



TC03559

Appeal number: TC/2012/10520

VAT –£39,498.06 penalty for failure to submit correct VAT returns - payments made against assessments – when prompted actual returns substantially higher – failure careless- penalty reduced to £22,750.32- appeal allowed in part.

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

JASWANT SINGH BHATT

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE DAVID S PORTER
MR LESLIE BROWN**

Sitting in public at Phoenix House, Bradford on 10 April 2014

Mr Nigel Broadbent, a solicitor, for the Appellant

Mrs Ann Sinclair, a Higher Officer, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents.

DECISION

1. Mr Jaswant Singh Bhatt (Mr Bhatt) appeals against a penalty in the sum of £39,498.06 raised by the Respondents (HMRC) in a letter dated 29 February 2012 arising from Mr Bhatt's failure to file the correct VAT returns for the periods 02/10 to 05/11. Mr Bhatt accepts that the returns had been completed incorrectly. He did not accept that there had been a deliberate intention behind the incorrect completion and that as a result the penalty should be reduced. At the hearing he stated that he had been suffering from overwork and depression. HMRC said that the penalty had been assessed on the basis that the earlier returns had been completed incorrectly deliberately, when Mr Bhatt knew that they were incorrect, and that the failure came to light as a result of a visit by HMRC when enquiring about a repayment.

2. Mr Nigel Broadbent (Mr Broadbent), a solicitor, appeared for Mr Bhatt. Mr Bhatt gave evidence under oath as did his partner Kathryn O'Brien. Mr Broadbent produced their witness statements at the appeal. Mrs Ann Sinclair (Mrs Sinclair), a higher officer, appeared for HMRC and called Mrs Josephine White, an Officer of HMRC, now retired, who affirmed. We were referred to the case of *Astoria Properties Ltd; Churchill* [2012] TC 01772.

The Law

3. Schedule 24 of the Finance Act 2007 (the Act) provides for penalties to be raised by HMRC where documents are submitted for VAT purposes, which do not disclose the true position. The amount of the penalty depends on the culpability of the taxpayer: That is, was the taxpayer careless; did the taxpayer act deliberately, but made no attempt to conceal the error or did the taxpayer seek to conceal it. A taxpayer's actions can become careless if discovering the error he or she failed to do anything about it.

4. The amount of the penalty depends on the taxpayer's culpability and is calculated on the potential lost revenue. The potential lost revenue is the amount by which the declared tax is increased by the default which includes the amount of the correction to a repayment. The taxpayer's liability to the penalty can be reduced by his or her disclosure, which is assessed on the basis by which the taxpayer tells HMRC of the details, assists in correcting the error and makes all necessary documents available to HMRC so that it can arrive at the correct figures.

5. It also matters whether the disclosure was prompted or not. The disclosure will be prompted if it has been made because HMRC enquiries have given rise to the disclosure. It is unprompted if the taxpayer has alerted HMRC to the position of his or her own volition. Where, as in this case, Mr Bhatt disclosed the default as a result of enquiries made by HMRC the disclosure was prompted.

6. The Act provides for a penalty of 30% of the potential lost revenue where the taxpayer has been careless; for 70% where the taxpayer has acted deliberately; and at 100% where the taxpayer has acted deliberately and has sought to conceal the error. These percentages can be reduced at each level dependent on the taxpayer's

disclosure as set out at paragraph 4 above. Such reduction cannot fall below 15% where the disclosure has been prompted and was careless and below 35% where the disclosure was prompted but deliberate.

5 7. A special reduction can be made by HMRC where HMRC considers that there are special circumstances which have given rise to the default. Special circumstances have to be something more than a 'reasonable excuse' and cannot include an inability to pay the tax or by the fact that the underpayment by one taxpayer has been corrected by an over payment by another.

10 8. Section 14 (1) of the Act provides that HMRC may suspend all or part of a penalty for a careless inaccuracy under paragraph 1 by notice in writing to then taxpayer. There is also an overriding relief from the penalty if the taxpayer can show that there was a reasonable excuse for the default. The Tribunal has all the powers that HMRC has in relation to the penalty, but may only order HMRC to suspend the penalty if it thinks that HMRC's decision not to suspend was flawed.

15 **The Facts**

9. Mr Bhatt told us that he was the eldest son of an Indian family and as such he was expected to take responsibility for the entire family, both financially and emotionally. He had originally worked for his parents in their hotel business. They had owned and run the Cartwright Hotel since November 1987. His mother cooked and his father ran the business. Mr Bhatt became a partner in the business in 1995, but worked as the front of house manager. The business was declining and the family tensions arose because they were all living at the Hotel.

25 10. As a result, in about 2000, Mr Bhatt decided to open a fish and chip business with his brother in Saltaire. They converted the fish and chip business into a restaurant and wine bar to be known as 'Don't Tell Titus'. The idea had been too ambitious and merely added to the family tensions. In 2009 the opportunity arose for Mr Bhatt to acquire The Boathouse Inn, which was just down the road from the restaurant. Mr Bhatt's relationship with his brother was so strained that it was not until 2012 that the partnership in that restaurant business was dissolved.

30 11. His parents decided to sell the Cartwright Hotel whilst he was also running the Boathouse Inn and helping his brother with 'Don't Tell Titus'. He had to deal with the sale of the Cartwright Hotel for his parents, which took place in 2007 and the families had to find other accommodation. As a result, he purchased a house for his parents for £190,000 with the assistance of a mortgage of £165,000 which his partner, Kathryn O'Brien, had arranged. The full capital balance of £165,000 is still outstanding.

40 12. From the start running the Boathouse Inn was very stressful. The trade was seasonal, because visitors only came to Saltaire when the weather was fine. This made gauging staff numbers a constant problem. Cash flow had to be watched carefully as the business veered from being either dead or too busy for him to cope. He ran the 'front of house' and as a result did not pay enough attention to the back office operation, which he had let slip. He appreciated that behind the scenes matters could

not be ignored and he engaged Andrew Craven, a customer, to deal with his VAT returns. He had paid Mr Craven £200 for the work he did, which had produced figures not dissimilar from the assessments raised by HMRC. He subsequently discovered that Mr Craven was not competent to prepare the returns.

5 13. Whilst he was struggling with the Boathouse Inn, his parents became unwell. In
September/October 2010 his father had a heart attack and in December was diagnosed
with cancer. In October /November 2010 his mother had a fourth hernia operation,
which was less than successful and she was in constant pain. Mr Bhatt said that both
10 parents expected him to look after them. He took his father to the hospital and kept a
check on his mother. Mr Bhatt was also being constantly criticised by the family, not
least because of the break-up of the business he had worked in with his brother.

14. Mr Bhatt produced to the Tribunal details of his treatment at the Westcliffe
Medical Practice. He appears to have been attending the Bradford North Primary Care
Mental Health Team, which provided 6 training sessions, to assist with his anxiety. It
15 is unclear when he first started to go to the sessions but the records provided indicated
that he entered into the Primary Care on 1 April 2011. He has produced his records
with the primary Care unit which show that he was suffering from continuing stress
beyond March 2014. We are satisfied from these records that Mr Bhatt was suffering
from a diagnosed stress condition from April 2011, which must have commenced
20 some time before that date arising from his business and family commitments.

15. In addition to his restaurant business, it appears that he had purchased the
Queen's Head Pub in Bingley, which he sold. In his VAT return for May 2011 he
claimed a refund of £42,106.20. As a result, HMRC had visited and discovered that he
had been paying his earlier VAT against assessments raised by HMRC and not arising
25 from correct returns. He believed the assessments were about right. Mr Bhatt had not
made any enquiries as to Mr Craven's competence which, with hindsight, he
regretted.

16. He next met Ms White, the officer from HMRC dealing with his matters, on 5
August 2011 when she went through his records. He accepted that there had been
30 underpayments, but he had been surprised at the level of the default because he
thought the business was operating at the assessments level. He had fully co-operated
with HMRC and had instructed his accountants, Bostocks, Boyce Welch, to prepare
accounts and the VAT schedule. The schedule revealed that £69,541.30 Vat was
outstanding.

35 17. Mr Bhatt had wanted to agree a time to pay arrangement with HMRC, but it had
been unwilling to agree and he had had to borrow the money from family members. It
was at this point that he went to see his doctor and was advised that he was suffering
from stress. The business is now being run by his partner Kathryn O'Brien. He
accepted that he had made a mistake with regard to his VAT returns, but that his
40 actions had not been deliberate and had arisen as a result of the pressure that he was
under.

18. Kathryn O'Brian, his partner, gave evidence under oath, which substantiated the deterioration in his health. She had not been involved in running the business, but she had realised that there were problems as he had indicated that the stock reports suggested that some of the staff were stealing. It was at about that time that she
5 noticed that Mr Bhatt was not sleeping well and that he had stopped engaging with his family. She believed that he had not intentionally understated his tax liability.

19. Ms Josephine White (Ms White), a retired officer, gave evidence and affirmed. She confirmed that she had originally visited Mr Bhatt at the Boathouse Inn to verify his repayment claim for the quarter ended 31 May 2011. She indicated that she had met
10 Mr Bhatt previously when he had been working with his parents at the Cartwright Inn. She had not been able to give any substantial details of the visit and we have therefore not taken any notice of her comments in that regard. She had, however, compared the VAT returns with Mr Bhatt's self-assessment and PAYE returns. These revealed that the business was operating on a much larger scale than that declared on the VAT
15 returns.

20. On her third visit to the business, Mr Bhatt gave her a copy of annual accounts and amended VAT figures. The trading and profit and loss account for the period 12 August 2009 to 28 February 2011 reveals sales of £1,260,860, wages of £313,792, a net profit of £166,646, and cash at bank of £50,840. In cross-examination Mr Bhatt
20 had accepted that he had been drawing £3,486 each week for wages and some £2000 for his drawings. He had also accepted that he had been stock taking as he had been concerned that some of his staff were stealing from him and he accepted that he had needed to keep a tight control on his inventory.

25

21. Ms White produced a table to the Tribunal which reveals in part the average weekly and daily takings from the VAT return against the actual amounts as follows:

VAT Period		Average weekly Gross takings	Divided by days	Average daily gross takings
11/09	Original	1,454	7	207
	Amended	16,023	7	2,289
02/10	Original	1,346	7	192
	Amended	13,762	7	1,966

05/10	Original	1,469	7	209
	Amended	19,194	7	2,742
08/10	Original	1,930	7	275
	Amended	23,000	7	3,285
11/10	Original	2,389	7	341
	Amended	16,875	7	2,410
02/11	Original	VAT rate	changed	
	Amended	13,722	7	1,960
05/11	Original	2,588	7	369
		19,603	7	2,800

- 5 22. Ms White also produced a schedule of the VAT as originally filed and the amended figures as under:

Period	Original Net VAT	Actual VAT due
11/09	1,161.55	(7,013.81)
02/10	1,626.11	9,361.40
05/10	1,922.72	22,667.93
08/10	2,541.42	26,122.44
11/10	3,161.31	15,718.46
02/11	3,981.04	12,704.38
05/11	(42,106.20)	(21,420.36)

It will be noted that the repayment for the period 05/11 was substantially less than the amount originally claimed. Also, that the VAT originally returned increases each quarter when in fact the liability fell in 11/10 and 02/11. The potential lost revenues for the periods was £94,043. We were surprised to learn at the hearing that Mr Craven had prepared the first three returns to 05/10, but Mr Bhatt appeared unable to say who had prepared the rest. In any event, he signed all of them.

23. Ms White wrote to Mr Bhatt on 29 February 2012 explaining how the penalty had been assessed and confirmed her view that Mr Bhatt's behaviour was deliberate on the following basis:

- 10 a. That Mr Bhatt must have known that the VAT returns he signed and rendered were incorrect.
- b. He was an experienced businessman, who had run similar businesses before, and
- 15 c. Because he evidently had the correct information for his business's performance available to him at the time he made the VAT returns (eg the till readings and purchase invoices and/or delivery notes) and
- d. He must have shown this information to the stock-taker, who had produced regular reports from it that reflected the true performance of the business.
- 20 e. The disclosure was 'prompted' as Mr Bhatt had not advised HMRC that his returns were incorrect until the first meeting when he had requested a repayment.

24. She had calculated the penalty on the following basis:

For a deliberate inaccuracy the penalty range is from 35% to 70%

25 As a result of the disclosures she had made the following percentage reductions:

Telling	10%
Helping	40%
<u>Giving access</u>	<u>30%</u>
Total reduction	80%

30 The difference between the minimum and maximum percentage is 35% (70% - 35%). 80% of 35% is 28%.

She then deducted the percentage reduction from the maximum penalty

70% - 28% = 42% and she applied that figure to the potential lost revenue

of £94043 which gave rise to a penalty of £39,498.06.

The submissions

25. Mrs Sinclair submitted that Mr Bhatt had been paying the assessments up to the visit arising from his application for a repayment. As could be seen from the figures provided by Ms White, the actual liability on a weekly basis was substantially higher than the returns showed. Mr Bhatt was regularly arranging for a stock take, which was based on figures provided by him at the time. Those figures must have alerted him to the fact that the VAT returns he was signing were incorrect.

26. The annual accounts produced for the first 18 months reveal that the business was performing very well. Mr Bhatt was taking substantial drawings from the business and paying substantial salaries. He has explained that cash was tight and he needed to watch it carefully. His VAT liability would have a substantial effect on his cash flow. The figures which had been submitted for VAT purposes showed a gradual growth over the period.

27. HMRC had considered whether there were any special circumstances and could not agree that there were. Ms White was correct in deciding that Mr Bhatt had been deliberate in withholding the true VAT position and the penalty should be confirmed.

28. Mr Broadbent submitted that Mr Bhatt had never given a proper explanation as to the reasons for his failure to check the VAT returns properly. He had told Ms White in November 2011 that he was very disorganised and that he had understood that Mr Craven was competent to deal with his VAT. It was not unreasonable for Mr Bhatt to have relied on Mr Craven. He also paid Mr Craven £200 for his trouble. The errors came to light when Mr Bhatt claimed a repayment. It is unlikely that an individual who was deliberately understating his VAT liability, would ask for a repayment and risk his dishonesty coming to light.

29. From the evidence before the Tribunal, it was clear that Mr Bhatt was under considerable business and family pressure. This ultimately led to him having medical attention. It was only when his partner, Mrs O'Brian, took over the administration of the business that matters improved. The fact that the business was badly managed does not mean that Mr Bhatt was dishonest. The Tribunal should not find that Mr Bhatt's behaviour was deliberate. They can find that his actions were careless when considering the cumulative pressure he was under at the time. Mr Broadbent submitted, however, that the Tribunal should remove the penalty in its entirety.

30. If the Tribunal was not minded to remove the entire penalty he considered that the pressure that Mr Bhatt was under amounted to a special circumstance which would allow the Tribunal to mitigate the penalty. If the Tribunal was of the opinion that the penalty had been correctly calculated they should consider suspending it in light of Mr Bhatt's clear medical state. A stay would mean that these facts could be brought into account if Mr Bhatt was in error again.

The decision

31. We have considered the law and the evidence and we have decided that Mr Bhatt was careless with regard to his VAT returns. We accept that he was under considerable pressure and that he relied on Mr Craven to complete the VAT returns. He was fundamentally involved in the day to day running of the business and delegated the completion of the VAT returns so that he could concentrate on the business as a whole. He signed the VAT returns without giving them any attention assuming that the figures were correct. We accept that he was running a very successful business, but that he appears not to have been aware as to the extent of the business until the accounts were struck. We are unable to reconcile his application for a repayment of his VAT with a deliberate intention on his part to act dishonestly. If he had deliberately understated his VAT he would have known that the amount he had avoided was substantially greater than the amount he was claiming by way of repayment. In those circumstances we do not believe he would not have brought HMRC's attention to the failure.

32. We do not accept that there were special circumstances. Special circumstances have to be something more than would give rise to a reasonable excuse. There is nothing special, in that sense, in Mr Bhatt's medical condition. We therefore reduce the penalty to be based on carelessness and not deliberate behaviour. We note that the penalty for careless action is 30%. The difference between the maximum of 30% and minimum of 15% is 7.5%. Applying the disclosure reduction of 80% to that percentage gives a percentage penalty of 6%. Deducting that figure from the maximum that could be charged produces a percentage of 24%. (30% - 6%) The potential tax loss was £94,043 and 24% of that figure is £22,570.32 and we reduce the penalty to that amount.

33. We do not agree that that penalty should be suspended. We do not think that HMRC's decision not to suspend the penalty was flawed. We have been referred to the case of *Astoria Properties Ltd; Churchill*. In that case the company secretary decided not to disclose the VAT position on the sale of a property in spite of the fact that he had been advised to do so. Mr Bhatt was oblivious to the fact that the VAT returns were incorrect as he had relied on somebody else to deal with them for him. That was undoubtedly careless, but not in our view deliberate.

34. 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.

DAVID S PORTER
TRIBUNAL JUDGE

RELEASE DATE: 9 May 2014