[2016] UKFTT 249 (TC)

TC05024

Appeal number: TC/2015/04443

VALUE ADDED TAX – penalties – penalty for inaccurate return – whether error "deliberate but not concealed" – paragraph 3 Schedule 24 Finance Act 2007 – no – appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

AUXILIUM PROJECT MANAGEMENT LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE ASHLEY GREENBANK
MICHAEL BELL ACA CTA

Sitting in public at Fox Court, 30 Brooke Street, London EC1N 7RS on 22 February 2016

Mr Clive Vernon of Vernon Associates, for the Appellant

Mrs Rita Pavely, officer of HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal against the decision by the Respondents ("HMRC") to impose a penalty under Schedule 24 of the Finance Act 2007 on the grounds that the Appellant, Auxilium Project Management Limited ("APM") provided to HMRC a VAT return which contained an inaccuracy for the three month period ended 30 September 2014 (the 09/14 period).

2. The penalty was imposed by a notice dated 17 March 2015 and was calculated on the basis that the inaccuracy was "deliberate but not concealed" as defined in paragraph 3(1) of Schedule 24 to the Finance Act 2007. The penalty was in the amount of £7,878.60.

3. APM does not dispute that the VAT return for the 09/14 period contained the inaccuracy. The only issue before the Tribunal is whether or not the inaccuracy was "deliberate" within the meaning in paragraph 3 of Schedule 24.

The hearing

4. HMRC produced a bundle of documents for the hearing. Both HMRC and APM produced additional documents at the hearing. We accepted all of these documents as evidence.

5. At the hearing, we heard witness evidence from Mr Clive Uren, officer of HMRC and from Ms Gillian Edgar, a director of APM. We also heard witness evidence from Mr Vernon.

6. As much of this decision turns on the evidence of Ms Edgar, we should say at the outset that we found her to be an honest and credible witness. We accept her evidence.

Facts

7. Ms Edgar is the sole shareholder in APM. Ms Edgar is also the sole director.

8. The company carries on business providing project management services in the construction field often in the public sector through the agency of Ms Edgar.

9. Ms Edgar used to provide her services through another company, C&D Consultants Southern Limited ("C&D"). She was formerly a director of that company. The other directors were Mr Dale Bennett and Mr Crawford Donachie. Mr Bennett was Ms Edgar's former husband.

10. At some point in 2014, it was decided to wind-up the business of C&D. The main reason for this decision was the separation of Ms Edgar and Mr Bennett. Ms Edgar set up APM to continue the provision of her project management services. Mr Bennett and Mr Donachie set up a new company in order to carry on their business.

11. Ms Edgar had taken over responsibility for the preparation of VAT returns for C&D with effect from the first quarter of 2014.

12. When she set up APM, Ms Edgar engaged Vernon Associates as its auditors. She also engaged Vernon Associates to deal with VAT compliance issues for APM.

13. APM initially accounted for VAT in accordance with the flat rate scheme. It moved to the standard cash basis for the period 09/14, the period to which this appeal relates. APM files its VAT returns electronically. So the final date for the submission of the return for the 09/14 period was 7 November 2014.

14. On 6 November 2014, the day before the return was due to be submitted, Mary Stephenson, an employee of Vernon Associates, contacted Ms Edgar by email to notify her that she (Ms Stephenson) had not submitted the VAT return for the 09/14 period. She asked Ms Edgar to supply relevant information that she required to complete the return.

15. Ms Stephenson also mentioned that she would not be in the office the following day, but that Faye Taylor, a newly qualified assistant, would be able to complete the return and arrange for it to be filed.

16. Ms Edgar sent the information to Vernon Associates that evening by email. The attachment to the email was a five page spreadsheet. The first page of the spreadsheet was a schedule showing the cash receipts of APM in the 09/14 period, the amount of VAT which was included in each payment, and the receipt net of VAT.

17. The spreadsheet showed 13 cash receipts from C&D in the period between 4 August 2014 and 22 August 2014 in an aggregate amount of £236,362 made up of 11 payments of £20,000, one payment of £1,000 and one payment of £15,362. The payments had been made in this way to deal with restrictions that were imposed on the operation of C&D's bank accounts.

18. The receipts from C&D are shown as not including any amount in respect of VAT. Ms Edgar said that this was because they were payments on account. The relevant invoice (to which we refer below) had been partly paid. She had treated the payments that had been made by C&D as discharging the non-VAT element of the invoice on the assumption that the VAT element would be paid when C&D recovered the related input tax from HMRC.

19. The spreadsheet also showed various other receipts in an aggregate amount of £35,100. The receipts from other customers are shown as bearing VAT at 20%. The total amount of output of VAT shown on the schedule is therefore £5,850.

20. On 7 November 2014, Ms Taylor submitted the VAT return electronically. The VAT return was in accordance with Ms Edgar's figures and accordingly recorded output VAT of £5,850 for the 09/14 period.

21. Some of the output VAT shown on the return was not accounted for on time. This has been resolved and is not relevant to this appeal.

22. On 4 December 2014, Mr Uren opened an enquiry into the repayment claim made by C&D for the 09/14 period. The repayment claim was in the amount of £49,470. Mr Uren contacted Ms Edgar who explained the decision to wind-up C&D. Mr Uren asked for a copy of the VAT account for C&D for the 09/14 period.

23. On 7 December 2014, Ms Edgar sent an email to Mr Uren attaching a copy of the VAT account for C&D. In that email, she recited the facts surrounding the winding-up of C&D and the creation of the two new companies. She then stated:

> "VAT account attached for C&D Consultants Southern attached - 2014 - 2015. C&D currently owes APM VAT, which C&D cannot pay until the reclaimed VAT from HMRC is available."

24. In the remainder of the email, Ms Edgar asked Mr Uren to contact her or C&D's accountants if there were any problems.

25. When questioned about this email, Ms Edgar noted that the mail chain to this point was entirely about the VAT position of C&D. C&D was not in a position to discharge all of its liabilities in full until it received the repayment of input tax from HMRC.

26. On 11 December 2014 Ms Edgar sent to Mr Uren by email copies of the relevant invoices which relate to the VAT repayment claim by C&D. There were only two invoices: one from APM dated 31 July 2014 in the amount of £236,362 plus VAT of £47,272.40 and one from CDB Surveying Limited in the amount of £12,638 plus VAT of £2,527.60.

27. The copy invoice from APM bears invoice number 005 and is annotated "PAID – not VAT". Ms Edgar said that the annotation was simply a note to herself. C&D did not have the cash to settle the invoice in full until it received the input tax repayment from HMRC.

28. On 17 December 2014, Mr Uren sent an email to Ms Edgar. In that email Mr Uren expressed some concern as to why the VAT charged on invoice 005 dated 31 July 2014 did not appear on the 09/14 VAT return for APM even thought the related input tax was reclaimed in the corresponding return for C&D. He suggested that the best way forward would be to arrange an appointment so that he could review all of the relevant records. He said he would not be available until 8 January 2015 and so a meeting would have to take place after that date.

29. On the same date, Ms Edgar replied to Mr Uren. In her email she states:

> "I quite agree with your comments on the VAT return for Auxilium for the last quarter which I have already raised separately with my accountants (Vernon Associates), who carried out the VAT calculations on behalf of Auxilium, to rectify the submission due for end December."

30. She said that she would ask Vernon Associates to comment on the non-inclusion of the output tax in the 09/14 return and agreed to a meeting in early January.

31. Mr Uren responded to her email also on 17 December 2014. In his email, he says:

> "Also with regard to the £47,272.40 not being declared - by all means please investigate this matter but please do not take an (sic) corrective action at this stage as I will need to discuss with you at our meeting and I will take the necessary action to remedy this error, if indeed that is the case."

32. Ms Edgar says that it was at this point that she began to understand the inconsistencies in the treatment of the two sides of the transaction and appreciated that a mistake may have been made.

33. There followed a series of emails between Mr Uren and Ms Edgar arranging a time for a meeting and the availability of information and records.

34. On 22 December 2014, Ms Edgar wrote to Mr Uren. In that email, she states that she had been advised by Vernon Associates that the accounts are not incorrect because they had been prepared on the cash basis "so that when Auxilium actually receives the VAT from C&D Consultants, it will be declared and paid it over to HMRC".

35. The inspection meeting was held on 20 January 2015 at the offices of Vernon Associates. The meeting was attended by Clive Vernon of Vernon Associates, Ms Edgar and Mr Uren. Mr Uren was provided with all the information that he requested relating to the return for the 09/14 period including access to bank account details. He also spoke to staff of Vernon Associates who had been involved with the preparation of the return.

36. Mr Uren's report of the meeting includes the following paragraphs.

> "The Director Gillian Edgar was asked as to why this income had not been regarded as VATable and included on the VAT return. She stated that these had been regarded as part payments and VAT not accounted for. She reiterated what had previously been said in an earlier email that it was a "cash flow issue – as APM needed the repayment due from C&D before they could pay their liability.""

And later in his report:

> "At the end of my inspection Gillian Edgar apologised profusely and stated that it was a cash flow issue again but that it was not too to gain a VAT advantage (despite the fact that that was the result) and that they had the money to pay the VAT and that as soon as they knew the total amount of VAT and penalty it would be immediately paid."

37. Following the meeting, Mr Uren spoke to his manager. They agreed that a penalty should be charged to APM on the basis that the error was "deliberate but not concealed". Mr Uren informed Mr Vernon of this decision by email dated 23 January 2015. The email stated that the penalty would be in amount of 35% of the tax due being a penalty of £16,545.00. This was on the basis that the maximum penalty of 70% was reduced by mitigation.

38. In his email of 23 January 2015, Mr Uren set out the behaviour on which the decision regarding the level of the penalty was based. He states as follows:

> "Behaviour was established through my discussion with Gillian Edgar, as follows:
>
> - Gillian explained that it was a cash flow issue and that she needed the repayment from C&D in order to pay the liability on APM.
>
> - A conscious decision was made to claim the total VAT on invoice 00531/07/14 of £47,272.40 – even though she knew and had endorsed the invoice Paid Not VAT through C&D. Furthermore, as cash accounting was being used the then maximum VAT claimed should have been £39,393.66 (VAT applicable to payments made to APM of £236,362.00)
>
> - Lack of consistency on both entities resulted in a financial advantage potentially gained by C&D to the detriment of HMRC.
>
> - A prudent action to resolve the liability and repayment position of the two companies would be to contact HMRC or discuss the situation with financial advisor – resulting in an accounting off-set being able to be actioned upon authorising letter/communication received from Director.
>
> - The following paragraph was contained in the email sent by Gillian dated 11/12/15 "VAT account attached for C&D Consultants Southern attached – 2014-2015. C&D currently owes APM VAT which C&D cannot pay until the reclaimed VAT from HMRC is available"."

39. There followed an exchange of correspondence between Mr Vernon and Mr Uren in which Mr Vernon protested against the level of the penalty that had been raised on APM. He argued that the error was principally due to mistakes made my staff at Vernon Associates, who may not have been adequately supervised, but that any errors made by Ms Edgar and Vernon Associates were "at worst, careless".

40. On 12 February 2015, HMRC wrote to APM setting out an explanation of the penalty that it intended to charge. The amount of the penalty as set out in that letter was £7,878.60 being 20% of the "potential lost revenue" of £39,393.00 on the basis that the error was "deliberate but not concealed" and allowing the maximum amount for mitigation.

41. On 17 February 2015, HMRC issued an assessment for the VAT due but not previously accounted for and interest from the due date. The assessment was in the amount of £39,674.08. This was on the basis that the part-payments of invoice 005 received by APM from C&D in the 09/14 period should have been treated as VAT inclusive and apportioned in accordance with VAT Notice 731 (cash accounting).

42. On 17 March 2015, HMRC issued a notice of penalty assessment to APM. The penalty assessed was £7,878.60.

43. By letter dated 1 April 2015, Vernon Associates requested a review of the decision to issue the penalty. In a letter dated 29 June 2015, from Miss Sarah Davis of HMRC to APM, HMRC confirmed the original decision to levy the penalty.

44. By a notice of appeal dated 21 July 2015, APM appealed to the Tribunal.

Issues for the Tribunal

45. APM does not dispute that the VAT return for the 09/14 period contained an inaccuracy. APM does not dispute that the "potential lost revenue" arising from the inaccuracy was £39,393.

46. The only issue before the Tribunal is whether or not the inaccuracy was "deliberate but not concealed" within the meaning in paragraph 3(1)(b) of Schedule 24 Finance Act 2007.

The law

47. The penalty regime with which this appeal is concerned appears in Schedule 24 Finance Act 2007. The relevant provisions are set out below. Paragraph 1 provides:

> "(1) A penalty is payable by a person (P) where -
>
> (a) P gives HMRC a document of a kind listed in the Table below, and
>
> (b) Conditions 1 and 2 are satisfied.
>
> (2) Condition 1 is that the document contains an inaccuracy which amounts to, or leads to –
>
> (a) an understatement of a liability to tax,
>
> (b) a false or inflated statement of a loss, or
>
> (c) a false or inflated claim to repayment of tax.
>
> (3) Condition 2 is that the inaccuracy was careless (within the meaning of paragraph 3) or deliberate on P's part."

48. The list of documents to which these provisions apply includes a VAT return.

49. Paragraph 3 provides in so far as relevant:

> "(1) For the purposes of a penalty under paragraph 1, inaccuracy in a document given by P to HMRC is –
>
> (a) "careless" if the inaccuracy is due to failure by P to take reasonable care,
>
> (b) "deliberate but not concealed" if the inaccuracy is deliberate on P's part but P does not make arrangements to conceal it.."

50. Paragraph 18 deals with the liability of a taxpayer to penalties under the Schedule where agents are acting on behalf of the taxpayer. It provides as follows in so far as relevant:

"(1) P is liable under paragraph 1(1)(a) where a document which contains a careless inaccuracy (within the meaning of paragraph 3) is given to HMRC on P's behalf.

(3) Despite sub-paragraphs (1) and (2), P is not liable to a penalty under paragraph 1 or 2 in respect of anything done or omitted by P's agent where P satisfies HMRC that P took reasonable care to avoid inaccuracy (in relation to paragraph 1) ..."

HMRC's arguments

51. Mrs Pavely for HMRC makes the following points.

52. She says that Ms Edgar's actions were deliberate within the meaning of Schedule 24. She was not dishonest but her behaviour was "deliberate" in that there was conscious thought behind her actions.

53. Ms Edgar was responsible for the VAT returns of both C&D and APM. She knew when the return was made for the 09/14 period that input tax was being reclaimed by C&D, but was not being accounted for by APM in the return for the 09/14 period. She made a conscious decision not to declare the output tax.

54. Mrs Pavely points to the various references in the correspondence and communications between Ms Edgar and Mr Uren which refer to the "cash flow issue" experienced by C&D. She says that Ms Edgar knew that a taxable supply was being made and that the only reason that she did not declare the output tax was the cash flow issue.

55. A responsible taxpayer would have contacted HMRC before the return was made and sought to resolve the issue.

The Appellant's arguments

56. Mr Vernon makes the following points on behalf of APM.

57. The only question before the Tribunal was whether the actions of APM were "deliberate". The burden of proof was on HMRC.

58. The actions of Ms Edgar and Vernon Associates on behalf of Ms Edgar were not deliberate. A mistake had been made. At worst, the error was careless.

59. APM and Vernon Associates had acknowledged the error and had made no attempt to conceal it. HMRC had been provided with full access to all information and to staff at Vernon Associates.

60. The error was made by an agent for APM, Vernon Associates. This was an agent error within paragraph 18 of Schedule 24. APM was not able to review the return because of the timing of events leading up to its submission, which again was a result of an error by Vernon Associates. If the inaccuracy was careless, APM should not be liable for a penalty as APM had taken reasonable care to avoid the inaccuracy.

Discussion

61. The only issue before the Tribunal is whether the inaccuracy in the return was "deliberate".

62. Schedule 24 Finance Act 2007 does not further define the word "deliberate". HMRC's manuals state that "a deliberate inaccuracy occurs when a person gives HMRC a document that they know contains an inaccuracy" (HMRC Compliance Handbook CH81150). We adopt a similar approach.

63. In our view, a deliberate inaccuracy occurs when a taxpayer knowingly provides HMRC with a document that contains an error with the intention that HMRC should rely upon it as an accurate document. This is a subjective test. The question is not whether a reasonable taxpayer might have made the same error or even whether this taxpayer failed to take all reasonable steps to ensure that the return was accurate. It is a question of the knowledge and intention of the particular taxpayer at the time.

64. The test of deliberate inaccuracy should be contrasted with that of careless inaccuracy. A careless inaccuracy occurs due to the failure by the taxpayer to take reasonable care (see paragraph 3(1)(a) of Schedule 24 Finance Act 2007 and *Harding v HMRC* [2013] UKUT 575 (TCC) at [37]).

65. As we have mentioned above, we found Ms Edgar to be an honest and credible witness. We accept her evidence. When she provided the information for the 09/14 return, she believed that she was providing accurate information. In particular, at that time, she thought that the correct approach in relation to the part payments of amounts under invoice 005 was to attribute those payments first to the non-VAT elements and then to treat the VAT element as paid as and when C&D recovered the input VAT from HMRC and was able to make the final payment to APM. APM would then be in a position to account for the VAT to HMRC.

66. We accept Ms Edgar's evidence that that was her belief. We are supported in that conclusion by the other correspondence and communications to which we have been referred and which is consistent with Ms Edgar's explanation. In particular, the cash flow issue to which she referred at several points in her communications with Mr Uren was quite clearly a reference to the cash flow issue for C&D and not a reference to a cash flow issue for APM.

67. In our view, therefore, the inaccuracy in the return was not a deliberate inaccuracy. Ms Edgar did not knowingly and intentionally provide an inaccurate document to HMRC. She made a mistake and Vernon Associates made a mistake. But we all make mistakes despite our best efforts.

68. We should, at this point, comment on Mr Uren's evidence. We do not wish to imply, in any way, that we do not regard Mr Uren as a reliable witness. We accept his record of the events. We do not, however, accept some of the inferences that he and others at HMRC drew from them. We understand that, in the course of his job, Mr Uren will come across many occasions in which individuals or companies seek to gain an advantage from a lack of full disclosure to HMRC. For that reason, he has to

employ a healthy scepticism in assessing their explanations. However, in our view, this was the case of an innocent mistake by the taxpayer which was compounded by an error on behalf of the agent who was acting on the taxpayer's behalf.

69. We then need to consider whether the inaccuracy was "careless". Mr Vernon accepted that the error was due to a lack of reasonable care and so "careless" within the meaning of paragraph 3(1)(a) Schedule 24 Finance Act 2007. He argued that APM had taken reasonable care in appointing Vernon Associates to undertake its VAT compliance and that the error was due to the failure of staff at Vernon Associates to take reasonable care in the making of the return. On that basis, Mr Vernon argued that paragraph 18(2) Schedule 24 Finance Act 2007 should apply and APM should not be liable to a penalty.

70. We acknowledge that there are circumstances in which a taxpayer may be regarded as having exercised reasonable care by relying on the advice of a competent professional adviser (see, for example, *J R Hanson v HMRC* [2012] UKFTT 314 (TC)). On the evidence before us, we do not accept that Ms Edgar could be completely excluded from responsibility for the error. For that reason, we take the view that paragraph 18(2) will not apply.

71. We note, however, that in assessing the penalty HMRC have treated the disclosure as "unprompted" (within the meaning of paragraph 9(2)(a) Schedule 24 Finance Act 2007) and allowed full mitigation to APM for its cooperation and assistance to HMRC following the discovery of the inaccuracy. We propose to adopt the same approach. This will reduce the penalty to nil.

Decision

72. We allow this appeal.

73. We reduce the penalty to nil.

Rights of appeal

74. 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: 13 APRIL 2016