



**TC07139**

**Appeal number: TC/2017/02132**

*VAT – denial of VAT credit – assessments to recover VAT credit – penalties  
– returns to best of ability in absence of records – whether deliberate  
behaviour*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**PHILIP NORMAN BAGSHAW**

**Appellant**

**- and -**

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

**Respondents**

**TRIBUNAL: JUDGE ANNE FAIRPO  
MS SUSAN STOTT**

**Sitting in public at Nottingham on 11 October 2018**

**The Appellant appeared in person**

**Mr Smithson, presenting officer, for the Respondents**

## DECISION

### Introduction

1. This is an appeal against:
  - (1) A decision under s25(3) Value Added Tax Act (“VATA”) 1994 to deny claims for VAT credit for the VAT periods 04/10 and 04/11
  - (2) Assessments under s73 VATA 1994 to recover VAT claimed and repaid for the VAT periods 10/10, 01/11, 07/11, 10/11 and 01/12
  - (3) Penalties issued under Sch 24 FA 2007 for inaccuracies within the periods in dispute

### Background

2. The appellant registered for VAT in 2008 as a sole trader providing telecommunications supplies and repairs. The registration was cancelled in 2013 as he ceased trading in 2012. During the period of registration, only one VAT return was filed (for the period 04/08).
3. As no returns had been filed, HMRC issued central assessments under s73(1) VATA 1994, totalling £14,036.
4. In October 2013 the appellant was contacted by HMRC and advised them that he had ceased trading in December 2012. He was advised that he needed to complete the outstanding VAT returns. The appellant requested, and was granted, two weeks to complete the returns.
5. On 29 May 2014 the appellant contacted HMRC Debt Management about the debt arising from the central assessments and was again advised that he needed to submit the outstanding returns within two weeks if he wished to dispute the amount owed.
6. The appellant subsequently filed VAT returns as follows:
  - (1) 07/08 to 04/09: returns filed on 5 May 2016
  - (2) 07/09 to 01/10: returns filed on 6 May 2016
  - (3) 04/10 return filed on 10 May 2016
  - (4) 07/10 return filed on 27 May 2016
  - (5) 10/10 to 01/12: returns filed on 01 June 2016
7. The appellant’s returns showed a net VAT liability of £1,492 with repayment claims made for the 07/08, 10/08, 04/10, 10/10, 01/11, 04/11, 07/11, 10/11 and 01/12 periods.

8. Several of the repayment claims were paid by offset against amounts due for other periods, but a credibility check was initiated by HMRC in relation to the 04/10 and 04/11 periods repayment claims. The officer decided to carry out checks on the other returns filed as well.

9. During a visit by HMRC to the appellant on 21 June 2016, the appellant explained that he had no records for the business.

10. As there was no supporting evidence provided, HMRC reduced all repayment claims made by the appellant to nil and issued assessments totalling £5,470, for recovery of the VAT which had been repaid by offset. The VAT credits for the 04/10 and 04/11 periods, totalling £3,695, were denied.

11. The returns showing an amount due to HMRC were not challenged by HMRC as there was no material on which to base an alternate assessment.

### **Appellant's case**

12. The appellant stated that he had no financial understanding or knowledge and could not afford professional advice.

13. The appellant explained, by way of background, that his business and books had been run by someone else several years earlier. The records of the business had been disposed of by someone other than the appellant, and the appellant did not find out until he checked storage.

14. This other person ran the business and undertook all the invoicing and other administration. The appellant explained to the Tribunal that he preferred not to explain why this person was running the business on his behalf. The appellant said that he had assumed, incorrectly, that this person was keeping all the records and books up to date. It was not until the problems with the VAT returns arose that he realised that there were no records available.

15. The appellant also explained that the business had been in difficulty for some time due to general pressures in the economy. Two of the main telephone manufacturers had gone into liquidation and the market for their phones had disappeared. The appellant's stock of the phones of one of these manufacturers was eventually sold for scrap. The appellant had attempted to adjust, offering refurbishment of phones, and selling used telephones. He had tried to make money by recycling plastics and initially received £300 per ton for such plastics but, within three months, had to pay for the materials to be taken away as China was no longer accepting plastics for recycling.

16. The appellant accepted that, as a sole trader, the business and its tax obligations were his responsibility.

17. He accepted that he should have filed the returns on time and that the returns were not in fact filed on time. He also accepted that some money was owed to HMRC, but he had had difficulties in communicating with HMRC.

18. The appellant stated that he had made several phone calls to HMRC about his VAT returns, asking to speak to someone about his VAT position. He was told that this was no longer possible as there were no offices open to the public to visit for assistance.

19. Accordingly, he was unable to obtain advice from HMRC as to how he should complete his returns without records. Eventually, he completed the returns as best he could from memory.

20. The appellant stated, however, that one of the returns (the return for the 07/10 period) which was recorded as received by HMRC was not submitted by him. The appellant explained that he believed that someone else had accessed his computer and had submitted the return. The return was filed late on a Friday evening before a bank holiday. The appellant submitted that the output tax declared for that period would have been a lot lower; in addition, the return is inconsistent with other returns which the appellant had submitted as it contains only output tax of £7,000 and no claim for input tax.

21. The appellant accepted that the returns could not be accurate, but he considered that they fairly reflected the activity of the business over the relevant VAT periods. The appellant stated that, if the business had been making the level of profit implied by HMRC's assessments, he would have had more assets and his wife would have been able to retire at the proper time instead of continuing to work until 2017 in order to pay off loans taken out to support the business.

22. The appellant explained that he could not provide evidence for the following reasons:

(1) no bank statements were available as the bank had closed the account and he was reluctant to "poke" the bank because he was aware that the account was overdrawn by approximately £4,500 when it was closed;

(2) his two main customers had ceased trading, which is where his business problems had started, and so he could not obtain any information from them.

23. The appellant did accept that he could produce his personal account bank statements, if required, but had not done so.

24. Accordingly, the appellant submitted that his estimates were closer to the reality of the business than HMRC's "guesswork" and that HMRC should have undertaken some enquiries to establish a more accurate figure.

25. In addition, the appellant argued that HMRC had acted unfairly as they had not amended VAT returns which showed an amount of VAT due to HMRC.

26. The appellant explained that he had no assets and received only his state pension and a small private pension. His wife's pension was similarly minimal. They had two old cars (one 23 years old, one 12 years old).

*Whether disclosure was prompted*

27. The appellant argued that the disclosure was not prompted: he had been trying to tell HMRC for years that he did not have records available to be able to accurately complete the VAT returns. He explained that it was not until Officer Morley visited him, as part of the credibility check, that he had an opportunity to talk to anyone at HMRC about the problem. The appellant stated that he had told Officer Morley at the start of the visit that records were not available and that all of the returns had been prepared in the same way.

*Whether actions were deliberate*

28. The appellant argued that he had not made deliberate errors in completing the returns: he had no other way to complete the returns, and HMRC had insisted that he complete the returns in order to be able to displace the central assessments which had been raised when returns were not filed.

29. The appellant submitted, therefore, that his actions could not be regarded as deliberate when no other option was available to him.

**HMRC's case**

30. The appellant had filed VAT returns which significantly reduced the VAT debt arising from central assessments which had been raised when returns were not filed on time. A number of the VAT returns resulted in a repayment claim; as the appellant's business dealt solely with standard-rated supplies, HMRC submitted that these figures were abnormal as in normal circumstances output tax would exceed input tax and result in VAT due on the return.

31. The appellant had filed the returns without any supporting records to confirm the declarations made. HMRC submitted that the appellant was required by law to keep records for VAT purposes for a period of at least six years (para 6(3), Schedule 11, VATA 1994) and had failed to do so.

32. HMRC submitted that the appellant had supplied no evidence of entitlement to input tax deductions, contrary to Regulation 29 of the VAT Regulations ("VATTR") 1995. The appellant had also not filed any self-assessment tax returns and no accounts were available.

33. In the absence of records or evidence to support the VAT returns, HMRC denied the VAT credits claimed in the 04/10 and 04/11 periods and raised assessments to recover the VAT credited to the appellant for the 10/10, 01/11, 07/11, 10/11 and 01/12 periods as the VAT credits claimed by the appellant had already been credited to him.

34. HMRC submitted that the burden of proof was on the appellant to produce evidence of the VAT liability for each period. In the absence of evidence, HMRC will make an assessment of tax on the basis of "best judgement". In this case, in the

absence of any evidence from the appellant, HMRC had exercised best judgement on the information available in line with the guidance available from case law.

*Whether the disclosure was prompted*

35. HMRC submitted that a disclosure about an inaccuracy should be regarded as “unprompted” if made at a time when the person making it has no reason to believe that HMRC have discovered or are about to discover the inaccuracy, otherwise it is “prompted”.

36. HMRC submitted that the disclosure was prompted, as the appellant did not tell HMRC about the inaccuracy before having reason to believe that HMRC had discovered it or were about to discover it. No disclosure was made before the appellant was contacted by HMRC to arrange a visit to confirm the accuracy of the returns.

*Whether the inaccuracy was deliberate*

37. HMRC submitted that the inaccuracy was deliberate but not concealed, as the appellant knew that the VAT returns were inaccurate when he submitted them, as he was relying on his memory rather than any records.

**Relevant law**

38. The legislation relevant to the present appeal is contained in VATA and the VATRR. For claims to input tax:

(1) s24 VATA defines input tax as the VAT incurred on supplies received and used for the purposes of a taxpayers business. The section also provides for the making of regulations specifying what evidence and documentation is required to support a claim to input tax.

(2) Regulation 29 VATRR provides that input tax claims are required to be evidenced by invoices received from the taxpayer’s supplier bearing specified information. There is however, a provision that permits HMRC to accept alternative evidence supporting such claims to input tax.

39. s73 VATA provides that where a taxpayer either fails to make returns or makes returns which HMRC consider to be incorrect then HMRC may raise assessments to the best of their judgement.

**Discussion**

40. The questions before this Tribunal were whether HMRC had used best judgement in their assessments and whether, to determine the penalty, the appellant’s behaviour was deliberate and prompted.

*Whether “best judgement” applied*

41. The question of when and whether assessments are made in HMRC’s “best judgement” is set out principally in *Pegasus Birds* [2004] EWCA 1015 in which the Court of Appeal stated that the relevant question when assessing best judgment had been set out in the previous case of *Rahman (no 2)* [2003] STC 150:

“whether the mistake is consistent with an honest and genuine attempt to make a reasoned assessment of the VAT payable; or is of such a nature that it compels the conclusion that no officer seeking to exercise best judgment could have made it. Or there may be no explanation; in which case the proper inference may be that the assessment was indeed arbitrary.”

42. Accordingly, *Pegasus Birds* established that the Tribunal’s primary task is to find the correct amount of tax by reference to the material and evidence available to it at the time of the hearing. If the Tribunal finds an assessment has not been made in exercise of best judgment it then has a discretion whether to amend the assessment or conclude that it is void.

43. The Court of Appeal states that it is only where there is not an “honest and genuine” attempt to ascertain the correct tax by reference to the evidence available that the whole assessment should be set aside. It is therefore clear that assessments should only be set aside where the basis on which the assessment was raised and/or its amount is wholly unsustainable on the evidence available.

44. The effect of HMRC’s actions with regard to the appellant’s VAT returns can be summarised as follows:

- (1) The appellant’s output tax figures have been accepted; and
- (2) The appellant’s input tax deductions have been accepted to the extent that they do not create a repayment claim for the appellant and denied to the extent that a repayment claim arises, and the VAT returns amended accordingly.
- (3) Where a repayment claim has been credited to the Appellant, assessments have been raised to recover the amount credited.

45. The first question for this Tribunal, following *Pegasus Birds*, is to determine whether the decision to amend the VAT returns by denying input tax credits to the extent that they give rise to a repayment claim represents the correct quantum of tax due, by reference to the evidence and material available to the Tribunal.

46. No evidence and material was available to us: the appellant’s evidence is that the deductions were arrived at from memory and not from any supporting documentation. The appellant suggested that he could have provided personal bank statements but he has not done so, and he preferred not to contact the bank where his business account had been held.

47. Despite the lack of documentation, HMRC did not deny all input tax credits but, instead, denied them only to the extent that the deductions created a repayment claim.

Accordingly, the appellant was given credit for input tax to the extent that his claim did not result in a repayment claim arising.

48. As there was no dispute that the appellant was trading, it seems to us that he should be allowed some measure of input tax deduction.

49. The case of *Bonomini* [2017] UKFTT 683 considered that a credit for 5% of output tax assessed would be reasonable: in this case, HMRC's methodology provides a considerably greater deduction for each period than that which would be available applying the 5% credit referred to in *Bonomini*.

50. HMRC did invite the Tribunal to use its powers under s84(5) VATA 1994 to deny more of the input tax deductions if we thought it appropriate, in line with *Bonomini*, but we have declined to do so. HMRC has had the opportunity to raise higher assessments but did not and are now out of time to raise further assessments, and we see no reason to disturb the position.

51. Following the test in *Pegasus Birds*, therefore, we find that HMRC have made an "honest and genuine" attempt to establish the VAT payable and have acted in best judgement and, indeed, appear to have given the appellant considerable benefit of the doubt in making their assessments. We find on the basis of the evidence and material available to us, that the amount of VAT payable as a result of HMRC's actions is not more than the correct amount and make no amendment to the assessments.

52. We noted the appellant's submission that HMRC had acted unfairly as they had made no amendments to the VAT returns which showed an amount due to HMRC. Following the decision in *Hok* [2010] UKUT 363, this Tribunal has no power to consider allegations that HMRC has acted unfairly in this context. However, we observe that the methodology used by HMRC to give credit for input tax, which we have found was in best judgement, could not have given rise to any amendments to these returns.

53. Dealing also with a point raised by the appellant in relation to a period which was not amended by HMRC: we noted the appellant's explanation that his 07/10 return may have been submitted to HMRC by someone who accessed his computer, and that the return does not properly reflect the economic position for that VAT period. He had contacted HMRC to try to change the return but had been advised that he could only do so by completing an error correction letter, which required a signed declaration that it was true and accurate. He could not sign this.

54. No evidence was put forward by the appellant to explain who may have accessed his computer, nor why they would have submitted a VAT return on his behalf. No evidence was provided to show that any input tax was due for that period. The amount on the return was not an amount assessed by HMRC and this Tribunal has no power to enquire into amounts on returns where there has been no assessment by HMRC.



55. Following *Hok*, this Tribunal also does not have jurisdiction to consider whether HMRC have acted fairly in not amending that return in the absence of an error correction letter from the appellant.

*Whether disclosure was prompted*

56. The appellant's evidence was that he repeatedly tried to explain to HMRC in telephone calls, before the returns were filed, that he had no records with which to complete the returns and that it was not until Officer Morley's visit that he was able to explain this.

57. No evidence of these calls was apparent in the HMRC debt management notes within the bundle provided to the Tribunal, although it was agreed that these are not a verbatim record of telephone calls, and the appellant did not suggest that he had tried to contact HMRC in writing to explain the lack of records.

58. Officer Morley's evidence was that the appellant explained the lack of records to Officer Morley when, at the beginning of the meeting, Officer Morley asked to see them.

59. On balance, as we considered that the appellant was a credible witness, we find that the appellant had informed HMRC that he had no records with which to prepare the returns before HMRC's visit (indeed, before he submitted the returns) and that the disclosure was, therefore, unprompted.

*Whether the behaviour was deliberate*

60. We considered that the appellant was a credible witness to the extent that he was prepared to explain his actions. There were clearly issues relating to the involvement of at least one other person in the operation of the business which he was not prepared to discuss with HMRC or the Tribunal and which appears to have led to the lack of records to support VAT returns.

61. The appellant's evidence was that he had no alternative course of action other than to submit VAT returns which were estimated and completed to the best of his ability in the absence of records, but that it was not a deliberate action on his part to submit inaccurate returns.

62. HMRC argued that, as he knew the returns were inaccurate when he submitted them, he had deliberately submitted the inaccurate returns.

63. We were not taken to any case law dealing with what constitutes deliberate behaviour but consider that case law has established that a deliberate action requires a taxpayer to specifically take an action (including failure to take action) that leads to the inaccuracy in the return.

64. We consider that the appellant in this case was aware that there would be inaccuracies in his return but that he considered that he had completed the returns to

the best of his ability and that there was no other alternative course of action available to him, at the time of filing, that would result in a more accurate return.

65. From the evidence before us, we consider that the inaccuracies arose as a result of the appellant's decision to allow someone else to run his business and undertake the administration of the business, and the subsequent failure of that person to do as the appellant had expected. There was no suggestion that this was done with any regard, or lack of regard, towards the appellant's tax obligations on the part of the appellant.

66. On balance, we consider that the inaccuracies therefore arose from carelessness on the part of the appellant, in relying on another person to deal with tax matters and keep tax records in respect of his business, rather than a deliberate action on the part of the appellant with regard to the returns themselves.

#### *Penalty re-calculation*

67. As we have found that the inaccuracy was careless rather than deliberate, and that the disclosure was unprompted, the minimum penalty is therefore 0% and the maximum penalty is 30% of the potential lost revenue.

68. HMRC gave a 25% reduction for "telling" them about the inaccuracy, out of a possible 30%. They also gave the maximum 40% reduction for "helping" HMRC understand the inaccuracies. No reduction was given for access to records.

69. Given that we find that the appellant told HMRC about the lack of records and his consequent inability to provide an accurate return prior to the visit by HMRC and, indeed, prior to the submission of the return, we consider it appropriate to increase the "telling" reduction to 30%.

70. As no records were provided, and the appellant's evidence was that he could have provided at least personal bank statements, we agree that no reduction should be given for access to records. We also agree with the maximum 40% reduction for "helping".

71. We consider that the reduction should, therefore, be 30% plus 40% = 70%.

72. The penalty is therefore calculated as follows:

- (1) Difference between minimum and maximum penalty: 30
- (2) Applying the reduction:  $30 \times 70\% = 21\%$
- (3) The penalty percentage rate is therefore  $30\% - 21\% = 9\%$

73. Applied to the potential lost revenue for the relevant periods gives the following penalty amounts:

- (1) 04/10 – PLR £1,813 – penalty £163.17
- (2) 04/11 – PLR £1,882 – penalty £169.38

- (3) 10/10 – PLR £2,144 – penalty £192.96
- (4) 01/11 – PLR £197 – penalty £17.73
- (5) 07/11 – PLR £2,115 – penalty £190.35
- (6) 10/11 – PLR £643 – penalty £57.87
- (7) 01/12 – PLR £371 – penalty £33.39

74. The total penalty amount is therefore reduced from £4,330.43 to £824.85.

### **Conclusion**

75. The appeal is dismissed with regard to the denial of input tax for the 04/10 and 04/11 periods and the assessments to recover VAT credits for the periods 10/10, 01/11, 07/11, 10/11 and 01/12. The appeal is partially upheld in relation to the penalty amounts which have been reduced to a total amount of £824.85 as set out in paras 67-74.

76. 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.

**ANNE FAIRPO  
TRIBUNAL JUDGE**

**RELEASE DATE: 14 MAY 2019**