[2017] UKFTT 563 (TC)

TC06005

Appeal number: TC/2016/04840

VAT – Appeal against penalty for failing to notify HMRC of liability to be registered for VAT – Schedule 41 Finance Act 2008 – Whether mistaken belief that goods were zero rated is a reasonable excuse or special circumstance

FIRST-TIER TRIBUNAL
TAX CHAMBER

NATHANIEL HENDRICKSON **Appellant**

- and -

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

TRIBUNAL: JUDGE CHRISTOPHER STAKER
MR ANDREW PERRIN FCA

Sitting in public at Cardiff on 8 May 2017

The Appellant in person assisted by his friend Mr Roland Brana

Mr Janic-Karim Nathoo for the Respondents

DECISION

Introduction

1. The Tribunal gave its decision in this appeal orally at the hearing, and issued a short form decision notice. Full reasons were subsequently requested by the Appellant, and are now provided.

2. The Appellant appeals against a penalty under Schedule 41 of the Finance Act 2008 ("FA 2008") for failing to notify HMRC of his liability to be registered for VAT.

Background facts

3. In 2015, HMRC looked into the Appellant's tax affairs. In a letter dated 7 December 2015, HMRC advised the Appellant's accountants that the matter would be referred to a colleague for a review of the VAT position.

4. In a letter to the Appellant dated 15 December 2015, HMRC advised that on the basis of the information available, the Appellant was required to notify HMRC of his liability to be registered for VAT not later than 30 October 2012, and that he ought to have registered for VAT on 1 November 2012. The Appellant was further advised that he may be liable to a penalty under Schedule 41 to the FA 2008, and was invited to contact HMRC.

5. In a letter to HMRC dated 22 December 2015, the Appellant's accountant advised that the Appellant was aware that once his sales reached £77,000 in 2012-13 he was required to register for VAT. However, his internet researches indicated that protective clothing was exempt, and he considered that all the motorbike protective clothing he sold was therefore exempt. He therefore considered that he did not need to register. The supplier of the motorcycle protective clothing that he sold also assured him that it was VAT exempt. All of the gear that he sold was kite marked and sold as protective clothing. He did not avoid paying VAT and did not charge his customers VAT. He took reasonable steps in the circumstances to satisfy himself that as all his supplies were exempt he did not need to register.

6. A letter from HMRC to the Appellant's accountant dated 26 January 2016 stated that the only items that could attract zero rating would be motor cycle helmets, and that zero rating does not apply to adult protective clothing. The Appellant was asked to refer to specific provisions of the VATA if he considered that other items were zero rated. The Appellant's accountant was asked to provide further details of monthly sales.

7. On 25 February 2016, the Appellant's agent provided HMRC with the Appellant's monthly turnover figures for April 2012 to September 2014.

8. In a letter to the Appellant's accountant dated 11 March 2016, HMRC advised that based on these figures, the Appellant should have been registered for VAT for the period 1 November 2012 to 30 September 2014, and that HMRC were considering the Appellant's liability to a penalty. The Appellant was invited to submit further information.

9. In an "FTN Penalty Reply Slip" completed by the Appellant on 22 March 2016, the Appellant stated that he had been assured by several people that motorcycle protective clothing was not subject to VAT, but he acknowledged that he "only took informal advice from supplier and a business acquaintance".

10. On 25 April 2016, the Appellant's accountant informed HMRC that they had recalculated the amount of VAT due for the period in question to be £23,962.25. The accountant added that the Appellant "did not charge VAT on his sales, made very little profit, has no assets and earns about £15,000 per annum".

11. On 13 May 2016, HMRC's VAT Registration Service wrote to the Appellant to confirm to him that he should have been registered for VAT for the period from 1 November 2012 to 30 September 2014, and advised him that the amount due for that period was assessed under s 73 VATA to be £23,962.25.

12. On 26 May 2016 HMRC sent to the Appellant a notice informing him that they intended to impose a penalty under Schedule 41 to the FA 2008 in the sum of £4,792.45. The notice explained that the failure to register for VAT was considered to be non-deliberate, and that the disclosure was considered to be prompted. Accordingly, the minimum penalty under Schedule 41 to the FA 2008 was 20% of the potential lost revenue. The notice stated that HMRC proposed to impose a penalty in the minimum amount of 20%. HMRC did not consider that there were any special circumstances justifying a special reduction.

13. In a letter dated 7 June 2016, the Appellant wrote to HMRC stating that he genuinely believed that the items were VAT exempt, that he did not receive VAT payments and could not be in a position to pay money he did not receive, that he had now given up establishing his own business and had now taken out a full time low paid job, and that he had made a fatal error which he would never make again.

14. On 28 June 2016 HMRC issued the Appellant with a notice of penalty assessment in the amount previously proposed.

15. On 3 July 2016, the Appellant requested a review.

16. In a review decision dated 24 August 2016, HMRC confirmed that the Appellant was liable to be registered for VAT in the period in question, and confirmed the assessment and the penalty.

17. In a notice of appeal dated 12 September 2016, the Appellant appealed to this Tribunal.

Applicable legislation

18. Paragraph 1 of Schedule 1 of the Value Added Tax Act 1994 ("VATA") at material times relevantly provided that a UK-established person who made taxable supplies but was not registered under the VATA became liable to be registered under that Schedule if, at the end of any month, the value of his or her taxable supplies in the period of one year then ending had exceeded the registration threshold.

19. Paragraph 5 of Schedule 1 VATA provided that a person who becomes so liable to be so registered shall notify HMRC of that liability within 30 days of the end of the relevant month.

20. Paragraph 1 of Schedule 41 to the FA 2008 provides that a penalty is payable by a person who fails to comply with the obligation under paragraph 5 of Schedule 1 VATA.

21. Paragraph 6 of Schedule 41 to the FA 2008 sets out the amount of the standard penalty for a breach of paragraph 1 of that Schedule. In the case of a "Category 0" failure, if the failure is not deliberate and not concealed, the standard penalty is 30% of the potential lost revenue. "Potential lost revenue" is defined in paragraph 8 of that Schedule.

22. Paragraphs 12(1)(a) and 13 of Schedule 41 to the FA 2008 provide for reductions in the standard penalty where there has been a disclosure. The reduction depends on whether the disclosure is promoted or unprompted. Paragraph 12(3) provides that a disclosure is unprompted if made at a time when the person making it has no reason to believe that HMRC have discovered or are about to discover the relevant act or failure, and otherwise it is prompted. Under paragraph 13(2)-(3) and the accompanying table, the minimum standard penalty that can be imposed for a prompted disclosure in a case where HMRC becomes aware of the failure more than 12 months after the time that the tax first became unpaid by reason of the failure is 20% of the potential lost revenue.

23. Paragraph 14 of Schedule 41 to the FA 2008 provides that HMRC may reduce the penalty under paragraph 1 if HMRC "think it right because of special circumstances".

24. Paragraph 20 of Schedule 41 to the FA 2008 provides that a person is not liable to a penalty under paragraph 1 for a failure that is not deliberate if there is a reasonable excuse for the failure.

25. Paragraphs 17 to 19 of Schedule 41 to the FA 2008 provide for an appeal to the Tribunal against a decision of HMRC imposing a penalty. However, in any such appeal the Tribunal may rely on paragraph 14 of Schedule 41 to a different extent only if the Tribunal thinks that HMRC's decision is flawed when considered in the light of the principles applicable in proceedings for judicial review.

The Appellant's evidence

26. At the hearing, the Appellant was assisted in the presentation of his case by his friend Mr Brana. Witness evidence was given by both the Appellant and Mr Brana, in which they said amongst other matters as follows.

27. The Appellant was very interested in motorcycles. He was not a businessman. He decided to try to make some money selling motorcycle clothing on eBay. There are many small eBay traders. Unlike the US eBay site, there is nothing on the UK eBay site that warns small traders when they are approaching the VAT threshold. The Appellant began in 2001 selling motorcycle helmets. Then he stopped and began again in 2012 selling motorcycle clothing (trousers and jackets) but no helmets. He reached the VAT threshold in 2012. At that time Mr Brana raised with the Appellant

the question whether he was subject to VAT and the Appellant said that he was not. If a Google search is done on protective motorcycle clothing, the top result suggests that it is zero rated. The Appellant's budget would not allow for professional help. When an accountant was subsequently consulted, she also thought that the items were zero rated.

The Appellant's submissions

28. The Appellant was badly advised when he was told that protective clothing was zero rated. He has never run a business and has no background in business or VAT laws. He never made any financial gain by not charging VAT to eBay buyers. He now has a full time job working for the minimum wage. He does not own a car, does not own his own home, has no savings, did not knowingly avoid paying VAT, and deeply regrets making a mistake. Every HMRC officer agrees that his behaviour was non-deliberate. It was a careless error for him to take advice from a well-established businessman and not contact HMRC. He kept records and made them available to HMRC. He stopped selling immediately (September 2014) when these issues came to light, so that he would not be causing further problems with VAT.

29. When the Appellant first contacted his accountant in 2015 after HMRC began looking into his tax affairs, his accountant had agreed with his assessment that protective motorcycle garments were not subject to VAT. Subsequently his accountant said that the type of garments sold by the Appellant were in fact VAT standard rated, and she apologised for this oversight. The Appellant cannot be blamed for making a mistake if a professional accountant could make the same mistake.

The HMRC submissions

30. There is no right of appeal against the assessment, as opposed to the penalty. Under s 83(1)(p)(i) VATA an appeal against an assessment made under s 73(1) can only be made where the Appellant has made a return as required by the VATA. In the 13 May 2016 HMRC letter, the Appellant was given the opportunity to make a return covering the whole of the period for which the Appellant should have been registered, but the Appellant did not take up this offer.

31. The penalty has been imposed in accordance with the legislation. HMRC has given maximum reduction to the standard penalty to reflect the Appellant's cooperation. The Appellant has no reasonable excuse for the failure, and there are no special circumstances justifying a special reduction.

The Tribunal's findings

32. The Appellant has no right of appeal against the assessment, for the reasons given by HMRC. In any event, the assessment was based on the figures supplied by the Appellant's own accountant on 25 April 2016.

33. The Appellant has not sought to argue that he was not required to register for VAT from 1 November 2012 to 30 September 2014. On the material before it, the Tribunal is satisfied that he was.

34. This is a Category 0 case. The Appellant's failure to register for VAT was not deliberate. The failure was not concealed. However, his disclosure of that failure was prompted: it was made only as a result of HMRC enquiries into his affairs.

35. The Tribunal is satisfied that HMRC became aware of the failure more than 12 months after the time that the tax first became unpaid by reason of the failure. If he had been registered for VAT from 1 November 2012, his first VAT return and VAT payment would have been for the period 1 November 2012 to 31 January 2013, and the first VAT payment would have been due on 28 February 2013. There is nothing to suggest that HMRC were aware of the failure prior to March 2013.

36. In the circumstances, the minimum penalty that can be imposed is 20% of the potential lost revenue of £23,962.25.

37. The penalty was in fact imposed in this minimum amount. The Tribunal is accordingly satisfied that the penalty has been correctly imposed in accordance with the legislation.

38. The Tribunal has considered whether the Appellant has a reasonable excuse for the failure.

39. The Tribunal accepts that the Appellant was not a businessman, had never run any other business and has no background in business or VAT laws, was a small eBay trader, did not have the resources for professional help, did not charge VAT and made no financial gain himself by not charging VAT, did not deliberately avoid paying VAT, regrets making a mistake, and has very limited personal resources. For purposes of this appeal, the Tribunal also accepts that his own accountant initially told him that the items he was selling were zero rated before subsequently telling him that this was mistaken.

40. However, the fact that the Appellant's behaviour was not deliberate is already one of the factors used in Schedule 41 to the FA 2008 for determining the level of the penalty. Given that the non-deliberate nature of the failure has already been taken into account in determining the level of the penalty, the Tribunal finds that it cannot then be relied on a second time as amounting to a reasonable excuse or special circumstances.

41. The Appellant acknowledges that he was aware, at the time that he reached the VAT registration threshold in 2012, that this was the case (see paragraphs 5 and 27 above). He thus understood at the relevant time that VAT law was potentially applicable to him, and that he had reached the VAT registration threshold. The circumstance that he relies upon as amounting to a reasonable excuse is thus simply that he was not aware that the particular items he was trading were standard rated rather than zero rated.

42. The Tribunal has considerable sympathy for the Appellant, given the matters referred to in paragraph 39 above. However, despite these matters the Appellant will not have a reasonable excuse unless he can establish that it was reasonable for him in all the circumstances to believe that the items he was trading were zero rated. The circumstances invoked by the Appellant are essentially an "ignorance of the law"

excuse. However, it is well established that ignorance of the law is generally not a reasonable excuse.

43. The Appellant says that he was told by his supplier, and by a reputable business person he asked, that the items were zero rated. However, little information has been supplied as to who his supplier or the businessperson were, or exactly what they told him or in what terms. Normally, the fact that an appellant has been given erroneous legal advice by a third party such as a supplier or a friend or acquaintance (even one who is considered knowledgeable) is not a reasonable excuse.

44. The Appellant says that his accountant at first also advised him that the items were zero rated. However, even if this is so, this advice was given by the accountant after the period in which the Appellant should have been VAT registered had already ended. That advice therefore cannot be the reason for the Appellant's failure. The Appellant's argument is simply that he cannot be blamed for making a mistake if a professional accountant could make the same mistake. However, the Tribunal is not persuaded by this logic. The question whether these items were standard rated or zero rated was not a complex legal question that only a specialist could understand. The question is whether the Appellant, at the time of the failure, was reasonably entitled to have believed that the items were zero rated. If he was not, that fact is not altered by the fact that a professional accountant made the same mistake as him.

45. The Tribunal considers that a reasonable trader would have considered all items to be standard rated, unless there were particular reasons for believing that a different treatment applied. Apart from what the Appellant says he was told by his supplier and a businessperson, the only basis for the Appellant's belief appears to be the fact that he previously had sold motorcycle helmets that were zero rated, and the fact that he seemed to have a general belief that protective clothing in general was zero rated. The Tribunal is not persuaded that the mere fact that motorcycle helmets are zero rated would make it reasonable to believe that all motorcycle protective clothing is zero rated. Furthermore, the Appellant has not established a reasonable basis for a belief that all protective clothing is zero rated.

46. At the hearing, it was argued on behalf of the Appellant that a Google search on the VAT treatment of protective clothing will return results suggesting that such items are zero rated. In fact, such a Google search will return a link to VAT notice 701/23, "Protective equipment", published 4 July 2011, which is to say, published before the commencement of the period in which the Appellant should have been VAT registered. This document states that motorcycle helmets and protective boots and helmets for industrial use are zero rated if certain requirements are met. The document states that "Boots and helmets that meet all the other conditions for zero-rating but are not for industrial use, such as motorcycle boots, are standard-rated". The document states that pedal cycle helmets are zero-rated and that children's car seats and travel systems are reduced-rated at a rate of 5% VAT. It states at section 1.1.1 that other protective equipment is not specifically reduced or zero rated, but that "certain protective clothing, headgear and footwear for young children may be zero-rated as young children's clothing and footwear". There is nothing in this document that suggests that motorcycle trousers or jackets, which are the items that the Appellant was selling, were zero rated. The document in fact indicates the very opposite.

47. The Appellant has acknowledged that he did not contact HMRC before proceeding on the assumption that the goods he traded were zero rated. Thus, even if "reasonable ignorance of the law" could be a reasonable excuse (and the Tribunal does not reach any decision that it can be), the Tribunal is not satisfied that the Appellant's ignorance of the law was reasonable, even taking into account his lack of resources to engage professional advice and the other matters referred to in paragraph 39 above. The Tribunal is not persuaded that the Appellant's belief that the items were zero rated was reasonable in all the circumstances.

48. The Tribunal therefore considers that the Appellant does not have a reasonable excuse for the failure.

49. The HMRC penalty decision appealed against found that there were no special circumstances justifying a special reduction. The Tribunal finds that this decision is not flawed when considered in the light of the principles applicable in proceedings for judicial review. However, even if it was, the Tribunal would itself find, notwithstanding its sympathy for the Appellant's circumstances, that the circumstances relied on by the Appellant do not amount to special circumstances within the meaning of paragraph 14 of Schedule 41.

Conclusion

50. For the reasons above, this appeal is dismissed.

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

DR CHRISTOPHER STAKER
TRIBUNAL JUDGE

RELEASE DATE: 13 JULY 2017