased and sold advertising billboard space.
>
> HMRC have retrospectively applied the higher percentage for management consultancy.
>
> The director does not believe that the original choice of percentage was unreasonable and more closely fits the business. The Director of the company has checked with other businesses of the same type within the industry who are on the flat rate scheme and their flat rate calculation is set at 11%.
>
> The decision by HMRC goes against their standard practice and no reasonable officer could have reached such a decision."

32. In his presentation to the Tribunal, Mr Talbot accepted that he and HSC had made a mistake and had together incorrectly applied for the management consultancy percentage. He said that HMRC conducted a check on the VAT position of the appellant but, despite being informed of the actual activities, refused to apply the advertising flat rate retrospectively. He considered this decision incorrect as his activities had always only been in advertising, and that it was unreasonable of HMRC to decide that the management consultancy percentage should be used throughout.

33. He was, he said, told by HSC a few years after starting in the flat-rate scheme that he was applying 11% which was the flat-rate for advertising, and that HSC did not think there was any VAT problem. On that basis he argued that HSC and he did make a conscious decision to use the advertising category.

34. He had read HMRC's cases and gave us a copy of *AML Consulting Ltd v HMRC* [2012] UKFTT 474 (TC) ("*AML*") with his annotations of the parts which he considered relevant to his case.

35. His main point was that he (and HSC) had made a genuine mistake in the application form, and that to charge him over £18,000 for this mistake was very harsh.

36. HMRC in its skeleton argument argues:

> (1) Traders are expected to select the category appropriate to their main business activity. They are expected to make themselves aware of the consequences of choosing the wrong sector – VAT 733 Paragraph 4.2
>
> (2) The Regulations require that HMRC is notified of any changes affecting the percentage: the appellant did not do so. HMRC was entitled to assume that there had been no change in the appropriate category or percentage.
>
> (3) The appellant intentionally selected "Management Consultancy", as shown on its application form.

(4) The appellant correctly applied the percentages for management consultancy in its first few periods until the rate changed.

(5) Contrary to the grounds of appeal the appellant had not intentionally used the advertising percentages: it was pure coincidence that the rate for amendment consultancy before 2010 and continuing to be incorrectly used by the appellant, and the rate for advertising after 2010 was the same.

(6) The cases of *Mr & Mrs Morgan (t/a The Harrow Inn) v HMRC* VAT Decision 19671 ("*Morgan*") and *Archibald & Co Ltd v HMRC* [2010] UKFTT 21 (TC) ("*Archibald*") support HMRC's position. *AML*, though one where the appeal was allowed, does not help the appellant.

37. In summary HMRC argues that the appellant was admitted to the FRS on the self-selected basis of Management Consultancy, that choice is not unreasonable, there is no provision for retrospective amendment of the category, provided the selection was reasonable, and that the decision to assess was reasonable in the circumstances.

Discussion

Appeals and jurisdiction

38. We need first to clarify what precisely was before us. From the papers we can see that HMRC made two different decisions. First, as set out in their letter of 29 August 2014 to Mr Talbot, HMRC decided to make assessments on the appellant covering the periods 09/10 to 03/14 for VAT and interest. These assessments were made to recover VAT calculated by applying to the turnover the excess of what HMRC say was the correct percentage over the 11% used by the appellant. Much the same decision was set out in another letter of 23 September 2014.

39. On 7 October 2014 the same officer of HMRC, Mr Culbert, wrote to HSC in response to their letter of 2 October 2014. In this letter he refused to allow the appellant to use the advertising rate retrospectively.

40. In both cases the appellant was informed of its rights to a non-statutory reconsideration, a statutory review or an appeal to the tribunal.

41. No review of either decision was requested, and on 11 May 2015 the appellant notified an appeal to the Tribunal. In that form:

(1) The HMRC reference number was that quoted on all decision letters.

(2) The "date of decision" was given as 23 September 2014, ie the date of the second "assessment" decision letter.

(3) The amount of tax was shown as £18,060, the total of the assessments.

(4) The grounds of appeal are as set out in §31 above.

(5) The desired result is that "[t]he VAT assessment should be rescinded."

42. On the face of it, it appears that only the decision to assess is under appeal and before us. But we are anxious to ensure that the appellant is not deprived of a right to

appeal because of a poorly worded or incompetently completed notice of appeal to this Tribunal. The issue here is whether the appellant should be treated as bringing to the Tribunal an appeal against the HMRC decision of 7 October 2014 not to allow the advertising percentage to be used retrospectively. We note that in her skeleton argument Mrs Pavely addressed the issue of backdating (see §37), although the Statement of case prepared by another officer does not do so. Mr Talbot also addressed it (see §32). We have therefore decided that in accordance with the overriding objective in Rule 2 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 we will consider that there was also an appeal against the decision of 7 October 2014 and that it is before us.

43. At the hearing Mrs Pavely put forward a further legal authority in addition to the ones in her bundle, s 84 VATA, and in particular s 84(4ZA):

> "(4ZA) Where an appeal is brought—
>
> (a) against such a decision as is mentioned in section 83(1)(fza), or
>
> (b) to the extent that it is based on such a decision, against an assessment,
>
> 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."

Section 83(1)(fza) covers:

> "a decision of the Commissioners—
>
> (i) refusing or withdrawing authorisation for a person's liability to pay VAT (or entitlement to credit for VAT) to be determined as mentioned in subsection (1) of section 26B;
>
> (ii) as to the appropriate percentage or percentages (within the meaning of that section) applicable in a person's case."

44. Applying the subsection and the paragraph to the facts of this case, HMRC's case is that we cannot allow either appeal unless we consider that HMRC could not have been reasonably satisfied that there were grounds for the assessment or the decision on backdating.

45. We accept that if the assessment was based on a decision by HMRC as to the appropriate percentages (within the meaning in s 26B VATA) applicable in the appellant's case then it must stand unless it can be impeached on what are effectively judicial review grounds (see *HMRC v Burke* [2009] EWHC 2587 (Ch) at [21]). We accept that the decision of 7 October 2014 (backdating) also falls to be judged in accordance with s 84(4ZA) VATA if it is correctly classified as a decision within s 83(1)(fza)(ii) VATA.

Appeal against the assessment

46. But first we approach the appeal against the assessment on the basis that our normal full review jurisdiction applies, because if the appeal fails on that normal basis

we do not need to consider whether s 84(4ZA) VATA applies. Section 73(1) VATA provides that where:

> "… it appears to HMRC that …. returns are … incorrect, they may assess the amount of VAT due from him to the best of their judgment and notify it to him."

47. It is not necessary for HMRC to show that the returns are in fact incorrect to allow it to assess. But if on an appeal the appellant shows to our satisfaction that the return is in fact correct then we would uphold the appeal. We make this statement of the obvious because unlike the law applying to direct taxes, there is no explicit statement in VATA of the Tribunal's powers such as is in s 50 Taxes Management Act 1970.

48. We turn first to Part VIIA of the Regulations which establishes what must be shown in a VAT return where the FRS applies. Regulation 55D requires an FRS trader (which the appellant is agreed to have been) to account for "the appropriate percentage ("AP") of his relevant turnover" for each period as if it were output tax. Regulation 55H defines the AP as the percentage determined in accordance with (relevantly) that regulation and regulation 55K. Regulation 55(2) provides that the relevant AP is that specified in the Table (in regulation 55K) for *the category of business that the appellant is expected, on reasonable grounds, to carry on* in each relevant period.[2] [Our emphasis].

49. We note that the phrases in the regulations we have quoted appear also in s 26B VATA and the italicised phrase is also in s 26B(6)(a).

50. In our view the category of business specified in the Table in regulation 55K that the appellant expected to (and did) carry on at each relevant date was "advertising", and that it would have had obvious reasonable grounds to have used the AP for advertising. We consider that this is the natural consequence of our findings of fact about what the appellant does by way of business. We are fortified in this view by the HMRC Manual for the FRS which includes advertising consultants, advertising space providers and advertising services such as billposting in the heading "Advertising" (see table in §10). We have found as a fact that the appellant is an advertising consultant, and is involved in the other two activities even if it does not itself provide them directly. We also note that in its VAT Registration form it said against the box asking for a "Description of your current and/or indeed business activities" "Consultant for the advertising industry". Admittedly it immediately followed that putting "Management consultant activities" against the box

[2] The precise span of these periods is not relevant in this case, though it appears that there is one split period, 03/11, where an increased rate applies to turnover in the period 4 January to 31 March 2011 (see regulation 55B(3)). And in the period 06/10 there was a change at 3 June 2010 the end of the regulation 55JB reduction period requiring a spilt of turnover. We do not have the information to tell whether the assessments take this into account.

"Categorisation of your current and/or indeed business activities". What this shows is that the appellant has always regarded itself as being in the advertising business.

51. Mrs Pavely did, somewhat faintly, suggest that the appellant was correct (or to put it in statutory terms, had reasonable grounds) to describe itself as a management consultant, primarily because the appellant's website shows that it offers "project management services". Mr Talbot vehemently denied that he was in anything other than advertising, and said that any project management he provided was as part of his advertising business. We put to Mrs Pavely the question whether a major advertising agency such as, we suggested, Saatchi & Saatchi, or rather, in an effort not to base it on a real life business, Sterling Cooper Draper Price, was, in much of the work it was doing, providing management consultancy or project management to client businesses, but in relation not to the overall structure of the business and the way it is organised but only to that separate part of any business that is concerned with advertising and with promoting brands. Mrs Pavely did not demur from the proposition that those type of advertising agencies would be carrying on "advertising" in regulation 55K terms, not management consultancy (though she confessed to not being a viewer of *Mad Men*).

52. We consider that the management consultancy heading is not the correct one for this appellant, and that the entry in the application form was a mistake: it is in any event unlikely to have been a deliberate choice because the percentage for management consultancy was at all times greater than that for advertising. We would further hold that the appellant did not have reasonable grounds to describe itself as a management consultant.

53. HMRC argued that it was entitled to assume that there had been no change in the relevant AP as no notice was given under regulation 55N. We agree no such notice was given, but regulation 55N applies only where the AP applicable in a future period differs from that used up to then. In this case either the AP for advertising was applicable in all periods, or that for management consultancy was. Regulation 55N does not cover a case where the trader comes to the view that it has used the wrong AP.

54. We consider now the cases cited to us.

55. *Morgan* involved a business which carried on two different activities with different percentages the balance of which changed over the years. The issue was whether the business had notified HMRC of the change in the balance of activities. This is not the issue in this case and we do not get any help from the case.

56. *Archibald* does concern a case where the appellant seems to have made the wrong choice of category. The case involved HMRC's refusal to allow her to backdate the change in classification. The Tribunal held that the refusal was not unreasonable. By contrast, in *AML*, a case which also concerns backdating, the appeal was allowed because HMRC were held to have been unreasonable in its decision-making processes. We consider these cases further when we discuss the appeal against the refusal to backdate.

57. We have considered what in fact a flat-rate scheme trader might or should do to correct the position if it comes to the view that it has used a wrong, higher, percentage but is no longer in the FRS. The only thing we can think of is that it should make a claim to correct the error in future VAT returns under regulation 34(3) of the Regulations (which it can do where, as here, the total overdeclaration is less than £50,000). That has not happened in this case in relation to the periods in 2009 and 2010 when the advertising rate was less than the rate actually used by the company, and it appears that the appellant would now be out of time to make any such claim – regulation 34(1A)(a) giving a period of four years to make the correction.

58. If a flat-rate trader comes to the view that it has used a lower percentage than it should have, then it should equally make a voluntary disclosure and might expect to be assessed.

59. But in this case the appellant has come to the view that, quite by coincidence, it has used the right percentage for all periods in 2011 and subsequently. What HMRC has done is to ignore the appellant's representation that it has in fact used the correct rate for 2011 and later, and effectively held it to its original mistake and assessed it accordingly.

60. It seems to us that it is not possible to characterise the appellant's VAT returns as having understated liability or being in any way incorrect for the periods for which assessments have been made. For those periods the requirement on the trader in regulation 55D, read with regulations 55H and 55K, is to account on the basis of using the percentage that is appropriate to the business expected, on reasonable grounds, to be carried on at the times when that question has to be judged, ie at the start of each period containing the anniversary of the trader's start date, which in this case is 1 April 2010 onwards. On any objective view of the matter the appropriate percentage is the one it has used. It cannot even be said that from the outset "advertising" was not thought by the appellant to be the business it was in as it is mentioned its VAT Registration application which was contemporaneous with the FRS application form.

61. As a result in our view the appellant had reasonable grounds at all relevant times to expect that its business of advertising would be carried on after each of those times. We therefore consider that the assessments are not justified and should be cancelled, at least if the normal full review approach to appeals applies.

62. Having come to the conclusion that the assessments are not justified on the normal basis, we have to go back to s 84(4ZA) VATA. Are the assessments based on a decision as to the appropriate percentage in the appellant's case? The assessments are based on the discovery by HMRC that the company did not increase the percentage that it used when two statutory instruments increased the rates applicable to all categories of business in order to ensure that the rates remained in accordance with Art 281 of the PVD when the UK increased its VAT rates. It seems to us that this is not the kind of decision that s 84(4ZA) is aimed at: rather it is aimed at cases where a trader has used a percentage that is not the appropriate percentage for the business it is actually carrying on or was reasonably expecting to carry on at the

relevant date. We base this opinion about s 84(4ZA) on two grounds. One is the fact that s 84(4ZA) dates from 2002 when the FRS was introduced, and at that time of course there was no question of there being any general increase in the percentages applying to every category. There was however then, and there still is now, clearly a possibility of a trader using the wrong percentage for its actual business.

63. The second matter is this. A supervisory jurisdiction over HMRC decisions is generally applied in VATA to cases where HMRC has some form of discretion in the way it exercises a power[3]. Thus a decision about whether to allow backdating of an application to be in the FRS is such a decision. But the change in percentages which the assessment in this case seeks to recover is not something over which anyone has any discretion: it is the result of a change in the law made mandatory by Art. 281 PVD and applying to every trader in the FRS, not a discretion vested in HMRC.

64. And in fact these considerations lead us to question what is the decision that HMRC have made on which the assessments are based. The answer it seems to us is that they have based the assessments not on a decision at all and certainly not one made by *them* as to the relevant percentage. The only decisions as to a percentage here were made by the House of Commons which decided not to object to the two statutory instruments concerned when they were laid before them[4].

65. We add here that we do find it difficult in any event to see where HMRC are empowered to make a decision "as to the appropriate percentage or percentages applicable in a person's case". HMRC go to some lengths to stress that the FRS is a self-assessment system where it is up to the trader to choose the percentage it considers the most appropriate. We can see nothing in s 26B VATA or Part VIIA of the Regulations which refers to HMRC (making the transposition required by the Commissioners for Revenue and Customs Act 2005) doing anything that might amount to a decision or determination as to the percentages. Where a power to make decision is not clearly set out in the law it may well be reasonable to regard a decision so made as one to which a full review jurisdiction might apply, if the effect of the decision is to alter a trader's VAT position. But it seems an odd (and some might say unacceptable) situation that what is in effect an unappealable decision (except on judicial review type grounds) is not one that can be clearly discerned from the statutory provisions.

66. We therefore hold that s 84(4ZA) does not apply to the assessments. We note that in *Pryor v HMRC* [2015] UKFTT 545 (TC) this tribunal (Judge John Brooks and Ruth Watts Davies) held that s 84(4ZA) did apply where a trader had not followed the

[3] The subsections of s 84 VATA which provide for a supervisory jurisdiction for this Tribunal are (4), (4ZA), (4A), (4C), (4D), (7) and (7ZA). The only one which arguably does not contain a discretionary element is ss (4) dealing with a determination by HMRC where it appears that input VAT is claimed in relation to something in the nature of a luxury, amusement or entertainment.

[4] It could be argued, though it would be extremely casuistic to do so, that because Dave Hartnett (as to both) and Bernadette Kenny and Steve Lamey (one each) made the statutory instruments which increased the percentages generally in this case the decision on which the assessments were based was a decision of HMRC.

increase introduced by SI 2010/2940. We are not bound by that decision and do not follow it for the reasons we have given in §62 to §64.

67. If however we are wrong about this, then we would have to consider whether the decision on which the assessment is based is one where HMRC could not reasonably have been satisfied that there were grounds for the decision. In *Pryor* the Tribunal noted:

> "As Lord Phillips MR (as he then was) said, at [40] of *Lindsay v HMRC* [2002] STC 588 in regard to whether a decision was one that could reasonably have been reached:
>
> > '… the Commissioners will not arrive reasonably at a decision if they take into account irrelevant matters, or fail to take into account all relevant matters'"

In this case we do not think that HMRC have shown that they took into account *all* relevant matters. The appellant disclosed on its VAT Registration form that it was a consultant to the advertising industry and when Mr Culbert, the relevant officer of Revenue and Customs, made an assurance visit to consider the appellant's first return after its leaving the FRS, he must have become aware that the appellant's business was advertising, not management consultancy, and in our view he should at the very least have looked at the appellant's website before making a visit. Since the assessments were made and objected to, HMRC have never seriously disputed the appellant's categorisation of his business. We note, and take some comfort, from the decision in *AML* where this tribunal (Judge Lady Mitting and Mr Blain) held that a decision not to backdate was flawed because among other things the decision-making officer there did not take into account the reasonableness of the original choice of category and percentage.

68. We have therefore decided to uphold the appellant's appeal against the assessments.

The decision to refuse backdating

69. We first need to consider whether the decision made by Mr Culbert on 7 October 2014 is appealable and is a decision to which s 84(4ZA) applies. Section 83(1)(fza)(i) allows an appeal against a decision:

> "refusing or withdrawing authorisation for a person's liability to pay VAT (or entitlement to credit for VAT) to be determined as mentioned in subsection (1) of section 26B"

Neither of these is the case here. Sub-paragraph (ii) allows an appeal against a decision:

> "as to the appropriate percentage or percentages (within the meaning of [section 26B]) applicable in a person's case."

One possible reading of the decision is that HMRC are, by refusing the claim to backdate, deciding that the appropriate percentage for periods before 2010 remained at 11% (the management consultancy percentage) so that s 83(1)(fza)(ii) is engaged.

This seems to us to be a strained reading, but if it is correct then s 84(4ZA) will apply and we consider that subsection on the assumption that it is correct.

70. We note that Mr Culbert, the officer making the 7 October 2014 decision and the same officer who made the earlier decision to assess, was clearly aware of the appellant's contention that advertising was always the correct category, and that the description of the business as a management consultancy was a mistake. The reasons Mr Culbert gave for refusing to backdate are:

> (1) A letter sent to the appellant when it applied to join the scheme "clearly states that … HMRC should be advised if the flat rate sector classification is incorrect or changes", and that the appellant did not so notify.
>
> (2) Public Notice 733 … para 4.2 "clearly states that HMRC will not retrospectively change the Flat rate sector that the business has chosen".

71. The letter sent to the appellant actually says: "Remember to notify us at the above address if your business changes so that it falls within a different flat rate sector or you are no longer eligible to use the flat rate scheme." It says nothing about notifying a case if the classification is incorrect.

72. VAT Notice 733 at 4.2 says:

> "**4.2 What if I get the sector wrong?**
>
> We will not normally check your choice of sector when we process your application. So if you have made a mistake you may pay too much tax or too little. Paying too little could mean that you are faced with an unexpected VAT bill at a later date.
>
> However, if we approve you to join the scheme, we will not change your choice of sector retrospectively as long as your choice was reasonable. It will be sensible to keep a record of why you chose your sector in case you need to show us that your choice was reasonable.

73. This clearly says that retrospection is not possible *if the original choice was reasonable*. As the Tribunal points out in *AML* at [16], to say what Mr Culbert says here, which is what HMRC said in *AML*, is not a correct interpretation of the policy of HMRC.

74. In our view Mr Culbert failed to take into account the evidence that he had and should have had that the business was advertising and the appellant's representations, and he took into account two things which he should not have so taken, that HMRC would not retrospectively change a classification, when in certain circumstances they clearly would, and that the appellant was under an obligation to notify HMRC of a "change".

75. On this basis we find the decision unreasonable and uphold the appeal. It is not possible for us to say that had he taken into account all that he should have and not taken into account all that he shouldn't have, he would inevitably have come to the same decision. *Archibald* is not relevant as it was decided on the particular facts of that case, and is not in any event binding on us.

76. In any event it seems to us that the decision of 7 October is without consequences unless HMRC go on to either make an assessment or refuse a claim under eg s 80 VATA for periods in 2009 and 2010.

77. Our decision on this backdating aspect of the appeal might in theory give the appellant a right to claim a refund for the periods when 11% (or 10% under regulation 55JB) was actually higher than the advertising rate (ie before 2011) but we suspect it would be out of time.

Decision

78. The appeal against the assessments to VAT and interest are upheld, the decision is cancelled and the assessments discharged.

79. The appeal against the decision not to backdate is upheld and the decision is cancelled.

80. 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. The interest assessed was £1130.84.

RICHARD THOMAS
TRIBUNAL JUDGE

RELEASE DATE: 30 DECEMBER 2015