[2019] UKFTT 203 (TC)

TC07051

Appeal number: TC/2018/01534

VALUE ADDED TAX - Penalty for an inaccurate return - Schedule 24 Finance Act 2007 - Whether inaccuracy deliberate? - No - Whether inaccuracy careless? - Yes - Whether there should be any further discount for disclosure? - No - Appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

FAUX PROPERTIES (A PARTNERSHIP) **Appellant**

- and -

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

TRIBUNAL: JUDGE CHRISTOPHER MCNALL

Sitting in public at Tribunal Hearing Centre, Alexandra House, 14-22 The Parsonage, Manchester M3 2JA on 28 February 2019

Mr Michael Faux, a Partner, for the Appellant

Mrs Samantha Carr, an Officer of HMRC, for the Respondents

DECISION

1. This is my decision in relation to the Appellant's challenge, made in a Notice of Appeal dated 13 February 2018, against a penalty of £15,379 issued to the Appellant on 1 July 2016 ('**the Penalty**') under Schedule 24 of the *Finance Act 2007*.

2. The Penalty related to the Partnership's VAT return for the period ending 05/15. The Partnership should have declared £33,800 as output tax, but instead made a nil return.

3. This appeal is made out of time. The Notice of Appeal contains an application to extend time, which HMRC does not oppose. I extend the time accordingly.

4. I remind myself that this is a penalty appeal, and therefore HMRC bears the burden (albeit, only to the civil standard, namely the balance of probabilities).

5. The Appellant is a partnership with four partners: Mr Faux, his wife, and their two children. However, I accept that Mr Faux was the only active partner and that the events which gave rise to this appeal involved him and him alone, and did not involve any of the other partners.

6. In its Notice of Appeal, the Appellant accepts liability for interest, and a penalty, but does not accept liability for what is referred to as 'the maximum charge', which I take to mean that it does not accept that its conduct should have been treated by HMRC as deliberate.

7. I heard oral evidence from Mr Faux. I also heard oral evidence from Officer Lenny Holmes, an Officer of HMRC, who had made a witness statement dated 21 August 2018.

The facts

8. The Appellant registered for VAT on 24 March 2006. Its business was described as one of commercial property acquisition.

9. The Appellant owned a commercial property in Warrington ('**the Property**'). On the same day that it registered for VAT, it opted to tax the Property. That had the effect that the Appellant could reclaim VAT spent (for example) on refurbishments, but would be obliged to charge VAT if and when the Property came to be sold.

10. On 20 March 2015, the Appellant sold the Property for £202,800 including VAT (£179,000 ex VAT). The VAT element was £33,800.

11. On that same date, the Appellant issued a VAT-only invoice to its purchaser.

12. It is common ground that the £33,800 should have been accounted for in the VAT period ending 05/15.

13. However, on 9 July 2015, the Appellant filed a 'nil' return for the period ending 05/15. It is common ground that this was an inaccuracy.

14. HMRC first raised the matter of the VAT on 11 August 2015 (when the sum of VAT due was stated, wrongly, to be £40,560). That letter asked the Partnership to contact the writer, Officer Lenny Holmes, a Compliance Officer of Specialist Investigations, within 14 days if it wanted to comment or give any further information. It did not do so.

15. The amount of VAT due was amended on 3 September 2015 to £33,800.

16. On 15 September 2015, Officer Holmes issued a Notice of VAT assessment of £33,800 to the Appellant, as well as interest for the period ending 05/15.

17. On 18 September 2015, the Partnership instructed a Mr Stephen Yates of FNI Limited, described on their stationary as 'Specialist Accountants, Business Advisers and Advocates' as its agent in relation to its VAT affairs.

18. On 22 September 2015, there was a conversation between Mr Yates and Officer Holmes, following which Officer Holmes sent Mr Yates scanned copies of the VAT invoice from Faux Properties and the completion statement for the Property, both showing VAT.

19. Various delays ensued, with Officer Holmes giving Mr Yates extensions of time. However, there was no communication, or no substantive communication, between Mr Yates and HMRC between October 2015 and February 2016.

20. On 26 February 2016, a penalty explanation letter was sent, setting out the sum of £15,739 and how this had been arrived at. It asked for relevant information by 25 March 2016. The penalty was notified again on 11 May 2016.

21. On 17 June 2016, FNI wrote a long letter taking issue with various matters, most of which seem to me to be of no real consequence when it comes to the VAT penalty which HMRC intended to charge. All it said in relation to the Penalty was that *'the error made by the taxpayer on this occasion was an administrative error made by an Administrator'*. Self-evidently, that explanation was inadequate. It did not explain how that alleged error came to be made, nor why, if made by an (unidentified) 'administrator' this has not been detected by the Appellant at the time. FNI sought cancellation of the penalty in its entirety *'due to the fact that the error was a basic administrative error'*.

22. On 23 June 2016, a Mr R Felstead, a Debt Manager from HMRC's office in Worthing wrote to Mr Yates stating that the penalty was £5,070. Although the letter does not say this, £5,070 is 15% of £33,800. It is otherwise far from clear how this figure can have been arrived at since at that time no penalty had been issued.

23. I accept Officer Holmes' evidence that the letter of 23 June 2016 was issued in error. It has given rise to some criticism by the Appellant which argues that it is unfair to penalise it for an error when HMRC itself makes errors. Having heard him give evidence, I am satisfied that Officer Holmes, who was the responsible officer, did not

know anything about it at the time. Moreover, and even though done in error, the error was extant only for a few days - that is, until the Notice of Penalty assessment was sent on 1 July 2016.

24. On 28 June 2016, Officer Holmes spoke to Mr Yates, and, following that discussion, wrote to him as follows:

> "You stated that, in your opinion, I had already decided at the beginning of this enquiry that a deliberate penalty would be due. I explained that your client had raised a VAT only invoice, received the money and not informed HMRC. Given the lack of any evidence to the contrary apart from the assertion by you that this was a 'minor administrative error' a deliberate penalty is deemed appropriate".

25. That was, and remains, a succinct summary of HMRC's position.

26. The Notice of Penalty assessment was sent on 1 July 2016. In accordance with its earlier position, HMRC, through Officer Holmes, calculated the penalty on the footing that the inaccuracy was deliberate and prompted, but not concealed, giving a penalty range of 35% to 70%. The penalty was subject to mitigation to reflect the quality of disclosure: 'telling' (0%); 'helping' (40%); 'giving' (30%) = 70%. The reductions for helping and giving were the maximum reductions, on the footing - explained to me by Officer Holmes in his evidence and which is entirely fair - that HMRC did not need any helping or giving to arrive at the penalty. The reduction of telling was 0% since 'we talked to partner Debbie Faux who advised that she would send details regarding the sale of the property. No information was received. When telephoned the accountant said that he was 'waiting for records from his client'.

27. The difference between the minimum (35%) and maximum (70%) is 35%. 35% x 70% deduction = 24.5%. Deducting 24.5% from the maximum of 70% = 45.5%. The Potential Lost Revenue is £33,800. £33,800 x 44.5% = £15,379.

28. The Appellant did not pay the VAT which was owed to HMRC until 21 December 2017. However, this is against the background that the Appellant had, on or about 30 June 2016, paid FNI £33,800 but FNI had not paid that money to HMRC (and indeed, according to Mr Faux, has not yet repaid it to the Appellant either). For these purposes, it does not matter that the VAT due was paid to FNI before (as it happens, on the day before) the penalty was levied. The penalty was levied for inaccuracy, and the inaccuracy had occurred on 9 July 2015.

The explanation for the inaccuracy

29. Mr Faux's evidence as to how the nil return came to be made was far from satisfactory. His evidence to me was that he did not have personal knowledge of how the VAT return came to be completed. It was an electronic return. He thought that this had been done by a former employee (from whom I did not hear any evidence) using a computer inside the building. Mr Faux had no satisfactory explanation as to why a former employee would have had unimpeded access to the building, and to Mr Faux's

computer inside it in July 2015, even though the building had been sold four months earlier, in March 2015.

30. Nor was Mr Faux's evidence wholly satisfactory when it came to the fact that, given his knowledge that the building had been marketed and sold for £179,000 (net of VAT) he had not been alerted to the need to pay VAT by the receipt of £202,800 in his bank account. The difference - £33,800 - is far from insubstantial and is obvious. I find it difficult to accept that someone who had sold something for £100 thousand something would not have found something untoward in the receipt of £200 thousand something. Mr Faux's evidence about where his bank statements were sent, and by whom they were read, was vague.

31. Mr Faux was unable to give any evidence as to how the VAT-only invoice came to be produced, by whom, when, or where.

32. Having realised that VAT was payable, Mr Faux's evidence as to what happened next does not speak wholly to his advantage. When he found out about the nil return, he took the deliberate decision to hold onto the VAT, and not to pay it over to HMRC - whose money it was. I am entirely satisfied that Mr Faux (who had been, until then, a compliant taxpayer), when he was made aware of HMRC's concerns as to the nil return, knew that the VAT was payable, and knew that he should have paid it.

33. I am likewise satisfied that if, as he says, he was told by his then-agent - after the due date - not to pay the VAT on the footing that his then-agents could use it as 'leverage' against HMRC when it came to the penalty, that Mr Faux knew that course of action to be wrong. But nonetheless, he went along with it for quite some time. I am not convinced by Mr Faux's explanation that, having engaged FNI, he was barred by FNI from contacting HMRC himself. I have not seen the contract between the Appellant and FNI. All I have seen is a short passage, set out in another letter, which, read in isolation, makes little sense. But in my view it is not relevant.

34. FNI wrote to HMRC on 1 July 2016 seeking to explain that the Appellant could not pay both the £33,800 '**and** cover legal costs to dispute the penalty' (emphasis in the original). This approach was wrong. It reflects a serious misapprehension of the Appellant's legal obligation to pay the VAT which it had received, regardless of the existence of any dispute as to the penalty.

35. However, and although Mr Faux was emphatic in seeking to attribute the making of the nil return to FNI, he fails to distinguish between matters which took place after the filing of the nil return, and those which took place before it. Matters which took place afterwards do not explain why the nil return was made: that is the inaccuracy with which I am concerned in this appeal. As such, events on or after 9 July 2015 are of very limited evidential value in shedding any light on how the nil return itself came to be made.

36. I also have regard that to the fact that, had HMRC, in the course of making a check into the tax affairs of the Appellant's buyer, not come across the Appellant's VAT

invoice, then, in all likelihood, HMRC would never have detected that the Appellant had received £33,800 VAT.

37. In some of the correspondence, Mr Faux mentioned that he had been suffering from ill health during this time. There was no other evidence. However, during the hearing, Mr Faux handed up a letter from a consultant dermatologist dated 26 February 2019 which confirmed that Mr Faux had been, and remains, under medical care since 17 September 2013.

38. Mr Faux had been diagnosed as suffering from a serious health condition, and I accept his oral evidence that the anxiety about this had affected his ability to deal with his everyday affairs, including the matter of the VAT in relation to this sale. It was clear from his oral evidence that he genuinely had little knowledge, or recollection, of the sale or the preparation of the VAT-only invoice. His evidence was often vague, and sometimes strayed into defensive, but I did not assess his evidence, overall, to be given dishonestly. It reinforced the evidence that he did not really know what was going on when the Property was sold. Hearing him give evidence, it was obvious to me that Mr Faux is still genuinely frustrated and anxious in relation to this situation.

The Law

39. Whilst Schedule 24 makes no provision for reasonable excuse, it would be nonetheless be wrong for me to disregard the evidence which he has put forward as to his state of health at the time.

40. Ultimately, this is a case about whether the conduct of Mr Faux, or those acting on his behalf, were 'careless' or 'deliberate' in making the inaccurate return.

41. As I commented in *Changtel Solutions Limited and another v HMRC* [2016] UKFTT 399 (TC):

> "96. When it comes the imposition of a penalty, inaccuracy is not, in and of itself, enough. That is simply the act. There has to be more - namely, a mental element. The penalty regime is fault-based ('degrees of culpability'). The basic structure is to divide inaccuracies into 'careless' (less serious) and 'deliberate' (more serious). Unfortunately, the legislation does not provide any further guidance as to where the dividing line between the two classes of inaccuracy is to be found. It is an important line to draw, or to discern, since the penalties are levied with reference to that element. It is clear by inference that there must be some inaccuracies which are neither careless nor deliberate, and in connection with which no level of culpability can be fixed upon the taxpayer.
>
> 97. We consider that 'careless' for these purposes can be equated with 'negligent conduct' in the context of discovery assessments, which is to be judged with reference to the reasonable taxpayer, and what the (hypothetical) reasonable taxpayer, exercising reasonable diligence in the completion and submission of his return, would have done. Hence, careless does connote some fault, sufficient to attract censure when measured against an objective standard.

98. 'Deliberate' goes beyond that. In terms of inaccuracy, we consider it to mean 'done with a set purpose'. That purpose must be to produce an inaccuracy, within the meaning of Schedule 24. There is an element of intent in 'deliberate' which is not present in 'careless'. It represents a higher degree of fault.

99. We are reassured that reasoning is correct given that the draftsman of the Schedule provides that concealment aggravates deliberate conduct, but is not a factor at all in careless conduct."

42. I acknowledge that different compositions of this Tribunal have articulated their approaches to this question in different ways, but all of these clearly differentiate between something done volitionally or with motive and those things done carelessly.

Decision

43. I have not found this an entirely easy question to answer. But ultimately, taking all the above into account, I am not satisfied, given the incidence of the burden in this appeal, that HMRC have succeeded in discharging the burden of demonstrating that the inaccuracy of the nil return was deliberate as opposed to careless. Therefore, the penalty, insofar as it was imposed on the basis of deliberate conduct, cannot stand.

44. Even though I am departing from the analysis applied and decision reached by Officer Holmes, I should say, to avoid any doubt on the point, that I found Officer Holmes' evidence coherent and impressive, and my decision does not reflect any lack of competence or lack of good faith on his part. My impression from his oral evidence was that he had also struggled with the decision as to whether this inaccuracy was deliberate or careless. I can understand why he decided what he did. But, put shortly, he came to one view, and I have come to another.

45. Although I have decided that the inaccuracy was not deliberate, I am nonetheless satisfied that HMRC has demonstrated that the inaccuracy was careless. There was a failure by Mr Faux, on behalf of the partnership, to take reasonable care in the making of the return. For the reasons already set out, I have a degree of scepticism as to Mr Faux's evidence. But, at the very least, he should have checked the return before it was sent, and he did not. If he personally was unable or unfit to check the return, then he should have authorised someone else to do so. He should have known that the Property had been sold for over £200,000 in March 2015, and so he should have known or realised that the purchase price included a non-trivial sum by way of VAT, which was payable.

46. I reach my conclusion that the conduct was careless irrespective of any concession on this point by the Appellant in its Notice of Appeal, and without any regard of the offers to settle of which I was made aware.

47. When it comes to the discount applied, I am not invited to reduce the maximum discounts applied to helping and giving. The only only element which requires my consideration is HMRC's decision not to apply any discount at all in relation to 'telling'.

48. I am satisfied that this decision was fair, and appropriate. I do not see any cogent evidence or material which would justify my interference with this element of HMRC's decision. As such, I do not interfere with the discount.

49. The Tribunal has no jurisdiction in relation to interest.

50. Accordingly, I allow this appeal in part. The penalty is to be re-calculated on the basis of careless conduct, applying the same deductions as before for the quality of disclosure.

51. 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.

DR CHRISTOPHER MCNALL
TRIBUNAL JUDGE

RELEASE DATE: 20 MARCH 2019