[2017] UKFTT 202 (TC)

TC05690

Appeal number: TC/2015/06195

VAT – Assessment – Best Judgment – Penalty – Carelessness - Second Hand Vehicles – Margin Scheme – Appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

KEITH ALLEN **Appellant**

- and -

COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: JUDGE RUPERT JONES
JULIAN STAFFORD

Sitting in public at Cambridge County Court on 13 October 2016

Mr Keith Allen, the Appellant, appearing in person

Esther Hickey, Presenting Officer for the Respondents

DECISION

1. The appellant appeals against a VAT assessment made by HMRC on 5 March 2015 in the sum of £26,503 for the periods 03/11 to 03/14 inclusive. The appellant also appeals against an assessment to a penalty made against him, as reduced on 7 September 2015, in the sum of £4,571 in respect of the same VAT periods.

Background facts

2. The Tribunal received a bundle of documents from HMRC, together with witness statements from HMRC officers, Mrs Janine Gill and Mr Dean Witziers. The tribunal heard oral evidence from Mrs Gill, Mr Witziers and the appellant, each of whom was cross examined.

3. The tribunal finds the following facts.

4. The appellant voluntarily registered for VAT with an effective date of registration of 01 July 2009. The VAT number of 974794455 was allocated to the sole proprietorship of 'Keith Allen trading as Wednesday cars'.

5. The main business activity was described on the VAT registration document as the 'sales of used cars and light motor vehicles' and the annual turnover was described as an expected £200,000 per annum.

6. The appellant operated the second-hand margin scheme for the purpose of accounting for VAT. Under the margin scheme, where a taxpayer purchases vehicles on which no VAT is charged they only have to account for VAT on the profit margin rather than the full selling price. So if they buy a car for £1,000 and sell it for £1,200, they account for VAT on £200. If they sell the vehicle at cost price or at a loss, no tax is due. However, no refund of tax can be due in respect of cars sold under the margin scheme because there is never any input tax to recover.

7. If a taxpayer is charged VAT on the purchase of a vehicle they cannot use the margin scheme. In these circumstances, they can claim VAT back on the purchase but must also account for VAT on the full selling price. So, if a taxpayer buys a car for £2,000 plus VAT (£400) and sells it for £3,000 plus VAT (£600) they should claim £400 input tax and £600 of output tax. If they sell the car at a loss, input tax would exceed output tax so they would be due a refund.

8. Over the period 01 July 2009 to 6 November 2014 the appellant's business had declared a net trading loss of £139,902 and had claimed VAT refunds from HMRC to a net value of £27,508 based on the following:

Total output tax declared: £8,989.30

Total input tax declared: £36,497.96

Total net tax reclaimed: £27,508.66

Total net sales declared: £166,448

Total net purchases declared: £306,350

Total net loss: £139,902

9. For the period 1 January 2011 to 31 March 2014 (covering VAT periods ending 03/11 to 03/14 inclusive), the period for which he was latterly assessed, the appellant's VAT returns declared a net loss of £95,865.

10. In each of the appellant's quarterly VAT returns since he registered for VAT he claimed refunds of tax, often substantial amounts. This would indicate that he was incurring VAT on the purchase some of the vehicles and not operating the margin scheme upon these. However, if this was the case, HMRC expected to see more sales (outputs) and output tax than the appellant declared.

11. On 5 November 2014 HMRC officers Gill and Witziers undertook a VAT assurance visit to the appellant. During that visit the appellant advised the officers that initially his business activity was the buying and selling of cars. He stated that approximately eighteen months to one year previously he had sold his last car and changed his business activities and thereafter bought and sold lawnmowers instead; he purchased them from various sources and auctions and which he sold on, usually for cash.

12. Also on 5 November 2014, the day of the visit HMRC received a VAT 7 registration request form electronically from the appellant. The reason for deregistration given was declared to be that the business was trading 'below the current deregistration threshold'.

13. During the visit the officers were advised by the appellant that he traded from a portacabin and containers at the rear of a rented premises. The appellant showed them some damage that had been caused by fire the property on 15 April 2014. The damage witnessed consisted of some Leylandii trees of which a small part appeared to have died back. These trees were situated behind the portacabin.

14. During the visit the appellant advised the officers that all his business records stored in the container were destroyed in the fire and that there were no backed up records on computer. The appellant stated that between £12,000 and £13,000 of stock had been destroyed and approximately £600 worth of damage had been caused to each container. In total the appellant stated that he had lost £15,000 as a result of the fire. He also stated that the stock which survived the fire was subsequently sold for £80.

15. Officer Gill explained to the appellant that the VAT returns he had submitted for the last four years showed a substantial loss of around £90,000 and she wanted to know how he had managed to fund such a loss. The appellant did not give an explanation other than it was through savings and cash sales. The officer asked if the appellant could evidence the funding. The appellant could not evidence his claim.

16. On 11 November 2014, the Norfolk fire service confirmed that they had attended a fire at the address on 15 April 2014. This was supplemented by an incident report provided by the appellant's representatives on 25 February 2015.

17. Following the visit, unable to verify that the VAT return declarations, officer Gill issued an information notice to the appellant on 12 December 2014 to produce: copies of bank statements for the period 1 July 2010 to 30 September 2014; a list of suppliers and customers since July 2010; an explanation of why some sales were declared on the VAT returns without any output tax being declared for those same sales.

18. HMRC received a letter from the appellant dated 5 January 2015. In this letter the appellant confirmed that the 'sales declared without VAT' were for sales, except for one quarterly period, 09/13, where of the £18,000 sales without VAT, part was made up of the sale of an engagement ring. The appellant also advised he was in the process of obtaining the bank statements. In later correspondence, the appellant confirmed that the sale of the engagement ring was for £15,000.

19. However, in his oral evidence before the tribunal the appellant stated that there was in fact no sale of an engagement ring and but that the sum of £18,000 represented a sale of a Range Rover which had been purchased and paid for by his former wife.

20. On 13 January 2015 HMRC received a letter from the appellant with enclosed bank statements. This letter also listed some suppliers and customers and commented that some sales would not show up in the bank statements as they were cash sales.

21. On 4 February 2015 Officer Gill sent a pre-assessment letter to the appellant outlining the record-keeping requirements under the VAT Act 1994 and informing the appellant that it was HMRC's expectation that as the registered taxable person, it was his responsibility to make an effort to reconstruct his records.

22. In this letter the officer expressed her concerns about how the appellant had funded the loss identified in his VAT returns and that in the absence of any evidence of funds, the submitted VAT returns did not appear to be credible. The letter informed the appellant that comparison of his bank statements to his VAT returns indicated that not all of his business income went through his bank accounts and that it pointed to the appellant using a substantial amount of cash while conducting his business affairs. The letter pointed out that VAT would equally be due on cash sales.

23. On 27 February 2015 HMRC received a letter from Mapus-Smith and Lemmon LLP, accountants and representatives, on behalf of the appellant. The letter advised that the appellant was using the 'second hand margin scheme' where VAT is declared on the marginal profit and not on full selling price and therefore the VAT declared on sales would not equal 20% of the net value declared in the same period. The agent stated that the reason for the negative mark-up was 'lower than expected sales' and that the stock was then destroyed in a fire. The appellant's agent also provided an income and expenditure report for the year ending 31 March 2013, compiled by the appellant's previous accountant, together with some stock books.

24. Officer Gill could not match any of the figures contained in the documents to the VAT declarations made by the appellant. The stock books showed a large value stock purchase from a company called Greyhound Sanctuary (UK) Ltd of which the appellant was a director. No evidence was supplied by the appellant regarding how any of these purchases were funded.

25. HMRC did not accept the claim of accidental inclusion of an engagement ring for the sum of £15,000 in the absence of bank deposits to this value and in the absence of any documentation. HMRC noted that cash transactions in excess of £10,400 require proper documentation as per money laundering provisions.

26. The officers who viewed the trading site did not accept the claim that a consistently negative mark-up from VAT registration in 2009 through to a fire in April 2014 was a credible explanation for the appellant's VAT returns.

27. HMRC calculated that the stock bought by the appellant had been £292,851 net over this period and stock sold over the same period had been £163,583 net, including the ring. If this was right, the destroyed stock which the appellant had on hand at the time of the fire would have been £129,268 worth of second-hand lawnmowers. This was not considered to be credible based on HMRC's visual inspection of the fire site.

28. On 4 March 2015 Officer Gill considered the income and expenditure report on the net loss position of the business and issued a notice of assessment tax on 5 March 2015 assessing the appellant to VAT for the total sum of £26,503 covering the VAT periods 03/11 to 03/14. These are the assessments which are the subject of the appeal.

29. On 18 June 2015 HMRC issued a notice of penalty assessment to the appellant under schedule 24 of the Finance Act 2007 for careless behaviour. The total penalty was calculated at 28.5% of the net tax due to HMRC in the sum of £7,553.60 for the same VAT periods, namely 03/11 to 03/14.

30. On 14 July 2015 the appellant requested a review and the review letter was issued on 7 September 2015. The review officer upheld the decision to issue the VAT assessment and the quantum of the assessment calculation. The review officer also upheld the decision to issue the penalty but reduced the penalty percentage to 17.25% of the assessed tax leading to reduction in the value of the penalty charged in the sum of £4,571.

31. The appellant lodged his appeal with the tribunal service on 6 October 2015 and provided additional information to the tribunal on 30th of October 2015 in the form of notice and grounds of appeal.

Summary of the Appellant's evidence and grounds of appeal

32. The appellant gave oral evidence to the tribunal at the hearing in line with his earlier correspondence and grounds of appeal, except to the extent noted above and below.

33. The appellant's letter to the tribunal dated 5 October 2015 made the following points:

34. The HMRC officers that visited the appellant's premises were shown sales and purchase invoices from a date after the fire and the fire was mid-VAT-period and the next three-month period was complete in terms of records. All of the invoices were checked by the two officers and the refund was paid into his bank.

35. Paperwork relating to the illness suffered by the appellant was relevant to the appeal and was accepted by an HMRC officer relation to an income tax self-assessment penalty for late self-assessment.

36. The sole reason for the VAT registration was that some of the vehicles which passed through the business were light commercial vehicles subject to VAT on the selling price as opposed to being subject to VAT on the marginal profit only.

37. In the appellant's grounds of appeal within his notice of appeal dated 27 October 2015 he made the following further points:

38. All of the appellant's stock and business records were destroyed by a fire at his premises in April 2014. The appellant was able to show HMRC sales and purchases invoices after this date which were for approximately one and a half VAT periods. The half period fell at the time of the fire. The full period was checked by HMRC and the refund was paid into his bank account.

39. He came to register for VAT by selling second-hand motor vehicles which was the residue of the business that had ceased trading. After a short period it had become clear to him that he needed to be registered for VAT as part exchange vehicles were light commercial vehicles, which VAT was added to. Some of the vehicles were three to five tonnes vans and subject to VAT. He sold these on plus VAT and this does not seem to have been noted by HMRC.

40. The appellant sold the vehicles to a Mr Andrew Lee of Wisbech. Many of the vehicles had originated in Northern Ireland and needed to be registered in the UK which Mr Lee did. Mr Lee would pay the appellant when this had been completed and a vehicle had been sold. It was not until Mr Lee sold a vehicle that the appellant would invoice him for it and so on paper it looked like the appellant had lost money when in fact the sale showed a small profit. Mr Lee ceased trading and owed the appellant the money for five vans which the appellant never received. Mr Lee was now deceased.

41. The appellant began trading with a part exchange ride-on tractor and he then acquired some lawnmowers and was led by requests. He sold a lot of items, both lawnmowers and cars for cash. This is what the customers wanted to pay and this could be seen in the purchase invoices. The appellant stated that this is where he went very wrong as with many of the sales he had to take in part exchanges in and made very little money and many times lost money.

42. The appellant did not know how HMRC had calculated their figures but he estimated that £100,000 seemed to be the amount he had lost over the period.

43. The appellant in correspondence stated that he did not start his business with any money, he started it with cars which were not his property. About £40,000 of cars were in the yard that he had taken on to sell and he did pay back £34,000 of the £40,000.

44. In his oral evidence to the tribunal the appellant stated that the cars, the initial stock of £40,000, and the business had in fact come from his former wife. She had ceased trading and the appellant was transferred the vehicles for his business. In this evidence he appeared to suggest that he did not in fact pay any sum back to his former wife and therefore she had borne the loss of around £40,000. This would therefore explain some of the loss suffered.

45. When Mr Lee went bust he did not pay for vehicles he had received. This resulted in a further loss to the appellant of £25,000. In his oral evidence to the tribunal the appellant stated this would explain a further a further amount of the loss suffered.

46. The appellant, in his grounds of appeal and oral evidence to the tribunal, stated the fire at the premises in April 2014 was set off by a security sensor light at the business and this destroyed about £30,000 of stock.

47. However, this explanation is in contrast to what he told officers at the visit on 5 November 2014 where he estimated that the value of the stock destroyed was between £12,000-£13,000, and at most a total of £15,000. In the sales invoices viewed by HMRC the appellant showed them a receipt for £70 plus VAT being the sale of what was sold after the fire.

48. The appellant in correspondence and oral evidence stated that all of the figures for his returns in the period of the VAT registration were prepared by accountants. The appellant would take all sales/purchase invoices to the accountants at the end of the period, the accountants prepared figures and in due course they would tell him what the income was. The appellant changed accountant but continued to use this same procedure. He was shown how to fill in a VAT return which he did once but he would simply sign off the returns.

49. The appellant stated he sold vehicles for cash and equally used cash to buy vehicles. The reason to use cash was to avoid receiving bank charges to deposit the money and also charges if he withdrew cash from the bank. He believed that his endeavour to try and save these costs by using cash had resulted in HMRC's investigation.

50. In the time he was registered for VAT the appellant stated he had never added or taken away anything which resulted in him being held to account for wrongdoing. The only invoices which were not raised were for the sum of the vans which Mr Lee had bought from him.

The law

51. Section 50A of the Value Added Tax Act 1994 ("VATA"), in so far as applicable to this appeal, provides that where a person makes supplies of motor vehicles the taxable person is entitled to opt that where he makes supplies of that description, VAT is to be charged by reference to the profit margin on the supplies, instead of by reference to their value.

52. Section 73(1) of VATA empowers the Commissioners to the best of their judgment to assess the amount of VAT due from a person who has failed to make any returns required under VATA or where such returns are incomplete or incorrect.

53. At paragraph 14 of his decision in *Queenspice Limited v Commissioners for HMRC* [2010] UKUT 111 (TCC), Lord Pentland stated:

'… the Respondents' task under section 73(1) of the 1994 Act is not, as he contended, of a strictly mathematical or statistical nature at all; no doubt, any calculations forming part of the assessment have to be arithmetically accurate, but the power given to the Respondents under statute is to make an estimate or an assessment to the best of their judgment on such

information as is available to them. This necessarily allows the Respondents a substantial margin of error. They are entitled to make what one might describe as an educated guess. They are not required to carry out exhaustive investigations.'

54. The time limits for assessments to be made under section 73 of VATA are provided under section 77 of VATA.

55. Section 77(1) provides that an assessment shall not be made more than 4 years after the end of the prescribed accounting period.

56. Section 83(1) of VATA provides that, subject to sections 83G and 84, an appeal shall lie to the tribunal with respect to certain matters. These include, pursuant to section 83(1)(p)(i), an assessment or the amount of an assessment under section 73(1) or (2) in respect of period for which the taxpayer has made a return under the Act.

57. Schedule 24 to the Finance Act 2007 ("schedule 24") provides for a liability to penalties in relation to errors in certain types of documents given to HMRC, including a VAT return. Penalties are charged under paragraph 1 of schedule 24 if: a) there is an inaccuracy which amounts to or leads to an understatement of a liability to tax, a false or inflated statement of a loss or a false or inflated claim to repayment of tax; and b) the inaccuracy was careless.

58. Careless in this context is defined by paragraph 3(1)(a) of schedule 24. This provides that an inaccuracy in a document is careless if the inaccuracy is due to a failure by a person to take reasonable care.

59. Paragraph 4 of schedule 24 sets out the standard amount of penalty for the behaviours that are the subject of the regime. Under paragraph 4(2)(a) a penalty for careless action is set as a standard amount as 30% of the potential lost revenue

60. Paragraph 9(2) of schedule 24 provides that a disclosure is unprompted if made at the time when the person making it has no reason to believe that HMRC have discovered or are about to discover the inaccuracy and otherwise it is prompted. This test is an objective one.

61. Paragraph 10 of schedule 24 provides that where a person who would otherwise be liable to a 30% penalty has made a prompted disclosure, HMRC must reduce the standard 30% to a minimum percentage not below 15% of the potential lost revenue which reflects the quality of the disclosure.

62. The burden of proof is upon the appellant to demonstrate the assessed tax was calculated in the absence of best judgement.

63. The burden of proof is upon HMRC to demonstrate that the penalty was properly and correctly charged.

Discussion and decision

64. The appellant's VAT registration began on 1 July 2009 and the appellant deregistered for VAT on 6 November 2014, the day following HMRC's visit.

65. Over this period the appellant's business had declared a net trading loss of £139,902 and had claimed VAT refunds to a net value of £27,508. HMRC made

assessments in March 2015 in relation to the period 1 January 2011 through to 31 March 2014 (covering quarterly VAT periods ending 03/11 to 03/14 inclusive). HMRC noted that according to his VAT returns, the appellant made a net loss of £95,865 over the periods of assessment.

66. For the reasons set out below, the Tribunal is satisfied HMRC was entitled to assess the appellant beginning with the earliest period of 03/11, being four years prior to the date of the assessment.

67. In each of the appellant's VAT returns since he registered for VAT he claimed refunds of tax, often substantial amounts. This would indicate that he was incurring VAT on the purchase of some of the vehicles. However, if this was the case one would expect to see more outputs and output tax than had been declared.

68. There are a number of possible explanations for this apparent discrepancy:

a) the appellant was erroneously claiming input tax on purchases where no tax was incurred;

b) the appellant correctly claimed input tax on vehicle purchases but then erroneously declared VAT on the profit margin on the full sale price;

c) the appellant correctly claimed input tax on vehicle purchases but made off-the record-sales and did not declare any of the output VAT due on them; or

d) the appellant consistently made substantial losses on cars bought and sold outside the margin scheme ever since he registered VAT.

69. The appellant contended that the reason for the excess of input tax over output tax was that the business had not been profitable with lower than expected sales. However, when the appellant was asked how he funded these losses and how he was able to keep buying vehicles for resale he was unable to provide satisfactory evidence to HMRC or details of finance or any loans etc.

70. HMRC were not provided with any of the following by the appellant:

- any insurance paperwork;
- any records of documentation to verify that a fire large enough to consume stock work at least £12,000 actually occurred;
- any sales or purchase invoices pre-April 2014;
- stock books or stock records for the years ending March 2012 or March 2014;
- any reasonable explanation as to the substantial net losses declared on the VAT return declarations;
- any evidence to support the inclusion of the value of the sale of an engagement ring to the value of £15,000 into the net sales in the period 09/13.

71. HMRC were provided by the appellant with: a) limited information in the form of income and expenditure account for the appellant for the year ending 31 March

2013 (01/04/12 to 31/03/13) prepared by a previous agent; b) bank statements for two bank accounts for the periods 03/11 to 03/14; and c) limited paperwork relating to the period from April 2014 onwards.

72. If the appellant's business bank account opened with an opening balance of £139,000 in 2009 and ended with a nil balance in 2014 or if a negative bank balance of £139,000 was evident on 5 November 2014 then this large net loss may be explainable. However the bank statements provided to HMRC by the appellant showed neither.

73. The tribunal accepts HMRC's submission that no sensible or realistic explanation has been given by the appellant that could explain the substantial net loss and that the VAT assessments made by HMRC provided reasonable adjustment to bring the trading figures back to a realistic level.

74. Although the appellant's evidence to the tribunal was not entirely clear and was sometimes difficult to follow, the explanation that the appellant appeared to give in oral evidence to the tribunal to explain the losses can be summarised as follows: that £40,000 of stock was acquired from his former wife with the business which he has not repaid, that he was owed £25,000 by Mr Lee for four vehicles and that £30,000 of stock had been destroyed in the fire.

75. The tribunal does not accept the appellant's explanation for the losses given in his oral evidence.

76. First, there is no written or independent evidence to support this explanation whatsoever.

77. Second, this is not an explanation that the appellant has at any time had previously given to HMRC throughout correspondence or during the officers' visit. The inconsistencies between his oral evidence to the tribunal and his previous correspondence, grounds of appeal and statements to Officers at the visit are noted above.

78. The appellant had originally claimed that he used a £40,000 loan to start up the business but that he repaid £34,000 of the loan; therefore this could at most explain £6,000 of the £139,902 deficit. It is inconsistent with his evidence that in fact the business came from his wife and she had transferred him £40,000 of vehicles for which he had not repaid her.

79. The appellant had contended that he had suffered losses when his customer Mr Lee, failed to pay for the supply of vehicles. We are satisfied that it was reasonable for HMRC to dismiss this argument on the basis it could not accept the bad sales that suffered the appellant at one single point in time and only to the extent of £25,000 could explain a trading business pattern over the course of five years of losses as set out in his returns.

80. The appellant claimed in his grounds of appeal and oral evidence to the tribunal that the fire at his business premises on 15 April 2014 had destroyed approximately £30,000 worth of stock and all the business books that had existed up until that point. During the VAT inspection on 5 November 2014 the appellant stated to officers that

the value of stock consumed was in fact between £12,000 and £13,000 and total losses were £15,000. This inconsistency suggests the appellant's evidence was unreliable.

81. The HMRC officers' witness statements and visit reports recorded that the damage they witnessed at the appellant's premises consisted merely of some Leylandii trees which had died back which were situated behind the portacabin which the appellant was currently using as an office. They also recorded that the appellant stated that the damage to the two containers was only to the extent of £600.

82. HMRC calculated the stock which might have been lost in the fire if the appellant's VAT returns were accurate. This they did by reference to the stock bought based on the appellant's VAT returns for the periods 09/09 to 03/14 totalling net purchases or inputs of £292,851 and total outputs or sales of £163,583 (ie. stock sold). The officers who visited the site were sceptical that a fire had occurred which was large enough to consume stock worth at least £12,000 let alone £129,268. Furthermore, there was no insurance claim by the appellant in relation to the same.

83. The tribunal is satisfied that HMRC were right to consider that such a large loss of stock would not be credible. It was not consistent with the appellant's explanations that he was only trading in lawnmowers and had sustained much lower losses (as above, he supplied two inconsistent figures for this), he had no insurance, and that the mowers were destroyed with the records. The tribunal is not satisfied that the fire could be a credible explanation any substantial part of his trading losses.

84. HMRC noted that the appellant by his own admission in his grounds of appeal stated that many of his customers paid in cash and many purchases were paid for out of the same cash with the cash never being banked in between.

85. HMRC submitted that the VAT assessment they raised was lenient in that it understated the true liability to tax; no additional cash sales have been included and instead the VAT assessment only sought to assess the appellant on the values deposited except where the values declared exceeded this deposited value.

86. HMRC submitted that they made VAT assessments to their best judgement and that any deposit into the bank accounts of the appellant that were identified as non-business were excluded.

87. The tribunal accepts HMRC's submissions and is therefore satisfied that the appellant's VAT returns do not reflect true state of affairs for his business. Either input tax, output tax or a combination of both have not been correctly declared by the appellant.

Unreliability of the declared figures

88. Furthermore, the documents provided by the appellant's accountants would appear to bear out the unreliability of the appellant's VAT returns.

89. For example, the tribunal is satisfied that the unreliability of the VAT return figures is borne out by the profit and loss report sent by the agent for the appellant.

90. The VAT returns for the year ending 31 March 2013 show inputs of £41,181. However, the profit and loss summary for the same period shows total costs of

£7,644. These figures clearly do not corroborate each other and give rise to a £33,537 discrepancy.

91. Sample stock lists submitted by the appellant's agent, when compared to the VAT returns submitted also demonstrate the unreliable nature of the figures provided. For example, in period 12/11 the appellant appeared to purchase cars valued at £39,775 (four vehicles from the Greyhound Sanctuary). He declared inputs of £46,138. However, he only accounted for input tax on £22,850 of declared inputs. This would suggest at this time the appellant was claiming VAT on some of the same cars and not on others.

92. If some VAT had been paid on the purchase of some vehicles, and the appellant was operating a mixture of the margin scheme and the normal accounting for commercial vehicles as he claimed, one would expect to see subsequent sales on which VAT is declared on the full sale price. However, values for output VAT shown on subsequent returns do not suggest this tool was being used. Rather the returns indicate that VAT was being declared on the margin.

93. In the next quarter, 03/12, the appellant claimed input tax of £4,825.47 in respect of inputs to the value of £24,363. However, no vehicles were bought in 03/12 according to the stock records provided by the agent. This gives further reason to doubt the credibility of the figures shown on the VAT returns.

94. For the quarterly period 03/11 (01/01/11 to 31/03/11) the stock book demonstrates that the total sales were for a total of £3,950 but the appellant's VAT return for the period 03/11 show £700 of sales as outputs and purchases (ie. inputs) of £4,194. The appellant's stock bocks suggest the only purchase is a Swift Challenger for £700 on 01 January 2011 and that thereafter there was a £700 sale on 11 February 2011 ie. with no profit. This cannot be reconciled with purchases of £4,194 on his VAT returns. At the same time his bank statements demonstrated £6,357.60 was received into his account with £5,886.95 expended.

95. For the quarterly VAT period 12/11, the income deposited to the bank was £4,600 according to the appellant's bank statements. Purchases were shown as outgoings from his bank account of £948.62. The appellant's stock book shows he purchased two vehicles and two number plates to value of £39,000, yet his bank statements show only £948.62 leaving the account. On the appellant's VAT return, the figure claimed in this period for input tax was only £4,530.

96. In the following quarterly VAT period of 03/12, the appellant claimed input tax of £4,825.47 on inputs of £24,363. However, the stock book demonstrates that no vehicles were bought in the period 03/12. This again gives further reason to doubt the reliability of the figures shown on the VAT return.

97. The stock book and bank statements do not support the appellant's VAT returns. The inconsistencies in the records are significant.

98. The appellant at no time has offered any satisfactory explanation for these types of discrepancies.

99. The tribunal is satisfied that the evidence, as produced by the appellant, suggests the figures included in his VAT returns are erroneous and the appellant was not using the correct method to calculate his input tax.

Calculation of the assessment

100. Due to the implausibility of the VAT return figures and the evidence suggesting that they were incorrect, HMRC sought to establish the amount of tax due by means of analysis of the bank statements of the appellant. It supports the assessments raised to the best of HMRC's judgment. The method of calculation is essentially as follows.

101. The officer excluded all the income going into the appellant's bank accounts that did not appear to be business-related such as housing benefit and DWP payments. What was left was deemed to be business income. With regards to outgoings in the bank, the transaction of the business nature were identified and these were treated as business expenses/cost of goods for resale.

102. For the purposes of the assessments the VAT was applied to both the income and outgoings on a period by period basis, compared to the figures in the VAT returns and the differences assessed for. Where the output tax declared in the VAT period was greater than the tax calculated from the bank statements, the officer HMRC assumed that these were cash sales. There was no assessment of output tax for these periods.

103. The tribunal is satisfied that HMRC's method resulted in a reasonable calculation of net tax due on income and expenditure. This is because whatever method used to account for tax on second-hand cars, the net tax should remain same. As HMRC submitted, suppose the car is purchased for £1,000 and sold for £1,200. If VAT is incurred on the purchase, VAT will be due on the full sale price, i.e. net tax due will be VAT on £200. If VAT is not incurred on the purchase then the VAT can be accounted for on the margin, again this amounts to £200.

104. Therefore applying VAT to all purchases and sales should produce the correct net tax due by the appellant.

105. HMRC prepared an analysis of the appellant's bank statements and his VAT returns which we are satisfied was accurate and reasonable. This calculated the total VAT due to HMRC for each period of the assessment 03/11 to 03/14 based upon the income and outgoings from his bank accounts in the sum of £26,503. All income from DWP, Housing Benefit and account to account transfers had been removed.

106. The tribunal is satisfied that any reliance by the appellant on third parties, such as an accountant, did not absolve the appellant of his legal obligation to ensure the VAT was correctly accounted for. Representatives can only prepare VAT returns on the basis of the books and records given by the taxpayer. It is unknown whether the appellant provided his agent with all the relevant records nor whether the returns eventually rendered were in accordance with the figures generated by the same agents.

107. We are therefore satisfied that in March 2015 HMRC raised the disputed VAT assessments in their best judgement and they should be upheld. The assessments were calculated in HMRC's best judgement based on the information available to them.

108. The appellant has failed to demonstrate how the assessed tax was calculated in the absence of best judgement. The appellant has not satisfied that the Tribunal on the balance of probabilities that the assessments to VAT were inaccurate, unreasonable or outwith HMRC's best judgement.

Penalty

109. As set out above, Schedule 24 to the Finance Act 2007 ('schedule 24') provides for a liability to penalties in relation to errors in certain types of documents given to HMRC, including a VAT return. The penalties in the appellant's case were charged under paragraph 1 of schedule 24.

110. We are satisfied that the appellant's behaviour which led to the inaccuracies on his VAT return declarations was careless. 'Careless' in this context is defined by paragraph 3(1)(a) of schedule 24 as being due to a failure by a person to take reasonable care.

111. VAT is a self-assessed tax and taxpayers are obliged to use the appropriate notice and guidance in order to ensure that they account for VAT correctly. This is doubly the case where the taxpayer voluntarily seeks to use a specific scheme such as the margin scheme.

112. In the appellant's case the inaccuracies on his VAT returns were careless because:

a) he made no effort to reconstruct his records;

b) he had no satisfactory explanation as to the substantial trading losses;

c) he provided inconsistent explanations to account for his losses in his evidence to the Tribunal, his explanations to HMRC in correspondence and the account he provided to HMRC officers at their visit;

d) he provided no information that could enable HMRC to discern how the inaccuracies could have arisen unless he had not taken reasonable care.

113. There is no direct evidence of deliberate behaviour by the appellant leading to the inaccuracies. Be that as it may, errors were made and it has not been satisfactorily shown what the precise nature of those errors was.

114. The appellant in correspondence and in evidence suggested he acted on the advice of his accountants who at one time prepared VAT returns. However simply relying on third parties does not absolve taxpayers of the legal obligation to ensure the taxes accounted for are correct. Further, representatives can only make VAT calculations based upon the books and records given to them by the taxpayer.

115. It is unknown and unverifiable whether the appellant's representatives or accountants were provided with all the relevant records by the appellant. Equally it is unknown whether the VAT returns rendered were in accordance with the figures generated by the accountants. It may be that there is little by way of evidence because of the fire. However, there is at least one instance where virtually all input tax claimed on the VAT return seems to relate to a vehicle which was not purchased in the period.

This clearly evidences a failure to take reasonable care as the error is so large it could not reasonably have gone unnoticed and unchecked.

116. The tribunal is satisfied that the appellant did not take reasonable care in the submission of his VAT returns. The standard by which reasonable care is to be judged is that of a prudent and reasonable taxpayer in the position of the taxpayer in question as outlined at paragraph 25 of the decision in *David Collis v HMRC* [2011] UKFTT 588 (TC).

117. Paragraph 4 of schedule 24 sets out the standard amount of penalty for the behaviours that are the subject of the regime. Pursuant to paragraph 4(2)(a), the standard amount of penalty for carelessness is set at 30% of the potential lost revenue.

118. Paragraph 9(2) of schedule 24 distinguishes between disclosure that is unprompted and disclosure that is prompted. The tribunal is satisfied that the categorisation of the penalty for a prompted disclosure was appropriate because the appellant did not advise HMRC about the inaccuracies before he had reason to believe that HMRC had discovered them or was about to discover them.

119. Paragraph 10 of schedule 24 provides that where a person who would otherwise be liable to a 30% penalty has made a prompted disclosure, HMRC shall reduce the 30% to a percentage not below 15% which reflects the quality of the disclosure. Paragraph 10 therefore provides in the case of prompted disclosure, for a minimum penalty for careless inaccuracy.

120. The tribunal is satisfied that the allocation of a penalty percentage of 17.25% of the net tax, a sum of £4,571, is reasonable in the circumstances of the appellant's case. HMRC made due allowance for the cooperation the appellant provided in respect of 'helping' and 'giving' and therefore considered, rightly in our view, that the appellant should be awarded full reductions in respect of these factors (5% of the tax due for each). However, the appellant was unable to substantiate his explanation as to how he funded his apparent losses. Therefore the tribunal is satisfied that HMRC reasonably decided that the appellant should only have been awarded half of the available allowance, a maximum reduction of 5%, for 'telling'.

121. The tribunal therefore considers that the penalty calculated at 17.25% of the assessed tax, being £4,571, should be confirmed. This percentage is only slightly higher than the minimum penalty which can be applied of 15%.

122. We are satisfied there is no special or unusual circumstances relating to this case for special reductions to be applied under paragraph 11 of schedule 24. Even though the appellant has previously suffered health problems, the tribunal was not provided with any information to demonstrate how this may have affected his ability to manage his VAT affairs.

123. We are therefore satisfied that the appellant is liable for the penalty and that HMRC applied a reasonable reduction to the penalty percentage. HMRC has satisfied us on the balance of probabilities that the penalty was correctly charged and properly calculated and that the appellant's careless behaviour led to the inaccuracies in his VAT returns for the periods 03/11 to 03/14. The appellant is therefore liable for the total penalty.

Conclusion

124. The tribunal therefore dismisses the appeal both against the VAT assessment and the penalty assessment.

125. 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.

TRIBUNAL JUDGE
RUPERT JONES

RELEASE DATE: 22 FEBRUARY 2017