[2017] UKFTT 683 (TC)

TC06102

Appeal number: TC/2015/04512

VALUE ADDED TAX – assessments – no evidence provided of entitlement to input tax – HMRC assuming for a period Appellant not trading – exercise of best judgement – reasonable quantum of assessments – appeal ALLOWED IN PART

FIRST-TIER TRIBUNAL
TAX CHAMBER

BONOMINI ASSOCIATES LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE AMANDA BROWN
DAVID BATTEN

Sitting in public at Taylor House, 88 Rosebery Avenue, London, EC1R 4QU on 14 August 2017.

No one appearing on behalf of the Appellant

Ms Esther Hickey, presenting officer of HM Revenue and Customs, for the Respondents

DECISION

1. This appeal concerns assessments raised against Bonomini Associates Ltd ("the Appellant") by HM Revenue & Customs ("HMRC") in respect of accounting periods 06/12, 09/12, 12/12, 06/13, 12/13, 03/14, 06/14, 09/14 and 12/14 for sums totalling £66,562.79

Hearing in the Appellant's absence

2. This matter was listed to be heard on 14 and 15 August 2017. The notice of hearing was sent to both parties by letter dated 15 May 2017. It was the third time that the matter had been listed, it having been postponed on two prior occasions.

3. By email dated 10 August 2017 the Appellant sought a further postponement of the hearing on the grounds that she was unwell and the first available appointment with a consultant was 14 August 2017.

4. The Appellant's application went before Judge Kempster who refused the application on the following grounds:

> "The dispute concerns evidence for input VAT claimed by the company. The company filed its appeal in 2015, so it has had adequate time to gather evidence of the input tax and to state its case. No medical evidence has been provided concerning the ill health of the company's director, which is apparently longstanding; even if she is unable to attend the hearing, a written statement of the company's case could be provided to the Tribunal. I do not consider that anything is to be gained by postponing the hearing to a future date and, accordingly, it would not be in the interests of justice to put off the hearing. I shall, however, give leave for the company to renew its postponement application before the hearing judge, in case there are other material matters that are not contained in the correspondence made available to me."

5. The Appellant's director again emailed the Tribunal on the morning of the hearing. It was contended that: no medical evidence was available because the appointment was the first appointment; that she had been seeking to obtain information from HMRC and hence was unable to provide the necessary evidence to substantiate input tax recovery; that a written statement was not possible because she had not obtained the evidence she needed from HMRC; and that the refusal to postpone was unfair.

6. Strictly speaking the email represented a request for permission to appeal Judge Kempster's refusal of a postponement; however, the Tribunal has treated it as a renewal of the application before us.

7. It was apparent from the papers before the Tribunal that the Appellant has made a number of what are known as System Access Requests ("SARs"). Pursuant to a SAR a taxpayer is entitled to copies of all material held by HMRC associated with, in

this case, their VAT registration, they are not governed by the Freedom of Information Act. HMRC have already provided the Appellant with a full copy of the VAT file on at least one occasion. It is perhaps somewhat stating the obvious that a SAR results in disclosure of material already provided to HMRC by the taxpayer and will not result in the provision of materials not previously provided to them.

8. As identified by Judge Kempster this case turns on the Appellant's entitlement to input tax which (as discussed below) is required to be evidenced by invoices from the Appellant's suppliers or some form of alternative evidence that the VAT claimed has been incurred.

9. However many SARs requests the Appellant makes they will not progress the Appellant's case. Simply put the Appellant must provide evidence of entitlement to input tax recovery and having not already provided it to HMRC there is no possibility that they can provide it back to the Appellant pursuant to a SAR.

10. As regards the Appellant director's health. The matter was listed for 1.5 days. The Appellant director's medical appointment was due to be on the morning of 14 August 2017. After some very preliminary matters the Tribunal adjourned until lunchtime when the Tribunal service were able to contact the Appellant director and invite her to attend in the afternoon following her appointment. The Appellant refused to attend and did not offer to provide a doctor's note.

11. Mindful of the power to proceed in the Appellant's absence (rule 33 Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009) and the overriding objective to deal with cases fairly and justly and avoiding delay but acting proportionately (rule 2 of the same rules) the Tribunal determined to proceed with the hearing.

Introduction

12. The relationship between the Appellant and HMRC appears to be a tortured one. The long and complex history leading up to this appeal is not relevant to the appeal itself given the statutory jurisdiction of the Tribunal to consider only the matters prescribed in section 83 Value Added Taxes Act 1994 ("VATA").

13. Recognising the Appellant's need (in their absence) to appreciate that all due consideration was given to the appeal it is noted that the Appellant has felt very aggrieved over a prolonged period with the perceived unfair treatment by HMRC. This Tribunal has no jurisdiction to consider such issues which, in any event, appear to have been extensively considered by the Adjudicator.

14. I the context of the various matters raised by the Appellant this Tribunal has the power and obligation to hear the Appellant's challenge in respect of the assessments raised by HMRC (pursuant to section 83(p) VATA) and as to the question of input tax recovery by the Appellant (pursuant to section 83(c) VATA) in each of the periods in respect of which an assessment has been raised. That is the limit of our jurisdiction.

Relevant history

15. The Appellant business is that of a design consultancy.

16. The Appellant's period 09/12 return was submitted showing output tax declared in the sum of £4,120 and input tax claimed in the sum of £11,590 thereby claiming a net repayment of £7,470.

17. The return was subject to a repayment credibility check. Such checks are part of HMRC's normal verification programme to ensure accuracy of returns, particularly where the taxpayer is a business in which, in the general course of trading, would not be expected to be in a repayment position. On 29 October 2012 HMRC wrote to the Appellant requesting to check the books and records for period 09/12. No response was received and the request was renewed on 4 March 2013.

18. By letter dated 26 March 2013 the Appellant notified that due to a power surge both their computer hard drive and back up had lost all relevant data and that it was all having to be re-entered. That letter indicates that the source documentation (invoices to customers, invoices to suppliers) had not been lost as it is clear that the Appellant director was recreating the computer files with a view to submitting her annual accounts for the year 2011/12.

19. On 25 April 2013 HMRC wrote again to the Appellant requesting an appointment to verify the repayment claim for 09/12 and now also 12/12 return which too had been submitted claiming a repayment.

20. Whilst correspondence between the parties continued in connection with a complaint which had been raised by the Appellant (and which is not relevant to the present appeal as a consequence of the Tribunal's statutory jurisdiction) the Appellant did not respond to the verification request. The consequence was that on 30 July 2013 HMRC amended both the 09/12 and 12/12 VAT returns by disallowing all input tax claimed in those periods.

21. On 13 August 2013, following receipt of a further repayment return for 06/13 (03/13 had been rendered showing a net payment due to HMRC of £11.16 and so had not been subject to a repayment credibility check) HMRC telephoned the Appellant to request that the 06/13 return be verified. At that time (as recorded in a telephone note and as set out in the subsequent letter from HMRC dated 16 August 2013) the Appellant director indicated that business commitments prevented a visit being undertaken. HMRC therefore requested the information needed to verify the return.

22. By the same latter of 16 August 2013 HMRC opened an inquiry into the VAT returns then remaining in time for assessment (i.e. those for the prior 4 years) on the basis that whilst those had been processed and not subject to verification they too were repayment returns and required to be investigated. The HMRC officer acknowledged the IT issued that had been referred to in the Appellant's letter of 26 March 2013 and invited direction on the inspection of the records for that period.

23. The Appellant's 09/13 return was a payment return showing net £22.97 due to HMRC. However, 12/13 was again a repayment claim and by letter dated 7 February 2014 HMRC opened a repayment credibility in respect of 12/13 period (incorrectly stated to be 11/13 in the letter).

24. On 6 May 2014 the Appellant notified HMRC that as a consequence of illness the director was appointing a third party to deal with the verification. The contact details of that third party were not, however, provided to HMRC.

25. On 28 August 2014 HMRC opened a repayment verification for period 06/14.

26. On 24 October 2014 HMRC notified the Appellant that the repayment claims for periods 12/13, 03/14 and 06/14 were refused. As with the 0912 and 12/12 for these returns the input tax claimed was reduced to zero leaving the net sum due to HMRC as equal to the output tax declared.

27. Also on 24 October 2014 HMRC issued assessments to VAT in respect of periods 12/10, 03/11, 06/11, 09/11, 12/11, 03/12, 06/12 and 06/13 (the assessment for period 06/13 was subsequently amended, see paragraph 29 below). The Tribunal were told that in respect of these assessments HMRC applied a policy that assumed that the Appellant was not trading in these periods. As a consequence of that assumption both the Appellant's declared output tax and input tax were reduced to nil with the consequence that the repayment claims that had been processed for those periods were reversed and HMRC sought to recover only that net sum.

28. The Appellants 09/14 return was not formally subject to a repayment verification. Given the history it was simply disallowed by a letter dated 5 December 2014. The return amendment again reduced the input tax claim to zero leaving the output tax due.

29. On 8 December 2014 HMRC amended the assessment for 06/13. The original assessment raised on 24 October 2014 assessed only for the net tax that had been over claimed on the return (i.e. both output tax and input tax were reduced to nil). By this assessment they reduced the input tax to nil leaving the full amount of output tax due from the Appellant.

30. A verification was opened on 6 February 2015 into the period 12/14 return and in the absence of any evidence supporting the input tax claim on 23 February 2015 the return was amended reducing the input tax to zero.

31. A summary of the amendments and assessments is provided in the appendix to this judgment.

32. It is also relevant to note that it appears that during April 2014 the Appellant business changed its address. The Appellant believed the change of address was then automatically notified to HMRC. However, the Appellant did not formally notify HMRC until May 2015 though it is apparent that in connection with one of the ongoing complaints HMRC did begin corresponding with the Appellant at its new address from February 2015. Communication regarding verification of returns and

the notification of assessments continued to be addressed to the business's old address until May 2015.

33. The Appellant's appeal documentation is not the easiest to follow. The letter which is stated to be the appealed decision is in fact a response to one of the many complaints issued by the Appellant. That letter dated 30 June 2015 provides the Appellant with copies of all amendments to returns and assessments and, in essence, represents agreement to any out of time appeal that the Appellant sought to bring.

34. Much of what is included in the grounds of appeal and correspondence deals with the perceived unfair treatment of the Appellant by HMRC and not with matters pertinent to the appeal. The points raised which are relevant to the matters to be considered by the Tribunal are that:

(1) in 2012 the business worked on a project for a client in the United Arab Emirates. To service that contract the Appellant was required to engage a number of subcontractors. Unfortunately the Appellant was not paid by its customer but had to make payments to the subcontractors. As the Appellant is on cash accounting (where VAT is declared not by reference to invoices raised and received but by payments on those invoices) it had claimed significant input tax but was not yet required to account for the associated output tax.

(2) due to an IT malfunction the Appellant did not have access to their records for the period up to 2012

(3) the assessments and amendments were not properly notified as they were sent to the wrong address.

35. HMRC confirmed that they had received corporation tax returns (though in some instances late) up to the 13/14 tax year.

Legislation and case law

36. The legislation relevant to the present appeal is contained in VATA and the Value Added Tax Regulations 1995 "the VAT Regs").

37. As regards the Appellant's claims to input tax:

(1) Section 24 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) Regulations 29 VAT Regs provides that input tax claims are required to be evidenced by invoices received from the taxpayer's supplier bearing certain specified information. There is however, a provision that permits HMRC to accept alternative evidence supporting such claims to input tax.

38. As regards assessments section 73 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. Assessments are to be

made within a period of 4 years from the end of the prescribed accounting period (section 77(1)) and whilst they are required to be notified to the taxpayer there is no time limit for notification.

39. There is a long history to the case law on what does and what does not amount to best judgement. However, for the purposes of the present appeal it is sufficient to summarise what is now a well-established test in determining whether assessments raised have been raised in HMRC's best judgement.

40. In the case of *Pegasus Bird Ltd v HM Customs & Excise [2004] EWCA 1015* 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) v HM Customs & Excise [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."

41. By reference to the *Pegasus Bird* judgement 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; thus where a Tribunal finds an assessment has not been made in exercise of best judgment it has a discretion whether to amend the assessment or conclude that it is void. It is clear from the judgment that a decision to void the assessments is not one that should be taken lightly and is likely to arise only in circumstances where the basis on which the assessment is raised and/or its amount is wholly unsustainable on the evidence available. 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.

HMRC's case

42. HMRC contend that the Appellant has completely failed to substantiate their entitlement to input tax having failed repeatedly to provide copies of invoices or any alternative evidence supporting the claim to input tax.

43. HMRC's representative explained that for the periods up to 06/12 it had been HMRC's policy when there was a complete refusal by a business to respond to requests for verification to consider the business as not trading and to reduce all entries on the returns to nil. From period 09/12 that policy changed and where no evidence justifying input tax recovery was provided any assessment or amendment to a return was only to reduce the input tax recovery to nil pending supporting documentation.

44. As regards the Appellant's change of address HMRC contended that they were entitled to rely on the recorded place of registration until notified otherwise. Such notification was made on 21 May 2015. HMRC also contended that it was apparent from correspondence that the Appellant was in receipt of most if not all relevant

correspondence. Irrespective of the change of address notification however, HMRC had not, in any way, prejudiced the Appellant as all appeals had been accepted out of time.

Discussion

45. The statutory provisions are absolutely clear: in order to claim input tax and off set it against output tax due a taxpayer must hold invoices from their suppliers or some alternative evidence to substantiate the claim. HMRC are entitled to be provided with that evidence before agreeing to honour the input tax credit claimed.

46. The Appellant has systematically failed to provide that evidence to HMRC. The Tribunal accepts that the Appellant suffered a catastrophic IT failure however, that does not absolve it of producing the relevant evidence of supplies made to it. As referred to in paragraph 18 above, there was no indication in the Appellant's letter of 26 March 2013 or subsequently, that the IT failure had caused a loss of the paper invoices received. Nor does the IT failure prevent the Appellant from producing bank statements evidencing payment, or obtaining duplicate invoices from suppliers. There are all manner of means by which the Appellant could substantiate the claim to input tax, they have just chosen not to do so.

47. The Tribunal agrees with HMRC that pursuing the SARs will not help the Appellant. The Appellant has never provided the evidence of input tax to HMRC so it will be impossible for HMRC to provide it back to the Appellant.

48. For all relevant periods post from 09/12 HMRC have amended the Appellant's returns by disallowing all input tax. In the absence of any evidence to support the input tax claimed, and by reference to the approach set out in *Pegasus Bird* the Tribunal must determine whether the those amendments (which represent assessments made against returns submitted but not processed) represent, by reference to the evidence and material available to the Tribunal, the correct quantum of tax due.

49. For the periods prior to 09/12 the position is more complicated because HMRC have raised assessments based on an assumption and policy that the Appellant was not trading.

50. The Appellant company has for all but two prescribed accounting periods in the period from 1 October 2010 through to at least 31 December 2014 rendered returns claiming input tax in excess of the output tax declared. For the accounting years up to 31 March 2014 the Appellant has also prepared accounts and corporate tax returns in respect of its business activity as a design company.

51. HMRC confirmed to the Tribunal that no attempt had been made by them to deregister the Appellant and by reference to the turnover stated on the returns the Appellant had not registered for VAT on a voluntary basis, their turnover exceeds the statutory threshold.

52. In the Tribunal's view there is no evidence to corroborate the conclusion that the Appellant business was not trading for the period up to 31 March 2013.

53. On the basis that the Appellant was trading, rendering VAT returns and, for the majority of the period also preparing accounts and corporate tax returns the Tribunal considers that it is reasonable to conclude that there is evidence that some input tax must have been incurred which HMRC could have recognised. The Tribunal therefore considers that HMRC, acting in best judgment, should have allowed some notional input tax recovery when making the assessments.

54. HMRC confirmed that in some instances they do assess taxpayers without evidence of input tax to output tax after giving credit for an imputed sum of input tax at a rate of 5% of the output tax assessed. The Tribunal considers for the periods from 03/13 it is reasonable to require that HMRC afford that same latitude to the Appellant reflecting the fact of trading as some form of alternative evidence. The Tribunal therefore reduces the assessments for each of periods 09/12, 12/12, 06/13, 12/13, 03/14, 06/14, 09/14 and 12/14 by 5%.

55. For the periods prior to 03/13 the conclusion that the Appellant was clearly trading presented the Tribunal with somewhat of a dilemma because it illustrates that the assessments have been raised based on a fundamental error. Somewhat ironically that error was one that was materially in the taxpayer's favour because as a consequence of also reducing output tax to nil the Appellant was given credit for sums which were unquestionably due to HMRC.

56. The Tribunal has reflected hard on how the *Pegasus Bird* test should be applied. What is clear is that a premise that the Appellant was not trading is a very fundamental error but it cannot be said that it was not a genuine and honest attempt to assess the Appellant for VAT considered to be properly due. The policy adopted by HMRC of assuming that an uncooperative trader was not in fact trading appears to have been a genuine attempt to give the taxpayer the benefit of the doubt. By reducing output tax to nil HMRC were stepping away from the collection of tax due to them and almost certainly, in that case, tax that was permitted as input tax credit in the hands of the Appellant's customers. The binding guidance from the Court of Appeal on how to apply the best judgment test requires this Tribunal to uphold assessments unless HMRC's error goes to the integrity of the assessment (as distinct from its accuracy). Where the error doesn't go to its integrity then the Tribunal should amend the assessment.

57. The cases in which the question of best judgment arises invariably, if not exclusively, where the taxpayer claims that the assessment has been over stated. Whilst the Appellant in this case too claims that the assessments have been over stated (because it is entitled to input tax despite any attempt to provide invoices or other evidence to substantiate that claim) the error identified by the Tribunal is one which leads to the conclusion that the assessments have not been over stated but rather that they have been considerably understated.

58. In such circumstances would it be right to conclude that the error was so fundamental that it represented anything other than a genuine attempt to assess the Appellant to a fair amount of tax? After careful consideration of the *Pegasus Bird* test the Tribunal has concluded that it would be wrong to set the assessment aside on

the basis of the error. To do so would further deprive HMRC of the ability to collect any tax in the periods in which, absent adequate evidence of input tax, is unquestionably due.

59. The Tribunal does have the power under section 84(5) VATA to increase the amount assessed where it is found that the assessment is under stated. The Tribunal has, in effect, found that the assessments for periods 12/10 to 6/12 have been under stated because HMRC would have been entitled to raise them on the same basis as those post 09/12 i.e. adjusting only the input tax down to nil thereby collecting the output tax collected by the Appellant from its customers. In order to increase the assessments the Tribunal is required to give a direction that the amount assessed is less than it should be.

60. HMRC did not invite the Tribunal to make such a direction and the Tribunal considers that it would not be right to do so. HMRC are out of time to raise further assessments and it does not seem fair on the Appellant that the Tribunal should correct HMRC's error in this regard. Whilst the assessments are materially understated the Tribunal takes the view that HMRC should carry the consequences of their own error to treat the Appellant as not trading. The consequence is that the Appellant has been given a substantially higher credit for input tax in those earlier period than it was entitled to in the absence of evidence to support the claim.

61. Finally, as regards the notification of the assessments. It is clear that even were it the case that the Appellant had not received notification of the assessments and amendments prior to 30 June 2015 they were all re-notified at that point. The legislation requires assessments to be made within the prescribed time limit and whilst it is HMRC's policy to also notify them within that time frame in this instance they were all sent to the Appellant's registered address and were not returned through the postal service; by virtue of section 98 VATA and section 7 Interpretation Act 1970 in so doing they effected legal service of the assessments and amendments. Neither HMRC nor the Tribunal have taken any issue with an out of time appeal and accordingly the Appellant has not, in any way, been prejudiced.

Disposition

62. The assessments for periods 12/10, 03/11, 06/11, 09/11, 12/11, 03/12 and 06/12 the assessments are upheld and the appeals dismissed.

63. The assessments for periods 09/12, 12/12, 06/13, 12/13, 03/14, 06/14, 09/14 and 12/14 are to be varied allowing 5% of output tax as credit for input tax on the grounds that by simply trading there is some alternative evidence for notional input tax recovery. Save to that extent the assessments are upheld.

64. Whilst the assessments have been upheld it remains open to the Appellant to comply with the long standing request to provide the books and records of the company to HMRC or otherwise provide evidence substantiating the input tax claimed. Upon production of such records HMRC will reduce the assessments.

65. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

AMANDA BROWN
TRIBUNAL JUDGE

RELEASE DATE: 4 SEPTEMBER 2017

Period	Amendment/ assessment	Date	Address sent	Stated reason	Amount
12/10	assessment	24/10/14	old address	Not trading	£1,089.00
03/11	assessment	24/10/14	old address	Not trading	£1,116.00
06/11	assessment	24/10/14	old address	Not trading	£42.00
09/11	assessment	24/10/14	old address	Not trading	£3,707.00
12/11	assessment	24/10/14	old address	Not trading	£3,773.00
03/12	assessment	24/10/14	old address	Not trading	£3,884.00
06/12	assessment	24/10/14	old address	Not trading	£4,874.00
09/12	amendment	30/7/13	old address	No evidence of input tax	£4,120.00
12/12	amendment	30/07/13	old address	No evidence of input tax	£6,998.31
03/13	NONE			PAYMENT RETURN	
06/13	amendment	08/12/14	old address	No evidence of input tax	£6,086.44
09/13	NONE			PAYMENT RETURN	
12/13	amendment	24/10/14	old address	No evidence of input tax	£7,818.69
03/14	amendment	24/10/14	old address	No evidence of input tax	£6,865.41
06/14	amendment	24/10/14	old address	No evidence of input tax	£5,722.10
09/14	amendment	05/12/14	old address	No evidence of input tax	£3,258.66
12/14	amendment	23/02/15	old address	No evidence of input tax	£1,460.16