[2015] UKFTT 0545 (TC)

TC04702

Appeal number: TC/ 2014/03717

VAT – Flat Rate Scheme – Assessment for under declaration as a result of application of incorrect percentage – Refusal to allow retrospective withdrawal from Flat Rate Scheme – Whether reasonable – Yes – Appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

JOHN DAVID PRYOR
t/a PURFLEET POST OFFICE **Appellant**

- and -

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

TRIBUNAL: JUDGE JOHN BROOKS
RUTH WATTS DAVIES

Sitting in public at Fox Court, Brooke Street, London EC1 on 19 October 2015

Mrs Anne-Marie Pryor for the Appellant

Barry Sellers of HM Revenue and Customs, for the Respondents

DECISION

1. Having orally announced our decision to dismiss the appeal, and after Mr Barry Sellers who had represented HM Revenue and Customs ("HMRC") had left the hearing room, Mrs Anne-Marie Pryor, who represented her husband Mr John David Pryor, asked whether an appeal would be possible. The parties had agreed (pursuant to rule 35(3) of the Tribunal Procedure (First-tier Tribunal)(Tax Chamber) Rules 2009) that it was unnecessary for full or summary findings of facts and reasons for the decision to be provided. However, as rule 35(4) of the Procedure Rules requires there to be a decision containing full written findings of facts and reasons before an application for permission to appeal can be made, this decision has been provided in order to enable Mr Pryor to decide whether to apply for permission to appeal and to assist him in formulating any such appeal.

2. This appeal concerns the operation of and withdrawal from the fixed rate scheme ("FRS"). In simple terms, the FRS is a scheme which allows traders within specific turnover limits to pay VAT as a percentage of their turnover rather than calculating the output and input the VAT on sales and purchases. In particular, Mr Pryor, who trades as Purfleet Post Office, appeals against:

(1) A VAT assessment in the sum of £13,869 being under declared output VAT for the VAT 05/10 to 01/13 accounting periods which arose as a result of the application of the incorrect "appropriate percentage" under the flat rate scheme ("FRS"); and

(2) The refusal of HM Revenue and Customs ("HMRC") to agree to allow him to backdate his application to withdraw from the FRS.

3. Before considering the relevant legislation applicable to the FRS it is first convenient to set out the background which led to the appeal.

Background

4. On 16 January 2007 Mr Pryor successfully applied to HMRC to use the FRS with effect from 1 October 2006, the date of his VAT registration. In the application he described his main business activity as "retailing food, confectionary, tobacco, newspapers, or childrens clothing" which had an applicable FRS percentage for this business activity was 2%.

5. On 10 February 2014 HMRC contacted Mr Pryor to notify him, as part of its standard compliance procedure, that his VAT returns for the periods 02/10 to 11/13 would be subject to a check to ensure that he was correctly operating the FRS and requested information in this regard. Mr Pryor responded on 16 February explaining that he ran a post office with a retail outlet and used the 2% as the percentage rate for the FRS based on the business activity detailed on his FRS application.

6. However, during a discussion on 4 March 2014 HMRC informed Mr Pryor that although there was a specific FRS category for Post Offices, as the retail side of the

business accounted for the higher turnover, the business was correctly categorised but that the appropriate FRS percentage for this type of business had increased from 2% to 4% from 4 January 2011 as a consequence of the increase in the standard rate of VAT from 17½% to 20% by virtue of the Value Added Tax (Amendment)(No 3) Regulations 2010.

7. In a letter dated 6 March 2014 from HMRC Mr Pryor was informed that because the incorrect FRS percentage had been applied there was an under declaration of VAT amounting to £13,869 (the VAT which would have been due had the correct percentage been applied). Mr Pryor wrote to HMRC on 8 March 2014 to withdraw from the FRS and following further correspondence between the parties, which addressed the issue of whether HMRC should have notified Mr Pryor of the change in the applicable FRS percentage, on 24 April 2014 HMRC issued an assessment to recover the under declared VAT. The assessment was upheld following a review and Mr Pryor informed of this by a letter from HMRC dated 10 June 2014.

8. On 5 July 2014 Mr Pryor appealed to the Tribunal.

9. During the initial hearing of the appeal on 20 February 2015 it was directed by Judge Mosedale, with the consent of the parties, that the appeal would be adjourned to give Mr Pryor time to make an application under paragraph 55M(g) and paragraph 55Q(e) of the VAT Regulations 1995 to be retrospectively removed from the FRS. Such an application was made by Mr Pryor on 23 February 2015. However, this which was rejected by HMRC on 6 March 2015 on the basis that there were no exceptional circumstances which could justify a departure from their policy of refusing such applications.

10. Mr Pryor then appealed to the Tribunal and the appeal against HMRC's decision not to allow Mr Pryor to retrospectively withdraw from the FRS was, as directed by Judge Mosedale, heard together with the appeal against the assessment.

Law

11. Under s 26B of the Value Added Tax Act 1994 ("VATA") HMRC may make regulations dealing with the operation of the FRS and have done so in the VAT Regulations 1995 (and all further references to Regulations are to these Regulations).

12. Insofar as applicable to the present case Regulation 55D provides:

> 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.

13. Although Regulation 55JB is not applicable in the present case Regulation 55H(1) is, this states:

> 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.

14. Regulation 55K provides:

> (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.
>
> (2) …
>
> (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.

15. A table in Regulation 55K sets out various categories of business and the appropriate percentage. This shows that the appropriate percentage for a Post Office is 5% and for "Retailing food, confectionary, tobacco, newspapers or children's clothing (as in this case) 4%.

16. Provision for withdrawal from the FRS is contained in Regulation 55M. Insofar as applicable to the present case this provides:

> (1) Subject to paragraph (2) below, a flat rate trader ceases to be eligible to be authorised to account for VAT in accordance with the scheme where –
>
> …
>
> (g) he opts to withdraw from the scheme …

As for the date of withdrawal Regulation 55Q provides;

> (1) The date on which a flat rate trader ceases to be authorised to account for VAT in accordance with the scheme shall be—
>
> …
>
> (e) where regulation 55M(1)(g) applies the date on which the Commissioners are notified in writing of his decision to cease using the scheme, or such earlier or later date as may be agreed between them and him …

17. Section 83(fza) VATA gives a trader a right of appeal to the Tribunal in respect of a decision by HMRC refusing or withdrawing authorisation to use the FRS. Under s 84(4ZA) VATA the Tribunal's jurisdiction on such appeals is limited to examining the reasonableness of the Commissioners' decision. It provides

> Where an appeal is brought —
>
> (a) against such a decision as is mentioned in section 83(fza), or

> (b) to the extent that is based on such a decision, against an assessment,
>
> the tribunal shall not allow the appeal unless it considers that the Commissioners could not reasonably have been satisfied that there were grounds for the decision."

18. 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"

Discussion and conclusion

19. Mrs Pryor, who accepts that her husband applied the incorrect FRS percentage and did not dispute the amount of the assessment, nevertheless contends that he should not be required to pay the additional VAT assessed as HMRC had failed to notify him of any change in the appropriate percentage for his trade sector. She described how she receives an email from HMRC every quarter to remind her when a VAT return is dues and contends that, as a matter of fairness, a similar system should have been in place with regard to any changes in the FRS percentage rates.

20. She also submits that it was unreasonable of HMRC not have checked the returns earlier and that the failure to do so has resulted in £13,869 being payable when it could have been a lower amount or even no payment due and says that had Mr Pryor not applied the FRS his VAT liability would have been lower than it was in the scheme.

21. With regard to the application to retrospectively withdraw from the FRS, Mrs Pryor emphasised the hardship caused as a result of the payment of the assessment and argues that this amounts to an exceptional circumstances which should have resulted in HMRC agreeing to the application.

22. For HMRC, Mr Sellers referred to the appropriate regulations and reminded us that the FRS percentages are laid down by Parliament and that HMRC have no control over them or any amendments that are made. He submits that there is no obligation on HMRC to notify traders of any changes to the appropriate FRS percentages rather it was for a trader to avail himself of the information available on HMRC's website as VAT is a self-assessing tax.

23. Although Mr Sellers accepts that Mr Pryor's liability to VAT was greater when operating the FRS he submits that this does not invalidate the scheme referring us to the following observations of the Tribunal (Judge Aleksander and Ms Bridge) at [7] of their decision in *Reynolds v HMRC* [2010] UKFTT 40 (TC):

> "The mere fact that a taxpayer will pay more tax under the flat rate scheme is not considered exceptional for these purposes. In our view this is a rational policy. The flat rate scheme is intended to provide a

> measure of simplification for small businesses, and is intended to be revenue neutral. The objective of the scheme is not to provide a mechanism for small businesses to pay less VAT – and this is clear from the provisions of the VAT Directive which allow member states to implement simplified VAT accounting arrangements for small businesses. The flat rate scheme is based on average rates of input VAT recovery for business sectors – and as it is based on averages, it is inevitable that some taxpayers will pay more (or less) than the average. If taxpayers were allowed to join or withdraw from the scheme retrospectively, then this would defeat the simplification objectives of the scheme. Taxpayers could "game" the system – and join the scheme on a "punt", and after three years review their input VAT and apply to withdraw from the scheme with retrospective effect if they found they would pay less VAT as a result."

24. Mr Sellers also relies on this passage from *Reynolds* to support his submission that HMRC acted reasonably in not agreeing to Mr Pryor's application to withdraw from the FRS retrospectively.

25. We agree with Mrs Pryor that it would be helpful if HMRC did issue email reminders to traders, as they do each quarter for VAT returns, advising of a change in the appropriate FRS percentage for their trade category. However, as any change in the appropriate percentage is likely to occur, as it did in this case, at the same time as a change in standard VAT rate, something which generates significant media coverage it is perhaps not surprising that there is no statutory obligation on HMRC to notify traders of such a change. Rather the onus is on the trader to ensure that he applies the correct FRS percentage.

26. Where an error is made, as in this case, the trader is clearly required to pay any VAT that has been under declared arising as a result. We understand that Mrs Pryor considers such a position to be unfair. However, it is clear from the decision of the Tax and Chancery Chamber of the Upper Tribunal in *HMRC v Hok Limited* [2012] UKUT 363 (TCC) (which considered whether a the Tribunal could reduce a penalty on grounds of "fairness" and which is binding on us) that this Tribunal does not have the jurisdiction to override a statute or supervise the conduct of HMRC.

27. With regard to the application to withdraw retrospectively from the FRS, although we appreciate that small businesses, such as that operated by Mr Pryor, may be in a worse financial position than they may otherwise have been had they not elected to apply the FRS, we agree with Mr Sellers and the Tribunal in *Reynolds* that this cannot amount to exceptional circumstances and, it follows, that neither can any hardship that arises as a result of the application of an incorrect FRS percentage.

28. As we have already noted (see paragraph 17, above) our jurisdiction in respect of Mr Pryor's application to withdraw from the FRS is limited. The issue for us is not whether Mr Pryor should have been allowed to retrospectively withdraw from the FRS (and it is not sufficient that we might ourselves have reached a different conclusion) but whether the decision taken by HMRC not to agree to such a retrospective withdrawal is one that could reasonably have been reached. Having regard to all the circumstance of the case we consider that it was.

29. Therefore, for the above reasons, we have no alternative but to dismiss the appeal.

Appeal Rights

30. 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.

JOHN BROOKS

TRIBUNAL JUDGE
RELEASE DATE: 23 OCTOBER 2015