[2016] UKFTT 0803 (TC)

TC05528

Appeal Number: TC/2015/02125

VAT –suspension of penalty – flawed decision – taxpayer de-registering – taxpayer becoming member of VAT group – held – decision flawed-order for penalty to be suspended

FIRST-TIER TRIBUNAL
TAX CHAMBER

Parklane UK Investments Limited **Appellant**

- and -

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

TRIBUNAL: JUDGE Rachel Short
Miss Susan Stott

Sitting in public at City Exchange, 11 Albion Street, Leeds on 8 November 2016

Mr Timothy Brown of Temple Tax Chambers, for the Appellant

Mrs Ann Sinclair, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. This is an appeal by the Appellant, Parklane UK Investments Limited ("Parklane") against HMRC's decision of 8 May 2014 not to suspend a penalty of £19,800.00 for a careless in accuracy in the Appellant's VAT return for the 12/13 period.

2. The amount of that penalty was reduced on review on 14 January 2015 to £11,800. The quantum of the penalty is not in dispute.

3. The Appellant appealed against HMRC's decision on 10 March 2015. That appeal was made late but before the Tribunal HMRC accepted that the time limit for the making of the appeal should be extended so that the appeal should be treated as made in time.

Background facts

4. Parklane is a UK resident company which was registered for VAT from 1 September 2012.

5. Parklane's VAT return for the 12/13 period claimed a VAT repayment of £66,000.00.

6. As a result of a visit from HMRC's officer Nathan on 27 February 2014 HMRC advised Parklane that since all of its supplies were exempt supplies it could not claim input tax and that it was not entitled to be registered for VAT.

7. Parklane was de-registered for VAT with effect from 1 April 2014.

8. Parklane became a member of a group of companies of which Park Lane Properties (Management) Limited was the representative member from 1 April 2014.

9. HMRC issued a penalty explanation letter in the name of Parklane on 8 May 2014 stating that under Schedule 24 Finance Act 2007 Parklane's careless behaviour had led to an inaccuracy in its tax return for the 12/13 period and stating that *"the penalty could not be suspended because it was not possible to set conditions"*. No further explanation was given for the reason not to suspend the penalty at this time.

10. A notice of penalty assessment was issued on Parklane on 29 July 2014.

11. HMRC undertook a review of the decision to uphold the penalty on 14 January 2015. In that letter HMRC gave a more detailed explanation of why they thought they could not suspend the penalty; *"Unfortunately in your case suspension is not possible due to the fact that you are no longer registered under VRN [Parklane's original VAT number] and are now part of a VAT group. HMRC therefore cannot impose conditions against VRN [Parklane's original VAT number]. Suspension conditions cannot be transferred to another VRN"*

The law

12. The legislation which sets out how penalties are calculated and assessed for these purposes is Schedule 24 to the Finance Act 2007. The conditions which allow HMRC to suspend a penalty charged under Schedule 24 are set out at paragraph 14:

"14 (1) *HMRC may suspend all or part of a penalty for a careless inaccuracy under paragraph 1 by notice in writing to P.*

(2) A notice must specify –

(a) what part of the penalty is to be suspended,

(b) a period of suspension not exceeding two years, and

(c) conditions of suspension to be complied with by P.

(3) HMRC may suspend all or part of a penalty only if compliance with a condition of suspension would help P to avoid becoming liable to further penalties under paragraph 1 for careless inaccuracy."

13. A taxpayer's right to appeal against a decision of HMRC not to suspend a penalty are set out in paragraph 15(3) and 17(4):

"*17(4) On an appeal under paragraph 15(3) –*

(a) the tribunal may order HMRC to suspend the penalty only if it thinks that HMRC's decision not to suspend was flawed,....."

14. The Tribunal's powers on an appeal in respect of HMRC's decision not to suspend a penalty are by reference to principles of administrative law as set out at paragraph 17(6): "*flawed" means flawed when considered in the light of the principles applicable in proceedings for judicial review*"

15. The UK VAT rules which apply to VAT groups are at s 43 Value Added Tax Act 1994.

16. It is agreed that the onus of proof is on HMRC to demonstrate that in this case its decision not to suspend penalties was not flawed.

17. We were referred to three First-tier Tribunal decisions which considered HMRC's exercise of its discretion to suspend a penalty:

18. *Shelfside (Holdings) Ltd* [2012] TC 01978

19. *United European Gastroenterology Federation* [2013] TC 02698

20. *Automation CPM Group Limited* [2015] TC 04380.

Evidence

21. No oral evidence was given before the Tribunal.

22. Mr Nathan a VAT assurance office for HMRC provided a witness statement of 19 May 2016 which was taken as read. Mr Nathan was the officer who visited Parklane's premises on 27 February 2014 and met with Parklane's financial controller Mr Flint.

23. Mr Nathan's witness statement records Mr Flint telling him that 100% of Parklane's sales were exempt, that there was no option to tax any of Parklane's properties and no intention to do so in the future.

24. Mr Nathan wrote to Mr Flint at Parklane on 4 March 2014 informing him that there were inaccuracies in Parklane's tax return for the 12/13 period and again on 30 April 2014 informing him that Parklane was not eligible to be registered for VAT.

25. Mr Nathan sent a penalty explanation to Parklane on 8 May 2014 explaining the basis for the penalty imposed and stating that it was not possible to suspend any of the penalty.

26. Mrs Sinclair referred us to Mr Nathan's explanation for why he decided not to suspend the penalty on Parklane initially "*I made the decision that no suspension conditions could be set, on the basis that the company [Parklane] made 100% exempt supplies, had no option to tax on its properties and had no intention of opting to tax in the future, according to Mr Flint [finance controller of Parklane].*"

27. We also saw various correspondence between the parties including;

(i) HMRC's review letter of 14 January 2015,

(ii) Parklane's response of 10 February 2015 to that letter asking why suspension conditions could not be imposed on the VAT group of which Parklane was now a member, and

(iii) HMRC's letter of 26 February 2015 saying that "*it is HMRC's opinion that P is the legal entity to whom the penalty was imposed. As soon as the legal entity changes/ceases, the suspension conditions cannot be applied. It is HMRC's opinion that Parklane VRN [Parklane's original VAT number] is P. As Parklane VRN [Parklane's original VAT number] no longer exists, there is no company to whom to apply the penalty to*".

Parklane's submissions

28. Mr Brown's arguments on behalf of Parklane rested on one issue only; that HMRC were not correct to view the provisions of paragraph 14 of Schedule 24 as applying to entities as defined by VAT registration numbers. The legislation referred not to VAT registration numbers but to persons, which included Parklane as a company. It was not correct that Parklane ceased to exist as a legal entity or a company as a result of becoming a member of a VAT group.

29. Mr Brown pointed out that if the penalty was collected by HMRC, it would be collected in the name of Parklane and not in the name of the VAT group's representative member. HMRC's approach was flawed since it suggested that an entity could escape liability for its VAT debts by the simple expedient of de-registering for VAT which would leave HMRC unable to collect significant VAT debts.

30. Mr Brown also said that it was wrong for HMRC to suggest that Parklane could not comply with any conditions which were imposed as a result of the suspension of a penalty just because it was part of a VAT group; it would still have VAT compliance obligations and any failures on its part would be reflected in the group's VAT position.

31. Mr Brown referred to the Tribunal's decision in the *Gastroenterology* case to support his approach, the Tribunal concluding in that case that

> *"HMRC's additional reason in their review decision for rejecting any suggestion of suspension was misconceived. The fact that the Appellant would have to apply for a new VAT registration if it chose to carry out any future taxable activities in the UK does not, in our view, mean that it should therefore be treated as an entirely different person for the purposes of Schedule 24*"[Para 68]

HMRC's submissions

32. For HMRC Mrs Sinclair said that when Parklane became a member of a VAT group it was no longer VAT registered as such. In a VAT group it is the representative member which is treated for VAT purposes as carrying on the business of the group and only the representative member is actually registered for VAT.

33. The penalty rules at Schedule 24 paragraph 1 impose a penalty on "P". Penalties could be suspended subject to compliance with conditions by "P". If the legal entity "P" changes or ceases to exist, it follows that conditions cannot be applied to "P".

34. In HMRC's view since Parklane no longer existed for VAT purposes when it became part of a VAT group, it was not possible to set conditions on Parklane as an entity which would allow a penalty to be suspended under paragraph 14(3), as explained in HMRC's letter of 26 February 2015.

35. Mrs Sinclair accepted that her arguments were based on a legal rather than a practical impediment to the application of conditions on Parklane. In her view the legal issues which arose when imposing suspension condition on a member of a VAT

group were demonstrated by the fact that in these circumstances paragraph 14(6) of Schedule 24 could not operate to bring a penalty back into charge, because Parklane as a member of a VAT group, could no longer be subject to any penalty.

36. Mrs Sinclair also referred to the rather different rationale for not suspending the penalty referred to by Mr Nathan in his witness statement; that there was no prospect of Parklane making taxable supplies and therefore there were no activities on which conditions could be set. Mrs Sinclair referred to the *Gastroenterology* decision in support of this approach:

> "*in the circumstances of this case (where there is no evidence of the Appellant having carried on any taxable activities in the UK since the 2009 congress, or having any intention to carry on any such activities in the foreseeable future) we would not in any event consider this to be a suitable case for suspension*" [Para 71].

37. Mrs Sinclair recognised that HMRC's grounds for refusing to suspend the penalty on Parklane had changed from the time when Mr Nathan first considered the position (in May 2014) to the time when HMRC set out its grounds in its review letter of 14 January 2015.

38. In response to questions from the Tribunal and Mr Brown, Mrs Sinclair did accept that when the penalty was collected, it would be collected against Parklane as an entity and by reference to its old VAT number. She referred us to a section of HMRC's VAT manual (V Group 01450) which states that the representative member of a group is not liable for VAT debts incurred by members of a group before they become group members.

39. Mrs Sinclair said that HMRC had considered whether in this case there were any "special circumstances" of which HMRC should take account which might lead them to reduce the penalties payable, but had concluded that there were no such special circumstances.

40. It was not suggested by either party that the penalty assessment had not been correctly served in the name of Parklane despite the fact that at the time when it was served Parklane was treated as part of a VAT group.

Findings of fact

41. The penalty assessment for the 12/13 period was issued in the name of Parklane, as a legal entity and any penalty would be collected against Parklane by reference to its old VAT number.

42. Parklane did not cease to exist as a legal entity as a result of becoming a member of a VAT group.

43. HMRC gave two different reasons for refusing to suspend the penalties on Parklane, one given by Mr Nathan in May 2014 and one given on review by HMRC in January 2015.

Decision

44. The question for this Tribunal is whether HMRC's decision to refuse to suspend the penalties assessed on Parklane was flawed in the light of judicial review principles, being a decision which could not have been reasonably reached by HMRC, including because they took account of irrelevant matters or failed to take account of relevant matters. As HMRC pointed out, the hurdle for the Tribunal to conclude that a decision is flawed for these purposes is rather high. As set out in the *Shelfside* decision HMRC's decision not to suspend a penalty must be:

> "*so unreasonable that no reasonable body of Commissioners acting properly within their powers could have taken it*" [Para 25]

45. HMRC in fact gave two different reasons for refusing to suspend Parklane's penalty. Leaving aside at this stage whether the giving of inconsistent reasons is in itself enough to make a decision "flawed" for these purposes, we have considered each of the reasons given by HMRC for refusing to suspend the penalty.

Mr Nathan's decision

46. HMRC first said that their decision was in line with the *Gastroenterology* case because there was no prospect of Parklane making VAT supplies in the UK; it was making exempt supplies and had no intention of opting to tax any of the properties which it owned.

47. This was based on the information which Mr Nathan had received after his visit to Parklane in February 2014. However, Parklane was not in exactly the same position as the taxpayer in the *Gastroenterology* case, although Mr Flint might have stated his current intentions, Parklane was carrying on business in the UK and it remained a theoretical possibility that it could opt to tax the properties in respect of which supplies were made.

48. In any event, the facts on which Mr Nathan based that decision subsequently changed; Parklane de-registered for VAT and became part of a VAT group. On that basis we do not consider that it is now open to HMRC to rely on Mr Nathan's original rationale as a reasonable basis for refusing to suspend the penalty on Parklane. To do so would be to fail to take account of a relevant matter, which was recognised by the time of HMRC's review letter of January 2015, being Parklane's membership of a VAT group.

The review decision – January 2015

49. HMRC's review letter of January 2015 gave a different reason for refusing to suspend penalties and was made on the basis that Parklane was part of a VAT group and that the conditions for suspension could not be transferred to another VAT registration number. HMRC argued that membership of a VAT group meant that

Parklane ceased to exist as a legal entity for VAT purposes and could not therefore comply with any conditions imposed as part of a suspension notice.

50. Fundamental to our consideration of whether HMRC's second decision was flawed is a consideration of whether their analysis of what it means to be part of a VAT group in the UK is correct, both by reference to legal principles and practical effect.

51. Our view is that HMRC's legal analysis of what it means to be a member of a UK VAT group is misconceived. There is no suggestion in the VAT legislation that membership of a VAT group entails the loss of legal identity for all group members other than the representative member. On the contrary, s 43(1) Value Added Tax Act 1994 states that all members of a group retain joint and several liability for the VAT debts of the group.

52. The VAT group representative member is just that, the representative, for VAT purposes, of all other members of the group. The VAT grouping legislation imposes a limited fiction for VAT purposes; the business of each member is treated, for VAT purposes, as being carried on by the representative member. That does not result in group members losing their legal identity.

53. In HMRC's favour, there are aspects of the suspension rules at Paragraph 14(6) of Schedule 24 (what happens if P becomes liable to another penalty during the suspension period) which might appear to be difficult to apply to a taxpayer which is a member of a VAT group, but we were not provided with any evidence to suggest that HMRC considered any possible basis on which any practical issues with imposing penalties on an entity which was part of a VAT group might be dealt with.

54. We have borne in mind that the purpose of the suspension rules is to provide guidance and support to a taxpayer to help them avoid penalties in the future. We were not provided with any evidence to suggest that HMRC had given any consideration to whether or how this could be applied to Parklane or the VAT group of which it was a member.

55. As Mr Brown pointed out, HMRC accepted that had a penalty been imposed, it would have been imposed on Parklane by reference to its old VAT number, despite the fact that it was now a member of a VAT group.

56. We agree with Mr Brown that there is no insurmountable barrier to imposing suspension conditions in circumstances where a company is a member of a VAT group and no reason in practice why conditions could not be imposed on Parklane, with implications for the whole group if those are not complied with. Leaving aside the possibility that in a relatively small group such as this, there is in any event a possible coincidence of personnel between group members.

Conclusion

57. Our view is that HMRC's approach in this case is flawed for three reasons; first it is based on a misunderstanding of the implications of VAT grouping, conflating the legal and VAT effects of being a member of a VAT group.

58. Second, it demonstrates a logical inconsistency, HMRC do not suggest that the penalty assessment could not be issued on Parklane, despite it being a member of a VAT group at the relevant time, recognising for those purposes that Parklane has an identity outside the VAT group, but nevertheless argue that Parklane has no separate identity as far as imposing any conditions in respect of the penalty is concerned.

59. Finally, it demonstrates an internal inconsistency; the reasons originally advanced by Mr Nathan for not suspending penalties are quite different than the reasons given to Parklane in HMRC's review letter of January 2015. HMRC did not advance any explanation for this change of approach.

60. The Tribunal has concluded that HMRC's decision not to suspend the penalty imposed on Parklane was flawed in the light of principles applicable to judicial review proceedings and orders that HMRC suspend the penalty on Parklane for the 12/13 VAT period.

61. 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.

RACHEL SHORT

TRIBUNAL JUDGE
RELEASE DATE: 30 NOVEMBER 2016