

CHAPTER 17

PENALTIES FOR FAILURE TO NOTIFY

17.1 Introduction

When a trader is late notifying HMRC that he should be registered for VAT, three things happen:

- 1) His **registration is backdated** to the date from which he was liable to be registered.
- 2) He must also **account for output tax** on his supplies from the date on which he should have been registered. However, credit for input tax can be given, if the normal recovery rules have been satisfied on purchases made in the same period of time.
- 3) He is liable to a **penalty** for the period of default, unless he can convince HMRC that there is a reasonable excuse for his delay.

17.2 Calculation of the penalty

Schedule 41 FA 2008 introduced a new penalty regime which applies when a taxpayer does not meet an obligation to notify HMRC. The penalty regime applies to VAT as well as other direct taxes, including income tax.

The penalty will be based on the behaviour of the person concerned and is a **percentage of the 'potential lost revenue'**. We will look at the definition of this later.

For a **deliberate and concealed failure**, the penalty will be a **maximum 100%** of the potential lost revenue; for a **deliberate but not concealed failure**, the **maximum penalty will be 70%** of the potential lost revenue; and for any other case - eg due to lack of care, the **maximum penalty will be 30%** of the potential lost revenue.

[FA 2008, Sch 41 Para 6](#)

A failure is deliberate and concealed where the failure is deliberate and the taxpayer **makes arrangements to conceal the situation** giving rise to the obligation. This would include creating false evidence of a non-taxable source of income to explain undisclosed income; creating false invoices to support inaccurate turnover figures or destroying books and records.

[FA 2008, Sch 41 Para 5](#)

A failure is deliberate but not concealed where the failure is deliberate but no arrangements are made to conceal the situation giving rise to the obligation. An example of this would be where a person has deliberately failed to keep records necessary to know when a notification is required, even though they knew it was likely that the conditions for notification would be met.

Reductions in the amount of the penalty are available for both '**unprompted**' and '**prompted**' disclosures.

The table below details the maximum and minimum penalties that could apply. Note that where the taxpayer is simply careless in not making the necessary notification, the reduction in the penalty also depends on how long has elapsed since VAT first became unpaid as a result of the failure.

Behaviour	Maximum penalty	Min penalty with unprompted disclosure		Min penalty with prompted disclosure	
		<12m	≥12m	<12m	≥12m
Deliberate and concealed	100%	30%		50%	
Deliberate but not concealed	70%	20%		35%	
Any other case	30%	Nil	10%	10%	20%

[FA 2008, Sch 41 Para 13](#)

Disclosure is unprompted if the taxpayer has no reason to believe HMRC have discovered or are about to discover the failure.

Disclosure takes place where a taxpayer **tells HMRC** about the failure, gives HMRC **reasonable help** in calculating the resulting unpaid tax and **allows HMRC access to records** to check the amount of unpaid tax.

[FA 2008, Sch 41 Para 12](#)

HMRC weight the elements of disclosure as follows:

Telling	30%
Helping	40%
Giving access	30%
Total	100%

The actual reduction in the penalty depends on the quality of the elements of disclosure, including **timing, nature and extent**.

17.3 Other points re failure to notify penalties

Failure to notify penalties must be **paid within 30 days** of the date the notice of assessing the penalty is issued, or interest will be charged.

[FA 2008, Sch 41 Para 16](#)

The decision to issue a penalty or the amount of the penalty payable **can be appealed against** by the taxpayer.

[FA 2008, Sch 41 Para 17 & 18](#)

Penalties will not be charged if the taxpayer has a reasonable excuse for the failure and the failure is not deliberate. The death of a close relative or domestic partner around the time that the person should have given notice is normally treated as a reasonable excuse, as is the serious illness of the person or a close relative.

[FA 2008, Sch 41 Para 20](#)

HMRC usually accept that there is a reasonable excuse if the letter or form giving the relevant notification is lost or delayed in the post as a result of an unforeseen event disrupting the postal service such as prolonged industrial action.

The legislation specifies that an insufficiency of funds is not a **reasonable excuse** (unless due to events outside the taxpayer's control). Relying on a third party is also not a reasonable excuse, unless the taxpayer took reasonable care to explain to the third party what they required them to do and made regular checks on progress.

[FA 2008, Sch 41 Para 20](#)

HMRC list in their guidance a number of situations which will not be accepted as a reasonable excuse, including pressure of work, lack of information and ignorance of basic law.

VAT Notice 700/41 para 3.1

17.4 Leading cases

Jo-Ann Neal v C&E

A freelance model began self-employment in April 1985, when she was 19 years of age. She became liable to register for VAT in October 1985, but did not do so until March 1986. The Commissioners imposed a penalty under what is now VATA 1994 s.67 and she appealed, contending that she had no knowledge of VAT and was unaware that her income exceeded the registration limits. It was held that her ignorance of the law could not constitute a reasonable excuse.

J Warnock

A trader, whose wife acted as his bookkeeper, appealed against a penalty under VATA 1994, s.67, (now repealed) giving evidence that his wife had been ill, and thus had been unable to keep his books up to date. He had therefore been unaware that his turnover had exceeded the registration threshold. The tribunal allowed the appeal, holding that the circumstances constituted a reasonable excuse.

K E Jenkinson

J, who had previously been an employee, began self employment in May 1987. He sought advice concerning VAT from G, an acquaintance, whom he had met while travelling to work by train. G had told J that he was a qualified accountant, and promised J that he would arrange his registration for VAT. In May 1987 he gave J a registration number, which J used on his invoices. In September 1987 J telephoned his local VAT office to enquire why he had not received a VAT return. It transpired that the number which G had given to J was not an official registration number, and G had not registered J for VAT. J subsequently discovered that G was not in fact a qualified accountant. The Commissioners imposed a penalty on J under what is now VATA 1994 s.67, and J appealed, contending that he had a reasonable excuse because he had genuinely believed that he was registered. The tribunal allowed J's appeal. Merely delegating a task to a third party was not a reasonable excuse, but in this case J had actually been given what he believed to be a registration number, and G's misrepresentations did amount to a reasonable excuse.

17.5 Interaction with other penalties

[FA 2008, Sch 41 Para 15](#)

The failure to notify penalty will be reduced by the amount of any other penalty calculated in respect of the same tax liability, such as a late payment penalty.

Example 1

G Ltd started trading on 1 July 2009 and makes taxable supplies. Supplies exceeded the registration threshold in March 2010, so G Ltd became liable to register for VAT from 1 May 2010.

The company did not realise this until after the appointment of a new Finance Director in December 2010. HMRC were notified on 31 December 2010. Sales in the period from 1 May 2010 to 31 December 2010 were £150,000.

Proper documentation for purchases was not kept so input tax cannot be recovered for this period.

You are required to calculate the late registration penalty payable by G Ltd.

Example 2

In April 2010, Fran used her redundancy pay to start up a tea-room in Didsbury village. Her takings are as follows:

	<u>2010</u>	<u>2011</u>
	£	£
January		6,000
February		8,000
March		10,000
April	5,000	12,000
May	7,000	15,000
June	8,000	18,000
July	12,000	25,000
August	22,000	30,000
September	18,000	
October	10,000	
November	9,000	
December	8,000	

Fran's main costs are food (which is zero-rated), staff wages and rent on the shop. She incurs a small amount of input tax (on cutlery, crockery and cleaning products etc) of £500 per month.

In March 2011, Fran realised that she should have registered for VAT. She notified HMRC on Form VAT 1 on 30 March 2011 and charged VAT on sales from 1 April 2011.

Fran explained to you that she had been on a basic financial awareness course and had been told by the tutor that, as food was zero-rated, she didn't need to charge VAT. She now realises this is wrong and wonders whether this can be put forward as a "reasonable excuse"?

You are required to calculate the penalty (if any) Fran will be liable to pay due to her late notification. (Assume the standard rate of VAT is 17.5% throughout the period.)

Example 3

Ruth (a sole trader) became liable to register for VAT at the end of March 2011 when taxable turnover for the previous 12 months exceeded the registration threshold. Although she was aware of the need to register, she decided not to register until she had a quiet period. She finally notified HMRC on 1 November 2011. Her sales and purchases during the period 1 April 2011 - 31 October 2011 were as follows:

	Value of Supplies £
April	5,000
May	6,000
June	6,500
July	9,500
August	11,500
September	7,500
October	5,100

All her supplies will be standard rated for VAT purposes. (Assume a standard rate of VAT of 17.5% throughout for the purposes of this question.)

Ruth will be able to claim input VAT of £2,111.

Calculate the potential lost revenue in respect of which any failure to notify penalty will be calculated and explain the maximum and minimum percentages which could apply.

Answer 1

The default period is 1 May 2010 to 31 December 2010 (8 months).

G Ltd had sales of £150,000 in the default period - these are deemed to be VAT inclusive as these sales should have included $17\frac{1}{2}\%$ VAT.

$£150,000 \times 7/47 = £22,340$ output VAT due ('potential lost revenue' for calculation of penalty below).

The penalty is a percentage of this potential lost revenue.

A maximum penalty of 30% of £22,340 will apply (assuming that it is a careless mistake). This gives £6,702.

As there is less than 12 months between when G Ltd should have registered and actually registered for VAT the penalty may be reduced to nil as a result of an unprompted disclosure.

Answer 2

Adding up Fran's turnover on a monthly basis, we find that by the time she gets to the end of September 2010, she has turnover of £72,000.

This exceeds the VAT registration limit of £70,000.

Therefore Fran should have notified HMRC by the end of October and she should have charged VAT on her supplies from 1 November 2010.

She actually registered for VAT on 30 March 2011, so her default period is 5 months.

Sales in this 5 month period were £41,000. These are deemed to be VAT inclusive.

Credit can be given for input tax in the period, so the net VAT due is as follows:

	£
Output tax	
£41,000 × 7/47	6,106
Input tax (£500 × 5)	<u>(2,500)</u>
VAT due	<u>3,606</u>

Maximum penalty in this case likely to be 30% reduces to nil with unprompted disclosure within 12 months of the registration date.

Otherwise, HMRC are unlikely to accept advice given during a conversation on a training course as a reasonable excuse for Fran's delay in registering, unless she has something in writing which confirms the advice.

Answer 3

Ruth should have been registered for VAT from 1 May 2011 and should have charged VAT on her supplies from this point.

VAT due (supplies deemed VAT inclusive):

	£
£46,100 × 7/47 =	6,866
Less:	
Input VAT reclaimable	<u>(2,111)</u>
Potential lost revenue	<u>£4,755</u>

The failure was a deliberate but not concealed failure and Ruth made an unprompted disclosure to HMRC, therefore a penalty of between 20% and 70% of the potential lost revenue will be charged.