



TC03344

Appeal number: TC/2012/10215

Value Added Tax – Best Judgment – whether assessment reasonable – appeal partly allowed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

MEDIAID TRAINING SERVICES LIMITED Appellant

- and -

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

**TRIBUNAL: JUDGE DR K KHAN
 MS HELEN MYERSCOUGH**

Sitting in Canterbury, Kent on 18 November 2013.

Richard Palmer represented the Appellant.

**Philip Rowe, Senior Officer, instructed by the General Counsel and Solicitor to
HM Revenue and Customs, for the Respondents.**

DECISION

Introduction

- 5 1. The Appellant appeals against an assessment made to recover £34,929 of VAT in respect of under and over declarations of output and input tax for periods 12/06 to 6/09.
2. The appeal also concerns a mis-declaration penalty of £1,067.00 in respect of periods 06/08 and 09/08.
- 10 3. The appeal was made out of time but was admitted at the hearing of the Appellant's application on 1 March 2013. The Respondents agreed that the appeal should proceed without the Appellant being required to pay or deposit the tax in dispute.

Background

- 15 (1) The Appellant operated a business of providing first aid training. The business had financial difficulties and ceased trading during the summer of 2009.
- 20 (2) An HMRC officer, John Dowdy, visited the director of the company at his home in July and August 2010. At the first visit the officer discovered that the business had ceased trading and arranged with the director to provide documentation to effect the de-registration of the company for VAT purposes.
- (3) The officer's inspection of the business records, on the later visit, led to the discovery of errors in returns submitted. The officer quantified the extent of the errors and an assessment was issued to recover the VAT under-declared.
- 25 (4) For year ending September 2007 the company turnover was £231,905 and for the year ending September 2008 the turnover was £336,653.
- (5) The Appellant was struck off and dissolved on 11 January 2011, at which point HMRC ceased to pursue the debt. On 16 March 2012 the Company was reinstated at Companies House following an application for administrative restoration.

30 Law and Evidence

4. The relevant materials included:
- (a) Two bundles of documents together with a file of authorities and legislation;
- 35 (b) The case law cited included *Customs and Excise Commissioners v Pegasus Birds Limited* [2004] STC 1509, a decision of the Court of Appeal ("Pegasus Birds");

5. The following is noted:

- (a) The assessment was raised under the provisions of section 73 VATA 1994;
- (b) The assessment was raised within the time limits prescribed by section 73 VATA 1994.
- (c) The penalties were raised under the provisions of section 63 VATA 1994;
- (d) The penalties were mitigated under the provisions of section 70 VATA 1994.

Appellant's submissions

- 10 (1) The Appellant says that correspondence sent by HMRC in the period September to November 2010 was not received. In that period, the Appellant made no submissions or representations on the case.
- 15 (2) The Appellant says that no additional VAT was due and that the Respondents failed to check papers and records which were made available to them in August 2010.
- 20 (3) The Appellant provided nil returns for the period 12/09 to 09/10 since no trading took place from the summer of 2009 and they were advised to do so by Mr Dowdy, an HMRC Officer. Using bank statements, purchase invoices, sales invoices and SAGE accounting information the Appellant Company through Matthew Palmer was able to produce figures which allowed HMRC to identify inaccuracies in returns which had previously been submitted. The VAT under-declarations were established on the basis of these figures. The under-declaration for the period 09/08 to 06/09 arising from the SAGE figures presented by Matthew Palmer were largely agreed between the parties
- 25 (4) The discrepancies identified were discussed between Mr Richard Palmer, Mr Matthew Palmer and Mr John Dowdy of HMRC. No satisfactory explanation could be provided by the Appellant as to why the figures provided on the VAT returns were so significantly different from those provided under the revised SAGE accounts. It was felt that a factor may have been the change in the Company's accounting to cash accounting in early 2008.
- 30 (5) The Appellant disputed whether the penalties which were imposed could have been considered to be a failure to take reasonable care while recognising that the declared figures in returns since 03/08 were significantly different from those declared prior to that date while there was no significant change in the business's activities or turnover.
- 35 (6) The Appellant provided no evidence to challenge the under-declaration or discrepancies in the returns submitted for the periods 30/09/2007 and 30/09/2008.

Respondents' submissions

- 5 (1) The Respondents say that they have correctly assessed VAT underpaid by the Appellant since the assessments are based on the records that were made available by the Appellant and therefore made to the best judgment of HMRC on the information before the officer. The Appellant has produced no other evidence which would cause the officer to amend the assessment;
- 10 (2) The errors which have appeared on the returns 09/08, 12/08, 03/09 and 06/09 appear to be the result of Appellant incorrectly claiming the net tax paid in the following quarterly period. The output tax in the 2nd period included the input tax from the 1st period and the input tax in the 2nd period included the output tax from the 1st period. The errors were discussed with the Appellant through their director, Richard Palmer and his son Matthew Palmer, who had been employed by the Appellant Company and was acting as a temporary bookkeeper. No plausible explanation was given. HMRC advised the Appellant of possible penalties.
- 15 (3) After the second visit by Officer Dowdy, he wrote to the Appellant again and provided a schedule of the VAT considered to be under-declared. As a penalty for the final period of trading, 06/09, fell to be charged under Schedule 24, Finance Act 2008, the officer asked for an explanation for the apparent discrepancy in the figures. There was no response and assessments were issued for penalties to be charged under s.63 for the appropriate period. No penalty was charged for periods 06/09 under Schedule 24, Finance Act 2008.
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Witness evidence

6. The following witnesses gave oral and written witness statements as follows:
- 25 (1) **Matthew Palmer**
- Mr Palmer made the following points:
- (i) He is a former employee and company secretary of the Appellant.
- (ii) In July 2010 a meeting was arranged with HMRC to discuss the fact that the VAT returns had not been completed for some time. In the same month, he provided some data to Mr Dowdy of HMRC and assisted in formulating some preliminary figures.
- 30 (iii) He had some technical issues with his computer and could not provide correct information on the day of the visit. He had all purchase and sales invoices available but they were not inspected by the visiting officer.
- 35 (iv) He presented zero returns in the period after the company had ceased trading and been de-registered for VAT. These were provided for the period 09/09 to 06/10.
- (v) It was agreed that the figures provided in the VAT return for the period 06/09 were inaccurate. They showed VAT due of £75,000
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5 on a turnover of £237,000. He explained that since the VAT returns
had to be filed in order for the company to be de-registered he
provided figures which, though inaccurate, would allow the
company to be de-registered so all filings would be up-to-date. He
had explained this to Mr Dowdy at the time. At the time of Mr
Dowdy's second visit to the Appellant, Mr Matthew Palmer was
able to get his SAGE records and computer records in some order.
He produced a set of quarterly figures which, though at variance
with the figures declared on the VAT returns, he considered to be
10 accurate figures. He explained that Mr Dowdy was happy to accept
the corrected revised figures since this was more consistent with the
business, its turnover and sales and purchase invoices taken together
with bank statements.

(2) Mr John Dowdy

- 15 (i) Mr John Dowdy is one of HMRC's VAT caseworkers. His duties
involve visiting the business premises which are registered for VAT
to check their records and ensure they have accounted for VAT
correctly and by the due date.
- 20 (ii) A visit was made to the Appellant's premises on 21 July 2010. On
checking the VAT records of the company it appeared that they
were incomplete. It was agreed that a return visit would be made
after an interval of 3 or 4 weeks. This should allow sufficient time
for the Appellant to provide all necessary VAT records. Blank
quarterly VAT returns were left with the Appellant for the periods
25 06/09 – 06/10 as no returns had been submitted for those periods.
- 30 (iii) It was explained that the company had not traded since the summer
of 2009. Records were requested from the Appellant for the period
03/07 – 03/09. During the second visit on 24 August 2010 with Mr
Richard Palmer and Matthew Palmer it was explained that Matthew
Palmer had been through the company's records and had brought
them up-to-date. He had a good understanding of the computerised
accounting system used by the company.
- 35 (iv) Computerised accounting system reports were provided in respect of
VAT periods 09/07, 12/07, 06/08, 09/08, 12/08, 03/09 and 06/09.
There were various discrepancies in these reports. The
discrepancies related to VAT amounts being incorrectly included in
more than one VAT periods. This appeared to have been the result
of the computerised accounting system not being shut down at the
end of each period. It had brought forward amounts being recorded
40 more than once. This resulted in the Appellant claiming back more
VAT than the company appeared entitled to. This error related only
to VAT periods up to and including the period 06/09 when the
company had ceased trading.
- 45 (v) An examination was conducted of the Appellant's profit and loss
account for the years ending 30 September 2007 and 30 September

2008 and an attempt was made to reconcile the VAT returns for comparable periods. This showed discrepancies and under-declarations for VAT relating to periods 12/06 to 09/08.

5 (vi) The discrepancies were not properly explained and a letter was sent to the company explaining the discrepancies and enclosing schedules detailing the relevant amounts. Various letters were sent reminding the Appellant to reply but nothing was received by HMRC.

10 (vii) The revised SAGE records provided by the Appellant were accepted as accurate. These were consistent with the business of the company and the turnover for the relevant periods. The figures were presented by the Appellant after a review of their purchase and sales invoices and bank statements.

15 (viii) Given his background knowledge of the training business Mr Dowdy accepted that the VAT charged on the figures presented were plausible as the main cost was labour with over 90% of supplies attracting VAT. The input tax was realistic when compared to other similar businesses.

20 7. It should be stated for completeness that a witness statement was also provided by Mr J C Ballard who was not called as a witness, who confirmed the two meetings between the parties and who questioned the accuracy of HMRC's official notes and minutes of the meeting.

Discussion and conclusion

25 8. Let us start by outlining the law on best judgment. The burden of showing that an assessment has not been made to the best of the Commissioner's judgment falls on the taxpayer. The taxpayer must establish on a balance of probabilities that the assessment was not made to the best of judgment. In *Pegasus Birds*, Carnwath LJ stated:

30 "Although the Tribunal's powers are not spelt out, it is implicit that it has power either to set aside the assessment or to reduce it to the correct figure ... In my view, the Tribunal, faced with a "best of their judgment" challenge, should not automatically treat it as an appeal against the assessment as such, rather than against the amount. Even if the process of assessment is found defective in some respects ... the question remains whether the defect is so serious or
35 fundamental that justice requires that the whole assessment to be set aside, or whether justice can be done simply by correcting the amount to which the Tribunal finds to be a fair figure on the evidence before it. In the latter case, the Tribunal does not require the assessment as a nullity, but should amend it accordingly."

40 9. The Commissioners must examine carefully the material before them. If a trader makes representations to the Commissioners, they must consider those representations and, if necessary, make further enquiries to enable them to reach a

5 decision which is reasonable and not arbitrary. The Commissioners are not required
 to do the work of the taxpayer in order to form a conclusion as to the amount of tax
 which is due. It must be remembered that the primary obligation to prepare returns
 rests with the taxpayer. The taxpayer's information must be made available to HMRC
 10 to carry out their investigations. The Commissioners should therefore make all
 reasonable investigations before making an assessment. The Commissioners are
 required to exercise their power in such a way that they make a valued judgment on
 the material which is before them. The judgment which the Commissioners make
 must be honest and bona fide. The Tribunal should decide whether the method of
 calculation adopted by the Commissioners is reasonable. The Tribunal's primary
 function is to examine the amount of the assessment.

15 10. If the Tribunal finds that the amount of tax to be properly due is different from
 the amount assessed by the Commissioners, then the Tribunal may think it appropriate
 to investigate why there is such a difference. While the Tribunal does have the power
 to set assessment aside, the Tribunal can also decide to give a direction specifying the
 correct amount which is due. The phrase "to the best of their judgment" relates to the
 amount of tax assessed not the manner of assessment of such.

20 11. For the period 09/08 to 06/09 the under-declaration is £29,277. This is based on
 figures provided by the Appellant in undertaking a revision of the VAT returns which
 had previously been provided. The figures were agreed both by HMRC and the
 Appellant.

25 12. The turnover figures first provided were checked against the quarterly figures
 and found to have discrepancies. The Inspector, Mr Dowdy, wrote to the taxpayer to
 express his concerns. He had discussed during his visit a number of errors relating to
 the operation of the company's SAGE accounting system. In addition, he noted
 discrepancies between the turnover detail in the company's year end accounts and the
 VAT return for the comparable period. He set out those concerns and apparent errors
 and discrepancies in a Schedule which was sent to the taxpayer. He asked that the
 Schedule be examined and for the taxpayer to comment on the Schedules provided.
 30 He made clear that if the taxpayer was unable to provide an explanation for the
 discrepancies he would issue a notice of assessment to bring the sums involved to
 account. He also explained that he intended to raise a penalty for the period 06/09
 under the provisions of the Finance Act 2008 Schedule 24. The Schedule which he
 provided was as follows:

35 Period		Declared	Actual
03/08	Output tax	£13,314	£13,380
	Input tax	£1,792	£2,339
	Net tax	£11,522	£11,041
40 Over-declaration		-£481	

Period		Declared	Actual
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	06/08	Output tax	£34,046	£16,670
		Input tax	£26,712	£3,278
		Net tax	£7,334	£13,392
5	Under-declaration		£6,058	
	Period		Declared	Actual
	09/08	Output tax	£43,525	£16,812.44
		Input tax	£38,504	£4,457.42
10		Net tax	£5,021	£12,355.02
	Period		Declared	Actual
	12/08	Output tax	£55,842	£17,338
15		Input tax	£48,883	£5,359
		Net tax	£6,959	£11,979
	Under-declaration		£5,020	
	Period		Declared	Actual
20	03/09	Output tax	£62,634	£13,751
		Input tax	£58,246	£2,405
		Net tax	£4,388	£11,346
25	Under-declaration		£6,958	
	Period		Declared	Actual
	06/09	Output tax	£75,100	£16,583
		Input tax	£65,778	£3,143
30		Net tax	£9,322	£13,710
	Under-declaration		£4,388	
35	Total under-declaration			£29,277

40	Financial Accounts Turnover and VAT returns discrepancies			
	Turnover FYE 30/09/2007	£231,905 x 17.5%		£40,583.75
	VAT declared on sales in Periods 12/06 – 09/07			£36,625.00
45	Apparent Shortfall			£3,958.75
	Turnover FYE 30/09/2008	£336,653		

	Plus opening debtors	£38,081	
	Less closing debtors	£47,536	
		£327,198 x 17.5%	£57,259.65
5	NB Debtors adjustment made for 2008 due to cash accounting being used in VAT Records and date of invoice accounts		
	VAT declared on sales in Periods 12/07 – 09/08		£56,562.00
	(allowing for corrections as above))		
10	Apparent Shortfall		£1,697.65
	Apparent Under-declaration		<u>£5,656.40</u>
15	Overall Under-declaration		£34,933.40

13. The HMRC Inspector therefore discussed the discrepancies during his first visit and during his second visit. The director, Mr Richard Palmer and the book keeper, Andrew Palmer, were not able to satisfactorily explain how the discrepancies arose. In particular the input tax seemed to be a very high figure for the business and no representations were made by the Appellant to explain those figures. The only explanation provided was by HMRC that the Appellant had incorrectly claimed the net paid tax in one period in the following period for a number of quarters.

14. Both parties agreed that the figures which were provided in the VAT returns were based on the initial SAGE figures and incorrect. The sales figures declared on the return were significantly higher at the time when the company was being de-registered and in financial difficulties. For the return 06/09, signed on 24th August 2010 (the date of Mr Dowdy's second visit) they had included the incorrect SAGE figures in the returns.

15. The main inaccuracy in the returns concerned the amount paid as input tax. The output tax declared in the 2nd period included the input tax from the 1st period and the input tax declared in the 2nd period included the output tax from the 1st period. As a result the net tax which has been paid and due in one period was reclaimed in the next period. This happened for four periods. The net tax was reclaimed as additional input tax.

16. Given the knowledge of the Inspector, Mr Dowdy, of similar businesses in the industry, he was able to take a view on the revised figures which were presented by the Appellant. His view is that the figures were accurate. They were more consistent with a company operating in that sector. As it was a training business, the input tax on costs was relatively low as most costs were labour related. For example in the period 03/08 the input was £2,339 and the output tax charged was £13,380. This pattern continued throughout the period 03/08 to 06/09. The turnover in 2008 was £336,653. This equated to roughly £55,000 of VAT at approximately £14,000 output tax per quarterly period. The declared figure for 2008 was £77,000 of VAT on a

turnover of £336,000. According to Mr Dowdy, if one took the historic quarterly figures and compared these to the 2008 quarterly figures then the revised figures represented a more reasonable and fair view of the business than the declared figures. The declared figures did not make any sense.

5 17. In the Tribunal's view given there were no representations made by the Appellant and that the revised figures presented by the Appellant form the basis for the recalculation of the VAT for the period 06/08 to 06/09 then those figures and that assessment is agreed. The VAT liability for that period is £29,277.

10 18. Turning to the periods 12/06–09/07 and 12/07–09/08 the Tribunal finds that the shortfall for the period 12/06-09/07 of £3,958.75 and for the period 12/07-09/08 of £1,697.65 are not accepted. In the evidence presented to the Tribunal it was established that the unreliability of figures arising from the SAGE calculations started in 06/08 there is no reason why the SAGE data for earlier periods did not form a good basis for the VAT returns. Further, it is possible that not all VAT invoices were
15 issued in the relevant period and so there is a possibility that a certain percentage of VAT was not declared at the time. In the notes prepared by the HMRC officer Mr Dowdy, he accepts that the inaccuracies started in the period 09/08 when the traders started reclaiming net tax paid in respect of previous periods. In making his calculations for the year end 30 September 2007, the Inspector took the accounting
20 turnover of £231,905 at the then tax rate of 17.5% and arrived at the figure of £40,583.37 as being the output tax due on all sales standard rated. However, he said that only £36,627 of output tax was declared for the period 12/06-09/07. Given the difference between the two figures he realised a shortfall of £3,958.75. For the year ended 30/09/2008 the adjusted turnover after taking into account debtors was
25 £327,198 which at 17.5% gave output tax of £57,259.65. The VAT declared on sales for the period 12/07-09/08 was £55,562. Given the difference between the two figures he realised a shortfall of £1,697.65.

30 19. In the Tribunal's view it would be inconsistent to argue that the "amended" SAGE data formed a better basis for the later periods but were unreliable as a basis for the earlier periods. The SAGE data for that period could be accepted as the basis of the VAT returns and therefore the shortfall assessments for those two periods should be removed from the calculations. This would mean rather than overall under-declaration of £34,933.40 should be reduced to £29,277. In the Tribunal's view the turnover extracted from the financial statements should not be used to, as it were, top-
35 up the assessments for the earlier period when there was not a problem with the SAGE calculations.

40 20. The last issue which the Tribunal has to look at concerns the mis-declaration and penalty. The mis-declaration in this case applies for the taxes understated as a result of a careless inaccuracy. The maximum penalty is 15% of the tax. In the case of an assessment for carelessness it means that the taxpayer has done or failed to do something which a prudent and reasonable person would have done or failed to do in those circumstances. The HMRC have given a reduction of 50% of the penalty for the cooperation of Mr Matthew Palmer. The penalty was correctly applied.

21. In this case the penalties were for the periods 06/08 with a total liability of £6,482 and for 09/08 with a total liability of £7,758. The penalty which was applied for 06/08 is £486 and the penalty for 09/08 is £581 with the appropriate mitigation. This means a total penalty of £1,067. The penalty carried no implication of dishonesty and allowances had been made for the cooperation of Mr Matthew Palmer.

22. The Appeal is accordingly partly allowed.

23. 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.

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**DR K KHAN
TRIBUNAL JUDGE**

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RELEASE DATE: 3 February 2014