



**TC04216**

**Appeal number: TC/2012/04556**

*Income tax - inaccuracies in tax returns over a period of eight years - overstated travelling and subsistence expenses - whether Revenue Amendments correct - yes - Penalty assessment - whether errors in returns were careless - yes - Appeal dismissed – penalties confirmed*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**KLS ELECTRICAL CONTRACTING**

**Appellant**

**- and -**

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

**TRIBUNAL:    JUDGE MICHAEL S CONNELL  
                  MR ROBERT ACKROYD**

**Sitting in public at City Exchange 11 Albion Street Leeds on 11 September 2014**

**Lynda Smith and Sarah Smith for the Appellant**

**Nadine Newham Officer of HM Revenue and Customs for the Respondents**

## DECISION

### The Appeal

1. This is an appeal by KLS Electrical Contracting (a partnership) (“the Appellant”) against partnership discovery amendments for 2000-01 to 2003-04 raised under s 29 Taxes Management Act (TMA) 1970; enquiry closure notices for 2004-05 to 2007-08 raised under s 28B(1) & (2) TMA 1970 and penalties under s 95A TMA 1970.

### Points at Issue

2. The points at issue are:
- i. Whether the partnership has overstated expenses for the years 2000-01 to 2007- 08 and if so by how much.
  - ii. Whether HMRC are correct in finding that Mrs Smith (as nominated partner) or her agent, was careless with regard to her record keeping.
  - iii. Whether the penalties imposed by HMRC are correct and appropriate

### Evidence

3. The documentary evidence consisted of five bundles prepared by HMRC, containing copy ‘Bank Day Books’ (which included an analysis of business expenditure); Nat West credit card statements, copy partnership returns, copy notes of meetings with the Appellant and the exchange of correspondence between the Appellant, her agents and HMRC during the enquiry period and copy invoices said by the Appellant not to have been claimed as business expenses.

### Background

4. Mr Keith and Mrs Lynda Smith are in partnership trading as KLS Electrical Contracting in Selby and Goole, North Humberside. The business has operated for over 20 years offering electrical services to domestic, commercial and industrial customers.

5. On 5 January 2007 an enquiry was opened into the Appellant’s 2005 partnership return in respect of the accounts for the year ended 30 April 2004. During the enquiry HMRC say that the following inaccuracies were found:

- i. Excessive Travelling and Subsistence claims.
- ii. Incorrect adjustments had been made for debtors leading to an increase in profits in the year ended 30 April 2004 of £12,766 and a corresponding decrease in profits in the year ended 30 April 2005 of £3,926.

iii. Omitted turnover was found in the year ended 30 April 2004 of £745 for 'Johnson' and £169 for 'Yorkshire Diesel'.

iv. Motor expenses on a Porsche amounting to £3,233 were not allowable in the year ended 30 April 2004, as the vehicle was not used in the trade.

5 6. Points ii) to iv) inclusive above have been agreed. The only point of disagreement on the amendments and Closure Notices issued, relates to item i), that is, the quantum of expenses for travelling and subsistence to be allowed in each year.

7. HMRC say that the travelling and subsistence claims of the Appellant were initially noted as over-claimed in 2004-05, and later found to have been over-claimed  
10 in all accounts years from 2000-01 to 2007-08 inclusive. The figures submitted in accounts were derived from personal credit card balances which the Appellant's agent erroneously claimed as travel and subsistence.

8. The enquiry Inspector initially allowed an estimated £2,000 as travel expenditure in 2004-05. HMRC later agreed that an amount based more on available  
15 evidence should be used and proposed that for 2004-05 a figure of £4,684 should be allowed instead.

9. The £4,684 for 2004-05 was made up of the £3,455.42 employee travel and a subsistence figure suggested by the Appellant's agent in respect of staff costs added to a £1,228.94 expenses figure provided by the agent, on the basis that, that amount of  
20 expenditure had remained unclaimed in each accounts year. HMRC then scaled this amount backwards and forwards to other years using the RPI.

10. HMRC's proposed allowable proportion of travelling expenses was as follows:

	2000/01	2001/02	2002/03	2003/04
Travelling Expenses claimed	32,813	29,312	26,399	24,307
Travelling Expenses proposed	4,291	4,366	4,431	4,572
Net adjustment	28,522	24,946	21,968	19,735
	2004/05	2005/06	2006/07	2007/08
Travelling Expenses claimed	30,206	28,770	37,321	37,158
Travelling Expenses proposed	4,684	4,832	4,956	5,181
Net adjustment	25,522	23,938	32,365	31,977

11. HMRC's Revenue Amendments to the Appellant's partnership profits are set  
25 out below:

Year	Decision	Further Profits
2000-01	Discovery Amendment	£ 28,522
2001-02	Discovery Amendment	£ 24,946
2002-03	Discovery Amendment	£ 21,968
2003-04	Discovery Amendment	£ 19,735

2004-05	Closure Notice	£ 42,435
2005-06	Closure Notice	£ 20,012
2006-07	Closure Notice	£ 32,365
2007-08	Closure Notice	£ 31,977

12. The revised tax liabilities and penalties relating to Mrs. Smith's share of the revised additions were as follows:

Year	Tax Difference	Class 4 NIC difference	Total	Penalty (35%)
2000/01	£3,137.33	£990.43	£4,127.76	£1,445
2001/02	£2,744.06	£873.11	£3,617.17	£1,266
2002/03	£2,413.79	£768.88	£3,182.67	£1,114
2003/04	£2,170.33	£789.36	£2,959.69	£1,036
2004/05	£4,667.80	£1,697.44	£6,365.24	£2,228
2005/06	£2,201.32	£675.11	£2,876.43	£1,006
2006/07	£3,559.85	£1036.19	£4,596.04	£1,608
2007/08	£4,896.36	£691.82	£5,588.18	£1,956
			£33,313.18	£11,659

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13. HMRC determined that the partners were negligent in the completion of the Appellant's partnership tax returns due to the inaccuracies on their partnership accounts and are therefore liable to a penalty under the provisions of s 95 Taxes Management Act 1970 on the partners' tax and Class 4 NIC, arising out of the partnership's further profits. HMRC also concluded that a penalty loading at 35% was reasonable.

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14. The Appellant appealed HMRC's decisions, saying that the proposed adjustments for business use and travelling expenses were too low and should be increased, and that the 35% penalty charged was excessive.

15 HMRC's case

15. HMRC examined the agent's breakdown and analysis of the Appellant's expenses for the year ended 30 April 2004. Under a column headed Travel & Subsistence, the figures inserted were identical to Mr and Mrs Smith's NatWest credit card balances for the same periods and the majority of expenses were for cash withdrawals, QVC ( a home shopping channel) and BID-UP TV, a satellite television and internet auction channel.

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16. At a meeting with HMRC Mrs Smith stated that some of the shopping channel purchases were business, such as batteries, torches and uniforms, whilst others were private. No invoices were produced in respect of QVC purchases but Mrs Smith produced a list of items purchased. HMRC did not accept that the items on the list represented business expenditure. The expenses could have been private and without receipts there was no evidence that the amounts and descriptions noted on the list were correct.

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17. Mrs Smith told the Inspector that she drew cash on her credit card to give to her employees for travelling and subsistence and other general expenses. However these deductions were not identified separately in the accounts.

5 18. The Appellant's agent provided HMRC with invoices that Mrs Smith claimed had not been put through the records, but paid by credit card by Mr and Mrs Smith. However many of the invoices had a reference number on them, and it was clear had already been included in the records prepared by Mrs Smith. It was put to the agent during the meeting that the invoices provided had already been included and that they had been produced to try and justify the expenses claimed.

10 19. At the time that Mrs Smith asked for HMRC's decision to be reviewed she also asked a newly appointed agent Gilbert Tax, to assist her, and having looked at the prime documentation prepared by Mrs Smith for the period to 30 April 2007 Gilbert Tax wrote to HMRC on 25 November 2010, to explain that although Mrs Smith put credit card payments in her day book under the sundry and subs column, the previous  
15 agent had taken it upon herself to attribute these payments to travel and subsistence. They said that when the accounts and returns were prepared each year, Mrs Smith just signed her tax returns and paid the tax that she was told to pay.

20 20. HMRC contend that Mrs Smith has to take responsibility in respect of the completion of the partnership tax return and ensure that the figures produced on the tax return are correct. Mrs Smith believes that the amounts claimed in the partnership  
20 accounts in respect of travel and subsistence cover items that do not appear in the accounts because they have been missed out by the agent. HMRC contend that this is not correct. It would have been quite obvious that the amount claimed for travel and subsistence was excessive and that should have prompted her to ask her agent how  
25 she had calculated the amount. Mr and Mrs Smith have been in business for many years and would have been aware that the figures claimed in respect of travel and subsistence were inaccurate. At the very least, they should have met the agent to establish how the figures for travel and subsistence in the accounts had been calculated.

30 21. Mrs Smith at one stage admitted that the reason some business expenses had not been claimed was to account for the private credit card purchases included as business expenses. However, sufficient evidence has not been produced to show that the amounts claimed related to business expenses that the partners had paid for out of their own money and allege not to have gone through the business accounts.

35 22. HMRC note that the partnership's agent completed the incorrect accounts for each year without allegedly consulting the partners on the travelling and subsistence figure she was including. It is also noted that Mrs Smith has been in ill health since 2002. However this does not mean that the partners do not have to satisfy their tax obligations. The incorrect travelling and subsistence debits in the partnership accounts  
40 are large, and the errors spread over eight years, but neither of the partners queried any of these returns with their agent before signing prior to submission to HMRC. As such penalties are due from each of the partners.

23. The onus is on the Appellants to prove that the amounts assessed as additional profits are incorrect.

24. In respect of a penalty determination HMRC has charged penalties on each of the partners under s 95A TMA 1970 for having delivered incorrect partnership returns due to neglect in ensuring that the entries on the returns were correct.

25. The penalty under s 95A TMA 1970 can be as much as 100% of the further duties payable but has been abated by 15% (out of 20%) for disclosure, 30% (out of 40%) for cooperation and 20% (out of 40%) for seriousness, by HMRC leading to a penalty loading of 35%. Despite Mrs Smith's ill health the partners should have been aware at some point over the eight years that incorrect accounts were submitted and that large erroneous claims were being made.

26. HMRC therefore contend that the penalty of 35% is fair and should be confirmed pursuant to s 100B (2)(b) (ii) TMA 1970.

#### The Appellant's case

27. In the Notice of Appeal, Mrs Smith says that HMRC, in estimating the business's travel and subsistence expenditure are just 'guessing.' She says that penalty charges of 35% are "rather high". She had provided everything asked for. She also says that the unusual circumstances of the case have not been taken into account, being that both partners have suffered "life-threatening illnesses, Mr Keith Smith having suffered from prostate cancer and Mrs Smith having suffered a massive brain haemorrhage".

28. At the hearing Mrs Smith said she accepted that her first agent, who prepared the accounts under appeal, had make mistakes. She said that she had been very ill at the time of the enquiry, but had nonetheless co-operated fully and had never tried to hide errors. She had not been aware of the seriousness of the mistakes made by the agent.

29. Although the figures for travel and subsistence were wrong, HMRC has underestimated the expenditure.

#### Relevant legislation

31. Paragraph 1 of Schedule 24 states in relevant part as follows:

(1) A penalty is payable by a person (P) where-

(a) P gives HMRC a document of a kind listed in the Table below,  
and

(b) Conditions 1 and 2 are satisfied.

(2) Condition 1 is that the document contains an inaccuracy which amounts to, or leads to-

(a) an understatement of a liability to tax,

- (b) a false or inflated statement of a loss, or
- (c) a false or inflated claim to repayment of tax.
- (3) Condition 2 is that the inaccuracy was careless (within the meaning of paragraph 3) or deliberate on P's part.
- (4) Where a document contains more than one inaccuracy, a penalty is payable for each inaccuracy.

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<i>Tax</i>	<i>Document</i>
Income tax or capital gains tax .....	Return under section 8 of TMA 1970 (personal return). .....

32. Paragraph 3 of Schedule 24 provides for degrees of culpability as follows:

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(1) For the purposes of a penalty under paragraph 1, inaccuracy in a document given by P to HMRC is-

(a) "careless" if the inaccuracy is due to failure by P to take reasonable care,

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(b) "deliberate but not concealed" if the inaccuracy is deliberate on P's part but P does not make arrangements to conceal it, and

(c) "deliberate and concealed" if the inaccuracy is deliberate on P's part and P makes arrangements to conceal it (for example, by submitting false evidence in support of an inaccurate figure).

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(2) An inaccuracy in a document given by P to HMRC, which was neither careless nor deliberate on P's part when the document was given, is to be treated as careless if P--

(a) discovered the inaccuracy at some later time, and

(b) did not take reasonable steps to inform HMRC.

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33. Paragraph 4 sets out the penalty payable under paragraph 1. Paragraph 4(1)(a) provides that the penalty, for careless action, is 30% of the potential lost revenue. For deliberate but not concealed action, the penalty is 70% of the potential lost revenue, and for deliberate and concealed action, the penalty is 100% of the potential lost revenue.

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34. Paragraph 5 defines "potential lost revenue" as "the additional amount due or payable in respect of tax as a result of correcting the inaccuracy or assessment".

35. Paragraph 9 provides for reductions in the penalty for disclosure depending on whether it is prompted or unprompted.

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36. Paragraph 10(1) provides that "Where a person who would otherwise be liable to a 30% penalty has made an unprompted disclosure, HMRC shall reduce the 30%

penalty to a percentage (which may be 0%) which reflects the quality of the disclosure”. Paragraph 10(2) provides that “Where a person who would otherwise be liable to a 30% penalty has made a prompted disclosure, HMRC shall reduce the 30% penalty to a percentage, not below 15%, which reflects the quality of the disclosure”.

5 37. Paragraph 11 further provides that HMRC may reduce the penalty under paragraph 1 “If they think it right because of special circumstances”.

38. Paragraph 14 also enables HMRC to suspend all or part of a penalty for a careless inaccuracy under paragraph 1, but (under paragraph 14(3)) “only if compliance with a condition of suspension would help P to avoid becoming liable to  
10 further penalties under paragraph 1 for careless inaccuracy”.

39. Under paragraph 15, a person may appeal against a decision of HMRC that a penalty is payable (sub paragraph (1)), or as to the amount of a penalty payable, (subparagraph (2)) or a decision not to suspend a penalty payable, (subparagraph (3)) or a decision as to the conditions of suspension (subparagraph (4)).

15 40. Paragraph 17 deals with the powers of the Tribunal in any such appeal.  
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(1) On an appeal under paragraph 15(1) the appellate tribunal may affirm or cancel HMRC’s decision.

(2) On an appeal under paragraph 15(2) the appellate tribunal may

20 (a) affirm HMRC’s decision, or

(b) substitute for HMRC’s decision another decision that HMRC had power to make.

(3) If the appellate tribunal substitutes its decision for HMRC’s, the appellate tribunal may rely on paragraph 11

25 (a) to the same extent as HMRC (which may mean applying the same percentage reduction as HMRC to a different starting point), or

(b) to a different extent, but only if the appellate tribunal thinks that HMRC’s decision in respect of the application of paragraph 11 was flawed.

30 (4) On an appeal under paragraph 15(3)

(a) the appellate tribunal may order HMRC to suspend the penalty only if it thinks that HMRC’s decision not to suspend was flawed, and

(b) if the appellate tribunal orders HMRC to suspend the penalty

35 (i) P may appeal to the appellate tribunal against a provision of the notice of suspension, and

(ii) the appellate tribunal may order HMRC to amend the notice.

(5) On an appeal under paragraph 15(4) the appellate tribunal

(a) may affirm the conditions of suspension, or

40 (b) may vary the conditions of suspension, but only if the appellate tribunal thinks that HMRC’s decision in respect of the conditions was flawed.

(6) In sub-paragraphs (3)(b), (4)(a) and (5)(b) flawed means flawed when considered in the light of the principles applicable in proceedings for judicial review.

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(7) Paragraph 14 (see in particular paragraph 14(3)) is subject to the possibility of an order under this paragraph.'

### Conclusion

10 41. The issues for the Tribunal to decide are whether the partnership has overstated expenses for the years 2000-01 to 2007-08, whether Mrs Smith (as nominated partner) was careless with regard to her record keeping and whether the penalties imposed by HMRC are correct and appropriate.

15 42. It is clear to us that insufficient care was taken when the Appellant's accounts/returns were prepared. This led to the travelling expenses and other items of business expenditure being incorrect. During the enquiry, Mrs Smith said that the reason some business expenses had not been claimed was to account for the private credit card purchases included as business expenses. Clearly she knew that was wrong.

20 43. The onus of proof is on the Appellant to show by satisfactory evidence that the amounts assessed as additional profits by HMRC are incorrect. HMRC have calculated what they consider, on the evidence and after a long and detailed enquiry, to be a fair assessment of the Appellant's travel and subsistence expenditure in the years under appeal. Estimates are necessarily to best judgement on the information available to them. In the absence of any documentary records being produced by the Appellant it is not possible for HMRC to make an objectively accurate assessment.  
25 HMRC's assessment is prima facie correct until shown to be wrong. A taxpayer must show not only negatively that an assessment is wrong but also positively what correction should be made to make it right or more nearly right. However, the Appellant has not produced any evidence to discharge the burden of proof upon her to show that HMRC's figures, on a balance of probabilities, are or may be incorrect.

30 44. We therefore find that the declared sales figure/profits, in respect of the years under appeal, were incorrect and should be adjusted in accordance with the figures set out in paragraph 10 above.

35 45. Further we find that the Appellant should have known that the tax assessed on submission of the partnership's returns was incorrect. Mrs Smith failed to take reasonable care in submission of the returns and was therefore careless.

40 46. The penalty has been assessed as 35% of the underpaid tax, which is within the penalty range for careless behaviour after allowing for seriousness and reductions for quality of cooperation and disclosure. The penalty has been assessed entirely in line with the legislation and is proportionate to the inaccuracies that occurred, in this case over many years. In the Tribunal's view there are no special circumstances which would justify a reduction in the penalty.

47. The Revenue amendments as referred to in paragraphs 10 and 11 above are accordingly confirmed and the appeal dismissed.

48. 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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**MICHAEL S CONNELL**  
**TRIBUNAL JUDGE**

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**RELEASE DATE: 6 January 2015**