



TC05597

Appeal number: TC/2015/06943

***NATIONAL INSURANCE CONTRIBUTIONS – Class 2 contributions –
whether failure to pay contributions was due to ignorance or error –
whether ignorance or error was due to failure to exercise reasonable care –
appeal allowed***

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

STEPHEN ARENS

Appellant

- and -

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

**TRIBUNAL: JUDGE ASHLEY GREENBANK
 MRS SUSAN LOUSADA**

**Sitting in public at the Tribunal Centre, 8-10 Howard Street, Bedford on 18 July
2016**

The Appellant in person

Ms Sandi Connolly, officer of HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. The Appellant, Stephen Arens (“Mr Arens”), appealed against a decision of the Respondents (“HMRC”) that Mr Arens’s failure to pay Class 2 National Insurance contributions (“NICs”) for various periods in the years 1973/74 to 1989/90 and the years 1994/95 to 2007/08 within the prescribed period was attributable to Mr Arens’s ignorance or error and that such ignorance or error was due to Mr Arens’s failure to exercise due care and diligence.

2. As a result of the decision, Mr Arens was unable to make further contributions for the periods between 4 March 1974 and 3 February 1990 and between 28 August 1994 and 11 April 2008 and so was unable to qualify for a full state pension.

The summary decision

3. Following the hearing, the Tribunal gave a decision in summary form in accordance with rule 35(3)(a) of The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (the “Tribunal Rules”) allowing the appeal made by Mr Arens. The summary decision was issued on 26 July 2016.

4. The summary decision was given subject to the parties’ rights to request full written findings and reasons under rule 35(4) of the Tribunal Rules. The respondents have requested full written findings and reasons for the decision. This is the full decision.

5. The summary decision contained a number of errors that I have corrected in this full decision. In particular, in the summary decision, I referred to HMRC’s witness, Mrs Crawford, by an incorrect surname. I apologise for the error.

The evidence

6. We were provided with a bundle of documents by HMRC and a further bundle of documents by Mr Arens.

7. Mrs Lesley Crawford, an officer of HMRC, provided a witness statement and gave oral evidence. Mr Arens made submissions and gave oral evidence. We found both Mrs Crawford and Mr Arens to be honest and credible witnesses.

The facts

8. The facts in this case stretch across several decades. It is inevitable that, over that period of time, the parties’ recollection of events is not as clear as it might otherwise have been. Furthermore, HMRC’s record of correspondence with Mr Arens is not complete. In particular, we were asked to accept that letters and communications would have been sent to Mr Arens on the basis of Mrs Crawford’s evidence of the custom and practice of HMRC and its predecessor departments at the relevant time.

9. We have set out details of Mr Arens’s contribution record and his interaction with the various government departments that have administered the National Insurance contribution system over the years in [15] to [25] below. We have first set out a few details of Mr Arens’s working life which provide some context for the details of his contribution record.

Background

- 10. Mr Arens was employed in the years from 1965/66 to 1973/74.
- 11. Mr Arens became self-employed towards the end of the 1973/74 contribution year. He remained self-employed from 1974/75 until he retired in 2014/15 except for a period, which began in the tax year 1989/90 and ended in the tax year 1994/95, during which he was unemployed.
- 12. Mr Arens registered for income tax purposes with the Inland Revenue when he became self-employed. He engaged accountants when he became self-employed and for the remainder of his working life. He continued to employ an accountant during his period of unemployment to which we refer below. He relied on his accountants to handle all of his tax affairs.
- 13. Mr Arens has met his income tax liabilities and paid Class 4 NICs in all relevant years. He did not, however, pay Class 2 NICs after he became self-employed, although he was given credits for periods during which he was unemployed, as we describe below.
- 14. Mr Arens says that he was not aware of any deficiency in his National Insurance contribution record until he contacted the Pensions Service approximately two weeks before his 65th birthday. We accept his evidence.

Mr Arens’s contribution record

- 15. Mr Arens paid Class 1 NICs in the years from 1965/66 to 1973/74. The Department of Health and Social Security (“DHSS”) records appear to show some minor shortfalls in Mr Arens’s contribution record in some of the contribution years this period. Those records also indicate that Mr Arens was sent details of his contribution record for the relevant periods (1968/69, 1969/70 and 1973/74) from which he could have identified a shortfall in his contributions. There is no record of Mr Arens having made good any shortfall.
- 16. At the time at which he became self-employed, there was no obligation on self-employed earners to register with the DHSS. Self-employed earners were, however, required to obtain and stamp a contribution card to show payment of Class 2 NICs and to surrender that card at the end of the contribution year. The DHSS has no record of Mr Arens having surrendered a contribution card for the 1974/75 contribution year.

17. The DHSS records suggest that a notice was issued to record the fact that no contribution card had been received from Mr Arens for the 1974/75 contribution year. However, this notice was sent to an address at which Mr Arens was no longer residing. It was returned undelivered.
- 5 18. The system of recording NICs was computerized from 6 April 1975. Class 4 NICs were also introduced in this year. Mr Arens was not recorded as self-employed on the electronic record held by the DHSS when records were transferred into computerized form because the DHSS had not received a contribution card for the 1974/75 contribution year.
- 10 19. Between 6 April 1975 and 5 April 1996, self-employed earners were required to register separately with the DHSS and subsequently the Department of Social Security (“DSS”) for tax and NICs. There is no record of Mr Arens having registered separately for NICs in this period.
- 15 20. Mr Arens next came to the attention of the authorities when he became unemployed in the tax year 1989/90 following the collapse of his business. Mr Arens was not entitled to claim unemployment benefit at the time. He would not have been entitled to benefit even if he had paid Class 2 NICs in the period between 1974/75 and 1989/90.
- 20 21. In that tax year, Mr Arens notified the DSS of a new address. The notes on the DSS records suggest that a notice was sent to Mr Arens to that address setting out details of his National Insurance record. Mrs Crawford in her evidence directed us to the form of notice that should have been issued to Mr Arens. However, there remained no automatic registration process for self-employed earners at this time. So, even though he had notified the DSS of his address, Mr Arens was not automatically registered with the DSS for National Insurance purposes.
- 25 22. The National Insurance records indicate that Mr Arens was sent notices advising him of shortfalls in his contribution record for the periods from 1988/90 to 1995/96. There is no record of Mr Arens having contacted the authorities in this period regarding any shortfall.
- 30 23. No further notices were sent to Mr Arens after the notice for the 1995/96 year. Mrs Crawford explained that it was standard practice to send a notice to a contributor in most cases where a contributor had made some contributions in a given year, but there was a shortfall in contributions. However, if the contributor had made no contributions in a particular year, a notice would only be sent for the first year in which no contributions had been made. No notices would be issued in later years if
- 35 the contributor did not respond to the initial notice.
- 40 24. Mr Arens said that he could not recall having received a notice from the DHSS or the DSS at any point setting out the deficiencies in his contribution record. Before Mr Arens became unemployed in 1989/90 and registered for unemployment benefit, this was likely to be because the notices that were issued by the DHSS were being sent to an address which Mr Arens was no longer living.

25. When he became unemployed, his house was repossessed and it may well have been that notices were issued by the authorities to that address of which he was not aware. Since 1995/96, Mr Arens has been resident at a permanent address of which the authorities have been aware.

5 *Mrs Crawford's evidence*

26. Mrs Crawford gave evidence of the practice of the various Government departments that have administered the National Insurance system over the past few decades. We found her evidence extremely helpful in understanding the intricacies of the system and how they have changed over time. Mrs Crawford was also able to
10 interpret some of the records relating to Mr Arens's contributions even though she has had no direct involvement in Mr Arens's case.

27. Much of Mrs Crawford's evidence is reflected in the statement of facts that we have set out above. There were, however, various other issues referred to in Mrs Crawford's evidence to which we should also refer.

15 28. Mrs Crawford referred to the various notes on tax returns and notices issued with tax assessments which should have been seen by Mr Arens and his advisers. The standard form notices include notes setting out the obligations of self-employed earners to pay both Class 2 and Class 4 NICs and the obligations of self-employed earners to register for payment of Class 2 NICs.

20 29. Mrs Crawford was asked whether the relevant Government department ever took steps to trace earners who were missing from or who had fallen off the register. She confirmed that no steps were taken to trace such people. The obligation was on self-employed earners to register themselves. She referred to regulation 88 of the Social Security (Crediting and Treatment of Contributions and National Insurance Numbers)
25 Regulations 2001 (the "2001 Regulations") in this respect.

30. Mrs Crawford was also asked whether the DSS or DHSS would have been aware that Mr Arens had registered for payment of income tax. Mrs Crawford said that the DHSS or DSS would not necessarily have known that Mr Arens was making his income tax returns and paying his income tax and Class 4 NICs.

30 *Mr Arens's evidence*

31. Once again, much of Mr Arens's evidence is reflected in the statement of facts that we have set out above. There were, however, various other aspects of his evidence to which we should also refer.

32. Mr Arens was asked whether he had been aware of his obligations to account for
35 NICs. He said that he was, but that he had thought that he was doing everything that he should be doing. He had made his returns and relied on his accountants to "get the tax right". He accepted that he may well have seen the notices on the tax returns and notices of assessment. However, those notices did not cause him to think that he was

not meeting all of his obligations. As far as he was aware, his NICs were being paid. He did not make a distinction between Class 2 NICs and Class 4 NICs.

33. Mr Arens was also asked what attempts he had made to notify the DHSS or the DSS. He accepted that he had not been aware of a separate obligation to notify the DHSS or the DSS. He had not seen any reason to contact the DHSS or the DSS because he thought he was fulfilling all of his obligations.

These proceedings

34. Mr Arens reached stated pension age on 12 November 2014. He contacted the Pension Service two weeks before his 65th birthday. He was initially told that he would be entitled to a 60% basic state pension. However, following a review he was informed that his pension would be reduced to a 43% basic state pension as a result of the removal of certain credits which had been wrongly attributed to his record for the period between his 60th and 65th birthdays.

35. Mr Arens was informed that his record had been updated to show him as registered as self-employed from 31 August 1994. He was advised that he should have paid Class 2 NICs for the 1994 to 2014 tax years but it was now too late for him to pay the contributions for the period from 28 August 1994 to 5 April 2008. An absolute waiver was granted to Mr Arens in respect of his liability to contribute the Class 2 NICs for this period.

36. Mr Arens was sent a bill for £946.15 in respect of Class 2 NICs for the period from 6 April 2008 to 5 April 2014. Mr Arens paid this amount on 26 February 2015. The payment of the additional Class 2 NICs increased the number of qualifying years from 13 to 19 and resulted in an increased pension for Mr Arens of 63% of a basic state pension.

37. There followed correspondence in which Mr Arens challenged the decision not to permit him to make further contributions.

38. On 14 August 2015, HMRC sent a notice of decision to Mr Arens. It confirmed HMRC's decision that Mr Arens could not pay any Class 2 NICs for the period from 4 March 1974 to 3 February 1990 or for the period from 28 August 1994 to 11 April 2008 on the grounds that any such contributions would be outside the prescribed time limits and, if paid, would be treated as not having been paid for the purposes of any contributory benefit.

39. The notice was accompanied by a letter providing an explanation of the decision. The letter informed Mr Arens that, although HMRC was satisfied that Mr Arens's failure to pay contributions was attributable to his ignorance or error, it was not satisfied that that ignorance or error was not the result of his failure to exercise due care and diligence (within regulation 6 of the 2001 Regulations).

40. On 2 September 2015, Mr Arens wrote to HMRC and requested an independent review of the decision.

41. On 2 November 2015, HMRC wrote to Mr Arens to explain that the independent review had been concluded and that the original decision had been upheld.

42. Mr Arens appealed against the decision.

The applicable legislation

5 43. Regulation 4 of the 2001 Regulations imposes time limits on the making of Class 2 NICs.

44. For Class 2 NICs payable in respect of a contribution week before 5 April 1983, regulation 4(2) provides that contributions that are paid more than two years after the year in which the liability arises are treated as not paid.

10 45. For Class 2 NICs payable in respect of a contribution week after 5 April 1983, regulation 4(3) provides that contributions that are paid more than six years after the year in which the liability arises are treated as not paid.

46. The legislation, however, permits Class 2 NICs to be made outside the six year time limit in certain limited circumstances. These circumstances are set out in
15 regulation 6 of the 2001 Regulations.

47. Regulation 6(1) provides so far as relevant:

“(1) In the case of a contribution paid by or in respect of a person after the due date, where:

20 (a) the contribution is paid after the time when it would, under regulation 4 or 5 above, have been treated as paid for the purposes of entitlement to contributory benefit; and

25 (b) it is shown to the satisfaction of an officer of the Inland Revenue that the failure to pay the contribution before that time is attributable to ignorance or error on the part of that person or the person making the payment and that that ignorance or error was not due to any failure on the part of such person to exercise due care and diligence

30 an officer of the Inland Revenue may direct that, for the purposes of those regulations, the contribution shall be treated as paid on such earlier day as the officer considers appropriate in the circumstances, and those regulations shall have effect subject to any such direction.”

48. Section 11 of the Social Security Contributions (Transfer of Functions, etc.) Act 1999 allows an appeal against any decision to be made to the Tribunal.

35 Issues before the Tribunal

49. It is accepted by both parties that Mr Arens’s failure to pay the Class 2 NICs was due to his “ignorance or error” for the purpose of regulation 6(1)(b) of the 2001 Regulations.

50. The only issue before the Tribunal is whether that ignorance or error was or was not due to a failure on the part of Mr Arens “to exercise due care and diligence”.

The parties’ arguments

51. Mr Arens makes the following points:

- 5 (1) He had registered as self-employed for tax purposes and paid his income tax liabilities and Class 4 NICs in all relevant periods.
- (2) He had employed reputable accountants to handle his tax affairs. He had assumed throughout that his National Insurance liabilities were being taken into account and dealt with appropriately. His accountant always kept the Inland Revenue or HMRC informed of his address.
- 10 (3) As far as he is aware, he has not received any notification from the authorities to suggest that there was any shortfall in his contributions.
- (4) He was not aware of any need to stamp his own contribution card once he became self-employed. His employer did not return his contribution card to him.
- 15 (5) His tax affairs had been under investigation twice. He had been unemployed in the period between 1990 and 1994. At no stage was any reference made to the shortfall in his contribution record.
- (6) He had reviewed his tax returns. He could not say that he had read and understood all of the details. He was aware that he was paying some NICs and had assumed that his liabilities were being met.
- 20 (7) He referred to the decision of the First-tier Tribunal in *Dr Jeremy Schonfield v HMRC [2013] UKFTT 244* in support of his contention that it was reasonable for him to have relied on his accountants to deal with his NICs.
- 25

52. Ms Connolly makes the following points for HMRC:

- (1) Mr Arens should have applied for a contribution card when he became self-employed in 1974.
- (2) Mr Arens should have notified the DHSS, and subsequently the DSS, that he was self-employed.
- 30 (3) Whilst the National Insurance authorities do seek to ensure that contributors are informed of their contribution records, it is up to the contributor to ensure that his or her contribution record is properly maintained. The fact that advice which is promulgated by the authorities is not received by a contributor cannot assist a contributor who has failed to seek the necessary advice.
- 35 (4) Mr Arens should have been aware of his obligations to pay Class 2 NICs. In particular, when Mr Arens became unemployed, he should have been advised of the requirements of the National Insurance scheme. When

5 Mr Arens registered for income tax purposes, he should have received notes with his tax return including information about Class 2 NICs and the need to register with the DHSS or the DSS. From 1996, the self-assessment return completed by Mr Arens explained the obligations of self-employed people to pay Class 2 NICs. This should have prompted Mr Arens to make enquiries about his National Insurance position.

(5) Mr Arens admitted that he did not read his completed tax returns and relied upon his advisers to do this for him.

10 (6) Mr Arens had instructed four different firms of accountants since he became self-employed in 1974. It was highly unlikely that none of these professionals was aware of his need to pay Class 2 NICs.

15 (7) In the final analysis, the onus was on Mr Arens to take steps to ensure that he met his obligations to register for and pay NICs. Ms Connolly referred to extracts from the judgment of Owen J in *Walsh v Secretary of State for Social Security* (1994) (unreported), the decisions of the First-tier Tribunal in *Catherine Thacker v HMRC* [2012] UKFTT 698 and the decision of the Special Commissioners in *Philip Langley Rose v HMRC* [2006] UKSPC SPC00574 in support of her submission.

Discussion

20 53. As we have noted above, we were referred to extracts from various cases by HMRC and by Mr Arens. We have considered the cases to which we were referred by the parties. We have also considered the decision of the Court of Appeal in *HMRC v Kearney* [2010] EWCA Civ 288, to which we were not referred by the parties but which is discussed in the decision of the First-tier Tribunal in the case of *Dr Jeremy Schonfield v HMRC* to which Mr Arens referred.

54. We do not intend to undertake an exhaustive review of the cases. We have set out below the main principles that we draw from the authorities to which we have been referred.

30 (1) First, it is the duty of the contributor, in this case Mr Arens, to maintain his National Insurance contribution record (see *Walsh* at page 4F of the judgment).

(2) Second, there is no duty on the authorities to “chase up” the contributor to ensure that he or she continues to make contributions (see *Walsh* at page 4F and *Kearney* at [24]).

35 (3) Third, the onus is on the contributor to show that the ignorance or error was not due to any failure on his or her part to exercise due care and diligence (see *Kearney* at [25]).

40 (4) Fourth, what amounts to a lack of due care and diligence will depend upon all of the circumstances of the case (see *Walsh* at page 11A-B of the judgment). It is the duty of the Tribunal to consider and balance all the relevant factors (see *Kearney* at [34]).

55. In the cases to which we were referred, the courts and tribunals have also given some guidance as to the meaning of “care” and “diligence” in this context. The cases suggest that a lack of care means a lack of concern, whereas a lack of diligence means a failure to apply oneself to the issue (see *Kearney* at [27]). On this basis, diligence
5 does require some form of positive action on the part of the contributor. The cases suggest that this may involve some duty to enquire of his or her obligations, although it may not be necessary for those enquiries to be made of HMRC (see, for example, *Kearney* at [29]).

56. We have come to the view that, on the facts of this case, Mr Arens should be
10 regarded as having exercised due care and diligence. We have set out in the paragraphs below the factors that we have taken into account.

57. We noted that, in many of the cases to which we were referred, the contributor’s knowledge of the National Insurance scheme was an important factor. Mr Arens was aware of the existence of the National Insurance scheme and of his obligations to
15 make contributions. He paid contributions whilst he was employed in the period up to and including the tax year 1973/74 and has paid Class 4 NICs since he became self-employed. As soon as he was aware of the shortfall in his contribution record took steps to make the contributions required to complete his record.

58. That having been said, Mr Arens is not a professional person. He is a tradesman
20 with little financial or legal expertise. He has been careful to ensure that his tax and National Insurance obligations are placed in the hands of professionals on whom he relied to meet his tax and National Insurance obligations. While he was aware that he had obligations to pay tax and NICs, he honestly believed that he was his paying tax and NICs. He was not aware of the distinction between Class 2 NICs and Class 4
25 NICs.

59. Ms Connolly stressed that the duty is on the contributor to register and to maintain his or her record. However, the fact that a contributor has not registered or maintained their contribution record cannot of itself be conclusive evidence of a lack of care or diligence. The provisions of regulation 6 must permit some circumstances
30 in which a contributor fails to register or maintain contributions, but is permitted to make a late payment. While we accept that Mr Arens cannot completely absolve himself of his duty to maintain his record, for a man in his position, we believe that he has demonstrated the relevant level of diligence by placing his affairs in the hands of an appropriate adviser.

60. As we have mentioned previously, we found Mr Arens to be an honest and
35 credible witness. We accept his evidence that he was not aware of having actually received a notice setting out the shortfalls in his contributions.

61. Given the time that has elapsed, it is not possible to say whether or not Mr Arens did in fact receive these notices. However, there are good reasons why, even if
40 notices were issued in accordance with the usual practice of the DHSS and the DSS at the time, this might have been the case for many of them. This is partly due to an accident of circumstances in which Mr Arens changed address regularly at relevant

times and so did not receive the notices that were issued by the DHSS or the DSS. The position has not been helped by the timing of Mr Arens's becoming self-employed, which happened to coincide with the transfer of the National Insurance records into computerized form, or by the policies of the relevant authorities not to issue further contribution notices if contributors did not respond to an initial notice.

62. In reaching our decision, we acknowledge that the tax return sent to Mr Arens and his advisers and the notices contained in them would have referred to the obligations of Mr Arens to make Class 2 NICs. However, there was nothing in them that would jolt Mr Arens into thinking that he needed to take any positive action. His understanding was that he was meeting his obligations. The notices included in the returns would not have caused Mr Arens to believe that he was not fulfilling his duties.

63. We also acknowledge that the test is a relatively strict test for good reasons. The time limits on contributions are generally necessary in order to prevent contributors from delaying their contributions but claiming relevant benefits. However, we do not believe that Mr Arens has deliberately set out to game the system. Mr Arens has met all his tax and Class 4 NIC liabilities and as soon as he was aware of the shortfall in his contribution record took steps to make the contributions required to complete his record. In our view, Mr Arens slipped between the gaps in the system. In the circumstances, he should be regarded as having exercised due care and diligence and permitted to make the additional contributions.

Decision

64. We allow this appeal.

Rights of appeal

65. 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.

ASHLEY GREENBANK
TRIBUNAL JUDGE

RELEASE DATE: 10 JANUARY 2017