[2018] UKFTT 0777 (TC)

TC06911

Appeal number: TC/2016/01454

VAT – Flat rate scheme – application to withdraw from scheme ab initio – invoiced supplies exceeding entry threshold for scheme – cash receipts always within threshold – correct method of calculating threshold – whether HMRC bound to agree to withdrawal ab initio

FIRST-TIER TRIBUNAL
TAX CHAMBER

APEX VEHICLE MANAGEMENT LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE MALCOLM GAMMIE CBE QC

Sitting in public at Taylor House on Tuesday 20 March 2018

Md Shahabuddin of Shahabuddin & Co (Chartered Accountants) for the Appellant

Ms Olivia Donovan, HMRC Litigator for the Respondents

© CROWN COPYRIGHT 2018

DECISION

1. Apex Vehicle Management Ltd ("the Appellant") appeals against the Respondents' refusal to allow it to withdraw retrospectively from the Flat Rate Scheme ("FRS") and against an assessment under section 73 Valued Added Tax Act 1993 ("VATA") to recover input tax of £40,625 and notified by letter on 6 November 2015.

2. The Appellant was registered for VAT with effect from 1 June 2012. Its trade classification was given as renting and leasing of cars and LMV. On 15 July 2013 it applied to join the Flat Rate Scheme ("FRS") with effect from 1 March 2013. The Respondents confirmed on 9 September 2013 that the Appellant was authorised to use the FRS with effect from the requested date. The Appellant's FRS application described its activity as accident vehicle management. Its business (or an element of it) was apparently to provide courtesy cars following accidents. The rate applicable to such activities was 9.5 per cent and the Appellant was entitled to a 1 per cent reduction to 8.5 per cent from 1 March 2013 to 28 February 2014.

3. On 17 September 2014, the Appellant's accountant wrote to the Respondents to notify them that in period 06/14 the Appellant claimed input tax of £16,104.83 in respect of three cars purchased for the purposes of its business. As a result, the return for the period showed a repayment claim of £14,350.13, which was duly processed on 23 September 2014. The Appellant sought confirmation that the input tax had been correctly treated. On 13 October 2014 the Respondents' Written Enquiries Team acknowledged the enquiry and indicated that it had been passed to the relevant team who would respond directly to the Appellant in due course.

4. On 15 October 2014, however, the Written Enquiries Team wrote again to the Appellant indicating that it had been agreed that it was best placed to provide the guidance requested. The letter drew the Appellant's attention to section 3 of VAT Notice 700/64 *Motoring Expenses* and also section 15 of VAT Notice 733 *Flat Rate Scheme for small businesses*. Section 15 of the latter publication provided guidance on capital expenditure goods and advised that such goods purchased to generate business income by being leased, let or hired should not be included in the VAT return and that input tax recovery was not permitted. The letter went on to advise how an error in a VAT return could be corrected.

5. Nothing further appears to have happened until the Appellant wrote on 1 September 2015 applying to cancel its participation in FRS with effect from 1 January 2015. No letter of that date was produced to me but as a result of a repayment claim made by the Appellant, one of the Respondents' Officers visited the Appellant's principal place of business on 9 September 2015. On his visit, the Officer was shown the letter of 1 September 2015 but it appears from correspondence in October 2015 that the letter had not appeared on the Appellant's file with the Respondents, suggesting that it had either not been sent or had never been received.

6. In any event, following his visit, the Officer concerned wrote to the Appellant on 13 September 2015 to confirm that if those concerned with such matters agreed to allow the Appellant to exit the FRS as requested, its VAT returns for 03/15 and 06/15 would require adjusting. The Officer requested that the Appellant produce 12 vehicle purchase invoices for the period 06/15 and provide the annual turnover figures to which it had apparently referred in its letter of 1 September 2015 together with a reconciliation with the income declared using the cash accounting scheme. Finally, the Officer asked for confirmation of the business' funding given that the last four VAT returns had shown expenditure of £329,737 against net income of £85,476.

7. On 16 October 2015, the Officer wrote to the Appellant again, noting that the Respondents did not have a record of the Appellant's request to be moved from the FRS and also requesting a reply to his letter of 13 September 2015. The Officer suggested that the letter of 1 September 2015 should be resent but noted that it incorrectly stated that the turnover limit for FRS had been exceeded on 31 December 2014. He pointed out that as the business was cash accounting, the FRS turnover should be calculated using the cash accounting turnover figure and that the Appellant had not exceeded that limit on 31 December 2014. He suggested that the Appellant correct this before re-submitting the letter. He advised that if this was not dealt with by 5 November 2015 and if the information that he had requested on 13 September 2015 had not been supplied by then, he would proceed to correct the 06/15 return by issuing an assessment to recover the VAT previously repaid to the Appellant.

8. The Appellant did not reply and on 6 November 2015, the Officer notified the Appellant of his assessment relating to the incorrect input deduction. This showed net VAT reclaimed of £36,324.38 in period 06/15. At the same time, he adjusted for the fact that the Appellant had applied the wrong FRS percentage (11 per cent) to produce an adjusted liability for the period of £3,714.12.

9. On 16 and 20 November 2015, the Appellant's agent provided schedules of sales invoices, starting with invoice number 1 of 24 April 2012 through to number 201 of 5 December 2014. The cumulative amount of those invoices was £1,319,387.71. However, a further schedule, in this case to invoice number 228 of 16 February 2015 recorded that 152 of the 228 invoices (exactly two thirds) were disputed or remained unpaid. The Appellant's agent stated that the Appellant was never eligible for inclusion in the FRS by reference to its turnover based on the invoices rendered although its turnover was within FRS limits based on the invoiced amounts actually paid. The Appellant accordingly requested that its entry into FRS be cancelled with effect from 1 March 2013.

10. Leaving aside the issue of why there were so many unpaid invoices and how the business could tolerate that state of affairs, from my inspection of the schedules several aspects of the listing seem to leave much to be desired in terms of the nature of the information they convey. It appears that in a number of cases invoiced amounts were in fact settled for a different amount to that shown in the invoice. For example, invoices 10 and 11 are each for £1,680 and both were settled for £840. Invoice 17 appears in one list dated 23.07.2012 and in another dated 26.07.2012, in an amount of £17,715.15 but evidently settled for £11,808.00. Invoice 31 is listed in the amount of

£2,400, but was apparently settled for £12,000. Whether this payment reflected amounts due under other invoices (still listed as outstanding) from the same customer is unclear. Similarly, invoices 21 and 22 appear identical in terms of the customer and date, but were for different amounts (£930.00 and £5,784.60) and each is listed as settled for £6,744.60. One assumes that this might reflect a single payment (albeit listed twice) to settle both invoices, save that the two invoices total £6,714.60). The same is true for invoices 90 and 91, each recorded as settled for £10,606.98 but that amount in fact representing the aggregate of the two invoices.

11. At some point the listing of the invoiced amounts and of the amounts paid in settlement no longer appear to be synchronised, so that amounts entered to settle particular invoices might well relate to the previous invoice number in the list. Thus, invoice 44 of 14.12.2012 was settled for £3,542.88 but appears to have been in an amount of £960. Invoice 43 of the same date was for £3,906.00 and invoice 45 of the same date was settled for £960.00 even though issued in an amount of £8,004.00. Again, it may be that the amount listed as paid for invoice 45 should have been entered for invoice 44 and the amount listed as paid for invoice 44 should have been entered for invoice 43.

12. Finally, I note that some of the early invoices appear to have been issued in the names of several individuals. Later invoices are generally only listed as in the name of a single individual but in a significant number of cases the same individual seems to have been invoiced twice on the same day and in some cases on three or four occasions in a space of one or two days. There may be a perfectly good explanation for all these points but the accuracy of the invoicing or its listing appears to require further consideration and without further explanation I am unclear what reliance can be placed upon the list. It does not appear that these (or any other) points had been raised by the Respondents in response to the Appellant's submission of the schedules.

13. On 30 November 2015 the Officer informed the Appellant that its withdrawal from the FRS could only be from a current date or period and could not be backdated. He further explained that as the business was cash accounting, the FRS turnover limits had not been exceeded at any time since the business registered for VAT but noted that if retrospective exit was allowed, output tax would be due on all sales invoices irrespective of whether they had been paid or not.

14. On 2 December 2015 the Respondents wrote to notify the Appellant following its agent's letter of 16 November 2015 requesting retrospective withdrawal, that it had been withdrawn from FRS with effect from 30 June 2015. Formal notification to that effect was issued on 3 December 2015. On 2 December 2015 the Officer also wrote requesting outstanding information and seeking an explanation of why such a high proportion of the Appellant's sales resulted in bad debts.

15. On 29 December 2015 the Appellant requested an independent review of the decision to refuse retrospective withdrawal from 1 March 2013. On 8 February 2016, the reviewing officer upheld the original decision and on 8 March 2016, the Appellant appealed to this Tribunal. The appeal was held over while the parties sought to resolve their dispute using ADR but that proved unsuccessful and ended in May 2017.

The legislation

16. Cash accounting is dealt with in Part VIII of the VAT Regulations 1995, SI 1995 No 2518 ("the Regulations"). The cash accounting scheme allows a taxable person to account for VAT by reference to the date payment is made or received and accounted for and paid to the Commissioners by the due date prescribed for the accounting period in which the payment or other consideration for a supply is received or given (Regulations 57 and 65). A taxable person may not, however, account for VAT under this scheme if the relevant supplies or purchases are within the scope of the FRS (Regulation 57A).

17. Section 26B VATA makes provision for the FRS and the relevant Regulations are found in Part VIIA of the Regulations. The legislation and Regulations, so far as relevant to the Appellant's case are set out in the Appendix to this decision.

The Appellant's case

18. The Appellant's case was relatively straightforward. Initially, it had applied to withdraw from the FRS with effect from 1 January 2015. In its letter of 16 November 2015, however, the Appellant noted that, based on the invoices raised, it had never been eligible to enter the FRS because the value of its taxable supplies exceeded the relevant threshold for the FRS. It was therefore seeking to cancel its use of the FRS and return to the normal cash accounting VAT regime with effect from 1 March 2013.

19. In essence, its case was that the threshold to be eligible for authorisation under the FRS was that the value of the Appellant's taxable supplies should not exceed £150,000. Section 19 VATA provided the basis for arriving at the value of supplies and it was clear from the Appellant's invoices that its supplies exceeded the FRS threshold. Although the FRS established its own turnover basis for calculating the VAT liability in respect of the Appellant's supplies, the FRS did not determine the value of the Appellant's taxable supplies, and therefore its eligibility to use the FRS.

20. On the basis that the Appellant was never eligible to use the FRS, the issue was whether the Respondents should allow the Appellant to exit the FRS *ab initio*. The Appellant drew attention to the Respondents' published practice under which it would consider requests for retrospective withdrawal. This noted that each case should be examined on its own merits, considering all the relevant facts. In particular, the Respondents indicate that they would be prepared to recognise exceptional circumstances, including compassionate circumstances and the survival of the business, as a basis for allowing retrospective withdrawal.

21. In this last regard, it was said for the Appellant that it was suffering considerable financial hardship, having accumulated significant losses in the three years to 31 March 2017, and the business was only continuing with the benefit of a bank overdraft and personal loan. It was submitted that this was due to new regulations issued by the Ministry of Justice on Accident Claim Management Business, which meant that the Appellant's turnover and profitability had not come up to expectations.

The Respondents' Case

22. HMRC submitted that it was the Appellant's choice to enter the FRS. As regards the Appellant's submission that if turnover had been accounted for under the normal rules, the Appellant would have failed the eligibility test, the Respondents noted that the Appellant did not account for turnover under normal rules because it had chosen instead to benefit from cash accounting, both prior to and after joining the FRS, and HMRC had appropriately applied the test for eligibility on a cash basis.

23. The Appellant's registration records had shown expected turnover for the following 12 months to be £130,000 and the VAT returns submitted prior to joining the FRS reflected a turnover of £45,184. Following its admission to the FRS, the Appellant's returns for 06/13 to 03/14 (13 months) and 06/14 to 03/15 reflected a turnover of £144,959 and £79,427 respectively. The Respondents therefore submitted that the Appellant was eligible to join the FRS at its start date and had never been ineligible to use FRS having regard to the gross turnover declared. Its expected turnover for the year on joining was not more than £150,000 and was less than £230,000 at any anniversary of the start date (see Regulations 55L and 55M).

24. The Respondents also noted that section 26B(5) VATA provided that "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." The Respondents' records showed that the Appellant had claimed input tax on new vehicle purchases in period 06/15. In this regard, the Respondents said that the Appellant operated in the vehicle rental and leasing sector and as such the purchase of vehicles were not classified as capital expenditure. The vehicles were used for onward supply of hiring / leasing to generate business income and this was specifically excluded from any input tax claim (see Regulations 55A(1) and 55E(1), VAT Notice 733 s.15.1 and *Contrast Graphic Supplies Ltd* [2010] UKFTT 289 (TC) at §19(c)). As such, the Respondents submitted that they had correctly denied the claim to input tax of £40,625.

25. The Respondents noted that the Appellant's request on 1 September 2015 for retrospective withdrawal from the FRS had followed HMRC's decision to deny input tax for period 06/15. They submitted that the request to backdate the operation of standard accounting to the Effective Date of Registration was solely designed to reduce the VAT liability, which was not the purpose of the scheme or of the option to withdraw from it. The Appellant had failed to demonstrate any exceptional circumstances to allow retrospective withdrawal and the effective date of withdrawal should therefore be 30 June 2015.

26. In this respect, the Respondents referred to *Reynolds* (TC 00354) [2010] UKFTT 40 (TC) where the Tribunal had concluded as follows:

> "… HMRC's policy is generally not to allow retrospective application or withdrawal from the flat rate scheme … and that retrospective applications should only be allowed in exceptional circumstances. The mere fact that a taxpayer will pay more tax under the flat rate scheme is not considered exceptional for these purposes. … The flat rate scheme is intended to provide … 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 … 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."

27. Summing up, the Respondents submitted that:

(1) They had correctly authorised the use of the FRS because the Appellant's turnover had not breached the turnover criteria, either on joining the FRS or on the anniversary of joining the FRS; and

(2) Section 26B(5) precluded a trader who was using the FRS from claiming input tax and the Respondents were therefore entitled to recover the incorrectly claimed input tax; and

(3) The Appellant had failed to demonstrate any exceptional circumstances to require the Respondents to agree to the Appellant's application to withdraw from the FRS retrospectively.

Analysis

28. Regulation 55L(1) states that a taxable person shall be eligible to be authorised to account for VAT under the FRS if there are reasonable grounds for believing that the value of his "taxable supplies" in the year then beginning will not exceed £150,000. For the purposes of VAT, a "taxable supply" is a supply of goods or services made in the United Kingdom other than an exempt supply (see s.4(2) VATA). The value of a supply for a consideration in money (as all the invoiced supplies appear to have been) is such amount as, with the addition of the VAT chargeable, is equal to the consideration (s.19(2) VATA).

29. Where a person elects to use the FRS, his liability to VAT is set at an appropriate percentage of his "relevant turnover". This is the total of the value of his relevant supplies that are taxable supplies, together with the VAT chargeable on them, and the value of his exempt supplies (section 26B(2)(c) VATA). In this respect Regulation 55L(1), although looking to the year ahead, is seeking to measure eligibility for entry into the FRS for that year in the standard terms of taxable supplies and not by reference to the turnover that will form the basis of his VAT liability in that year under the FRS, if admitted to the FRS.

30. This conclusion gains support from the Regulation 55M(1)(a), regarding cessation of eligibility for the FRS, which looks at "the total value of his income" for the past year on the anniversary of the start date. "Income" for these purposes is calculated using whichever FRS turnover method has been adopted under Regulation 55G.

31. The cash accounting scheme under Regulation 57 envisages that a taxable person may "account for VAT in accordance with a scheme ... by which the operative dates for VAT accounting purposes shall be (a) for output tax, the day on which payment or other consideration is received or the date of any cheque, if later; and (b) for input tax, the date on which payment is made or other consideration is given, or the date of any cheque, if later." This suggests that the cash accounting scheme is concerned with the time at which VAT has to be accounted for rather than the value of the taxable supplies by reference to which the VAT liability arises.

32. As regards the application of the cash accounting scheme, Regulation 58(1) is in similar terms to Regulation 55L, in providing that a taxable person may use cash accounting if he has reasonable grounds to believe that the value of his taxable supplies for the coming year will not exceed £1,350,000. In contrast with Regulation 55M, a person must cease to use the scheme if the value of his taxable supplies for a year ending with a prescribed accounting period exceeds £1,600,000. In this case, withdrawal from the scheme is not linked to whatever VAT has been accounted for under the scheme in that period but to the value of the supplies on which VAT is charged.

33. Apart from the above, the basic obligation to register for VAT is driven by the value of a person's taxable supplies over a particular period (Schedule 1 VATA). It seems clear, therefore, that Regulation 55L must be referring to the value of a person's taxable supplies calculated in the same way at that used for the purposes of registration or the application of cash accounting. There seems no reason why it should be adopting a different approach or why one should attach a different meaning to "the value of taxable supplies" for these purposes.

34. I have already noted a number of unsatisfactory aspects of the Appellant's list of invoices. Taking them at face value for the moment, however, by 27 February 2013, immediately before its entry into the FRS, invoices 1 to 55 (including invoices 5A and 17A, i.e. 57 invoices in total) showed a cumulative value of invoiced taxable supplies of £288,667.82 over a 10-month period. The list of payments to 27 February 2013 omits invoice 17A and suggests that only £44,000 had been paid to that time.

35. The application for admission to the FRS was made on 15 July 2013, by which time a further 33 invoices had been issued in a further amount of £270,903.76 and suggesting that in the year to the date of application the value of the Appellant's taxable supplies was of the order of £445,408.38. Between 1 March 2013 and the date of its application, some further £34,000 had been paid to settle invoices. Looking forward a year from the time of application, the taxable supplies actually invoiced over that year amounted to some £581,665. The amount actually listed as settled over that year, however, amounted to around £140,455. While these amounts may appear very precise, they are inevitably subject to the vagaries of the listings to which I have already drawn attention.

36. Notwithstanding the significant issues that appear to surround a business that apparently invoiced some £500,000 annually but only recovered a fraction of that amount, it seems reasonable to conclude that, by reference to its invoiced taxable

supplies, the Appellant was not eligible to elect for the FRS in July 2013 on the basis that (having regard to its invoiced taxable supplies) it is difficult to think that the Appellant could have reasonably believed (had it correctly directed itself on the matter) that the value of its invoiced taxable supplies for the year to come would not exceed £150,000.

37. The application form, however, requires the applicant to declare that it is eligible for the FRS. The Respondents took the Appellant at its word on this, presumably without knowing of the significant value of invoiced but unpaid supplies given (as I believe was the case) the use of cash accounting. If the Appellant was equating the value of its taxable supplies in respect of which it had account for VAT under the cash accounting scheme with the value of its taxable supplies for the purposes of Regulation 55L, it is at least possible to understand how the application might have come to be made. The Appellant's admission to the FRS may therefore have come about through a mistake on the part of by both parties.

38. Nevertheless, following the Respondents' agreement to admit the Appellant to the FRS, it was then duly authorised by the Commissioners under Regulation 55B to account for and pay VAT in accordance with the FRS from 1 March 2013, its start date.

39. Once in the scheme, withdrawal from the scheme depends upon Regulation 55M. As this indicates, the question whether a flat rate trader ceases to be eligible to be authorised to account for VAT under the FRS depends upon the total value of the trader's income under the FRS and no longer depends upon the value of the trader's taxable supplies. Accepting the listing of invoices and payments, notwithstanding its deficiencies, it does not appear that the total value of the Appellant's income was more than £230,000 on any anniversary of the start date. That being so, the Appellant only ceased to be eligible to be authorised at the point at which it opted to withdraw from the scheme (Regulation 55M(1)(g)).

40. Following its option to withdraw, the date on which the Appellant ceased to be authorised to account for VAT in accordance with the FRS was the date on which the Respondents were notified in writing of its decision to cease to use the scheme, or such earlier or later date as is agreed between the Respondents and the Appellant (Regulation 55Q(1)(e)).

41. As Regulation 55Q(1)(e) indicates, it is open to the Respondents to agree to a withdrawal from the FRS with effect from an earlier date than that of notification. As the Appellant noted, the Respondents' published practice indicates that they may so agree in "exceptional circumstances". In this respect, however, I do not accept that the Appellant has demonstrated that it falls within what the Respondents term, "the survival of the business". It seems entirely possible that a business with 'bad debts' on the scale suggested by the Appellant's schedules of invoices and payments may be making losses. However, apart from the schedules and a 'micro-entity' balance sheet at 31 March 2017, I have no other information on which to reach any conclusion about the business, how it was run and financed or whether its survival is in fact in issue.

42. That leaves the question whether the possibility that (as was submitted) the Appellant had mistakenly applied to join the FRS *ab initio*, believing that the relevant threshold depended upon its cash accounting when in fact the value of its taxable supplies (if the schedule of invoices is to be taken as correctly recording those supplies) significantly exceeded the threshold, is something that negates the Respondents' authorisation or should lead the Respondents to agree to an earlier withdrawal on the basis that the Appellant should never have been in the FRS in the first place.

43. There are perhaps two points to make about this. First, the possibility that the Appellant may never have been eligible to enter the FRS does not appear to have been a factor that the Respondents took into account (or, at least, approached correctly) at the time of their original decision or on review; indeed, the Respondents' submissions on this appeal suggest that this was not a relevant factor. Second, once within the FRS, withdrawal with effect from a date earlier than the notification is a matter for agreement between the taxpayer and the Respondents.

44. The Appellant's argument is, essentially, that it was admitted to the FRS by mistake. If I could be satisfied on that point, I might be prepared to conclude that the Appellant was never eligible to join the FRS and it should therefore be treated as never having done so. That conclusion would, however, involve a degree of speculation on my part. The Appellant's declaration of eligibility depends upon a reasonable belief regarding its supplies for the coming year, and I heard no substantive evidence (only general description) about the nature of the Appellant's supplies nor do I have any explanation as to why so many invoices were unpaid (or of any other apparent deficiencies in the listing). At the very least, I would need evidence as to the basis on which the Appellant's application and declaration were made before concluding that the Appellant's admission to the FRS should, effectively, be set aside. The application form was signed by the Appellant's director and he did not give evidence.

45. Nevertheless, it seems apparent that the Respondents failed to pay due regard to this aspect of the matter in reaching their decision on the timing of the Appellant's withdrawal from the FRS, and applied the wrong criteria to determining its eligibility for entering the FRS having regard to the claimed value of the Appellant's taxable supplies. The possibility that the Appellant was in fact never eligible for the FRS would seem to be a relevant factor that should at least enter into the Respondents' consideration of an application to withdraw from the FRS retrospectively, even if not among the usual "exceptional circumstances" of their published guidance. The Respondents are best placed not only to assess and test the information being put forward by the taxpayer but to consider the financial impact on the taxpayer's business and the revenue at risk to the Exchequer.

The appropriate course of action

46. Absent authority to the contrary, I would have thought it not within the Tribunal's power to agree on the Respondents' behalf to the earlier date of withdrawal sought by the Appellant or to direct that the Respondents should agree to it. The

consequence of the Respondents' failure to consider the matter properly might ordinarily be expected to be for the Respondents to consider the matter again in the light of the Tribunal's decision.

47. Section 83(1)(fza) VATA provides that an appeal lies to the Tribunal with respect to a decision by the Respondents withdrawing authorisation for a person's liability to pay VAT under the FRS. The more usual situation in which such an appeal would be made is perhaps likely to be a case in which the Respondents themselves have decided to withdraw the benefit of the FRS rather than a case in which the taxpayer has opted to withdraw. On the other hand, the Respondents' decision in this case has been to direct that the Appellant should withdraw from the FRS from a particular date, leading to an assessment to recover wrongly credited input tax, and there seems no reason why this should not be a relevant decision against which an appeal lies under section 83(1)(fza).

48. Where an appeal lies under section 83(1)(fza), section 84(4ZA) provides that an appeal against the decision or against an assessment based on that decision, shall not be allowed unless the tribunal considers that the Respondents could not reasonably have been satisfied that there were grounds for the decision. There are a number of tribunal decisions in which the Tribunal has reviewed a refusal by the Respondents to allow a retrospective application for entry into the FRS (see e.g. *Anderson v HMRC* (2007) V20255; *March v HMRC* [2009] UKFTT 94; *Skinner (t/a DLS Packaging) v HMRC* [2010] UKFTT 64; *S D Solutions Ltd v HMRC* [2010] UKFTT 228; *Anycom Ltd v HMRC* [2011] UKFTT 654; Lennie v HMRC [2012] UKFTT 669; *Wilmington v HMRC* [2012] UKFTT 287; *Seeff (t/a TPL Associates) v HMRC* [2013] UKFTT 335; *C & N Hollinrake Ltd v HMRC* [2014] UKFTT 203; *Goodman v HMRC* [2016] UKFTT 34). The relevant Regulation that deals with a retrospective application to join the FRS is Regulation 55B(1), which (in similar fashion to Regulation 55Q) states that the Respondents may authorise a person to account for VAT under the FRS with effect from, "(b) such earlier or later date as may be agreed between him and the Commissioners."

49. Regulation 55B was considered by Henderson J in relation to a retrospective application to join the FRS in *HMRC v Burke* [2009] EWHC 2587 (Ch). Having noted the Respondents' published guidance on the matter, Henderson J continued at [19]:

> "The important point to note in this, in my judgment, are, first, that consideration will be given to all the facts in dealing with an application for an earlier start date and, secondly, that retrospection will not normally be allowed for periods for which liability has already been calculated on the normal, or indeed any other, basis. It is implicit in this that special circumstances would have to be shown in order to displace the normal policy set out in the notice."

50. Having referred to section 84(4ZA), Henderson J then described at [21] the nature of this Tribunal's jurisdiction in relation to any appeal:

"[Section 84(4ZA)] imposes a high threshold and confines the jurisdiction of the tribunal to allow the appeal to cases where it considers that the Commissioners could not reasonably have been satisfied that there were grounds for the decision under appeal. In other words, although the jurisdiction is an appellate one, its content is, in essence, a supervisory one and it differs little, if at all, from the grounds upon which judicial review might otherwise be available in the absence of an express right of appeal."

51. Henderson J then went on to consider the facts of Mr Burke's case and the decision of the Tribunal on those facts, concluding that the Respondents had not misdirected themselves in Mr Burke's case and that there was therefore no material which could properly have led the Tribunal to conclude that the high threshold condition for a successful appeal was satisfied. This conclusion made it unnecessary for Henderson J to consider the Respondents' alternative submission that even if they had misdirected themselves, so that the Tribunal was correct to allow the appeal, the Tribunal was nevertheless wrong to substitute their own view of what the Respondents ought to have done in response to Mr Burke's application. As to that Henderson J said that he could see "considerable force in the submission" but he preferred to make no ruling on the point.

52. In this respect the parties did not draw my attention to any comparable cases to the Appellant's and I have identified only two in which HMRC's failure to allow an earlier withdrawal from the FRS has been in point: *Reynolds v HMRC* [2010] UKFTT 40 (to which the Respondents referred in submissions) and *Northern Renovations Ltd v HMRC* [2012] UKFTT 409. In both cases, the taxpayer entered the FRS but subsequently discovered that the FRS operated to its disadvantage; hence, the application to withdraw from an earlier date. To an extent that reflects the Appellant's case, in so far as it seeks to avoid the recovery of incorrectly claimed input tax. In neither *Reynolds* or *Northern Renovations*, however, does it appear that the taxpayer was, or might have been, ineligible to enter the FRS from the outset. In effect, in both cases the taxpayer remained within the FRS for longer than was appropriate.

My decision

53. For the reasons that I have given, I am unable to say on the evidence before me that the Appellant was never eligible for admission to the FRS and entered the FRS by mistake, with whatever consequences that may entail. Nevertheless, it seems that I should set aside the Respondents' decision (and allow the Appellant's appeal to that extent), on the basis that the Respondents failed to consider and take into account a relevant factor, namely the possibility that the Appellant was never eligible for the FRS, and in any event have applied the wrong criteria for determining whether the Appellant was in fact eligible to enter the FRS.

54. I therefore direct that the Respondents are to reconsider and remake their decision on the Appellant's application for retrospective withdrawal from the FRS with effect from 1 March 2013 in the light of my decision and the Appellant's evidence (which appears to require further explanation and verification). To facilitate

the remaking of their decision, I direct that the Appellant shall be entitled, within one month of the release of this decision or such longer period as the Appellants and the Respondents shall agree, to submit to the Respondents such further evidence regarding its taxable supplies and its financial position as it thinks appropriate. Thereafter, it will be for the Respondents are at liberty to decide what further information or explanation they may then require to facilitate the remaking of their decision. I neither confirm nor set aside the assessment to recover input VAT, the validity and amount of which will, it seems to me, ultimately depend upon the outcome of the Respondents' further decision.

55. 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.

MALCOLM GAMMIE
TRIBUNAL JUDGE

RELEASE DATE: 31 DECEMBER 2018

APPENDIX:
THE RELEVANT LEGISLATION AND REGULATIONS

Section 26B VATA provides for the FRS (so far as relevant to the Appellant's case) as follows:

> "(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. ...
>
> (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. ...
>
> (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 FRS is dealt with in Part VIIA of the Regulations. They provide (so far as relevant to the Appellant's case) as follows:

55A Interpretation of Part VIIA

(1) In this Part

…

"capital expenditure goods" means any goods of a capital nature but does not include any goods acquired by a flat-rate trader (whether before he is a flat-rate trader or not)

(*a*) for the purpose of resale or incorporation into goods supplied by him,

(*b*) for consumption by him within one year, or

(*c*) to generate income by being leased, let or hired;

…

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

"end date" has the meaning given in regulation 55Q(2);

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

"relevant purchase" has the meaning given in regulation 55C;

"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; ...

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. ...

(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.

55E Input tax

(1) For any prescribed accounting period of a flat-rate trader, he is entitled to credit for input tax in respect of any relevant purchase of his of capital expenditure goods with a value, together with the VAT chargeable, of more than 2,000.

(2) Where paragraph (1) above applies, the whole of the input tax on the goods concerned shall be regarded as used or to be used by the flat-rate trader exclusively in making taxable supplies.

(3) Section 26B(5) of the Act shall not apply to prevent a taxable person from being entitled to credit for input tax in respect of any supply, acquisition or importation by him that is not a relevant purchase of his. ...

55G Determining relevant turnover

(1) The Commissioners shall prescribe, in a notice published by them, three methods to determine when supplies are to be treated as taking place for the purpose of ascertaining the relevant turnover of a flat-rate trader for a particular period, as follows

(*a*) “the basic turnover method”, which shall be a method based on consideration for supplies taking place in a period;

(*b*) “the cash turnover method”, which shall be a method based on the actual consideration received in a period;

(*c*) “the retailer's turnover method”, which shall be a method based on the daily gross takings of a retailer. ...

(3) In any prescribed accounting period, a flat-rate trader must use one of the methods to determine the value of his relevant turnover.

55L Admission to Scheme

(1) A taxable person shall be eligible to be authorised to account for VAT in accordance with the scheme at any time if

(*a*) there are reasonable grounds for believing that

(i) the value of taxable supplies to be made by him in the period of one year then beginning will not exceed £150,000, ...

55M Withdrawal from the scheme

(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

(*a*) at any anniversary of his start date, the total value of his income in the period of one year then ending is more than £230,000,

(*b*) there are reasonable grounds to believe that the total value of his income in the period of 30 days then beginning will exceed £230,000, ...

(*g*) he opts to withdraw from the scheme, or

(*h*) his authorisation is terminated in accordance with regulation 55P below.

(2) A flat-rate trader does not cease to be eligible to be authorised by virtue of paragraph (1)(*a*) above if the Commissioners are satisfied that the total value of his income in the period of one year then beginning will not exceed 191,500.

(3) In determining the value of a flat-rate trader's income for the purposes of paragraphs (1)(*a*) and (*b*) and (2) above, any supply of goods or services that are capital assets of the business in the course or furtherance of which they are supplied, shall be disregarded.

(4) For the purposes of this regulation, “income” shall be calculated in accordance with the method specified in regulation 55G(1) (determining relevant turnover) used by the business to determine the value of its turnover whilst accounting for VAT under the scheme.

(5) Where a business has used more than one method to determine the value of its turnover whilst accounting for VAT under the scheme, the method referred to in paragraph (4) above shall be the most recent method used.

55P Termination by the Commissioners

The Commissioners may terminate the authorisation of a flat-rate trader at any time if

(*a*) they consider it necessary to do so for the protection of the revenue, or

(*b*) a false statement was made by, or on behalf of, him in relation to his application for authorisation.

55Q Date of withdrawal from the scheme

(1) The date on which a flat-rate trader ceases to be authorised to account for VAT in accordance with the scheme shall be

(*a*) where regulation 55M(1)(*a*) applies

(i) in the case of a person who is authorised in accordance with regulation 50(1) (annual accounting scheme), the end of the prescribed accounting period in which the relevant anniversary occurred, or the end of the month next following, whichever is the earlier, or

(ii) in all other cases, the end of the prescribed accounting period in which the relevant anniversary occurred,

(*b*) where regulation 55M(1)(*b*) applies, the beginning of the period of 30 days in question, ...

(*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, and

(*f*) where regulation 55M(1)(*h*) applies, the date of issue of a notice of termination by the Commissioners or such earlier or later date as may be directed in the notification.

(2) The date with effect from which a person ceases to be so authorised shall be known as his end date.

55R Self-supply on withdrawal from scheme

(1) This regulation applies where

(*a*) a person continues to be a taxable person after his end date,

(*b*) for any prescribed accounting period for which he was a flat-rate trader, he was entitled to, and claimed, credit for input tax in respect of any capital expenditure goods, and

(*c*) he did not, whilst he was a flat-rate trader, make a supply of those goods.

(2) Where this regulation applies, those goods shall be treated for the purposes of the Act as being, on the day after his end date, both supplied to him for the purpose of his business and supplied by him in the course or furtherance of his business.

(3) The value of a supply of goods treated under paragraph (2) above as made to or by a person shall be determined as though it were a supply falling within paragraph 6(1) of Schedule 6 to the Act."