[2019] UKFTT 615 (TC)

**TC07399**

**Appeal number: TC/2016/05661**

***VAT-best judgment assessments-supply of labour or outsourced payroll services - held labour – appeal against assessments dismissed – penalties for inaccurate returns - careless or deliberate - held careless – appeal against penalty assessment allowed in part.***

**FIRST-TIER TRIBUNAL**
**TAX CHAMBER**

**IN TANDEM RESOURCES LTD** **Appellant**

**- and -**

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

**TRIBUNAL: JUDGE NIGEL POPPLEWELL**
**MR MARK BUFFERY**

**Sitting in public in London on 14 May 2018 and 8 February 2019 with further written submissions by both parties received on 14 August 2019**

**Mr Roger Purkiss, director of the Appellant, for the Appellant**

**Mr Keith Golder, litigator of the Respondents' Solicitor's Office, for the Respondents**

DECISION

## Introduction

1. This is a VAT case which concerns assessments (the "**assessments**") for underpaid VAT (both underpaid output tax and over recovered input tax) and penalties for inaccuracies in VAT returns.

2. The central issue is whether the appellant (the "**Company**" or "**In Tandem**") supplied labour to its customers as the respondents (or "**HMRC**") contend, or outsourced administration services (as the Company contends).

3. The amounts in question are large. The specific amounts assessed which were the subject matter of the original appeal are for VAT of £9,199,978 (over recovered input tax of £4,140,589 and under declared output tax of £5,059,396) together with interest of £446,172.09. These relate to tax returns for the period 27 June 2012 to 29 November 2016. But further assessments have been made since the appeal (the one of which we are aware is dated 8 March 2017 and is for £2,262,356 of VAT). There is also interest on that of £412,186.16. We are told there are others. The parties agree that this decision and the reasons for it will apply equally to any other assessments for VAT and interest which have been visited on the appellant.

4. The same goes for penalties. The appellant has been assessed to a penalty of £6,278,989.85 for deliberate inaccuracies in its VAT returns. HMRC now accept that that amount is overstated and should be £4,157,139.55.

5. We were told that the total amount of VAT interest and penalties which might be affected by this decision is more than £20 million.

6. Furthermore, it is HMRC's intention (in their pleadings they say they have already done this but that turns out not to be the case) to make Mr Purkiss personally liable to pay the penalties under paragraph 19 of schedule 24 of the Finance Act 2007 ("**Schedule 24**").

7. So there are five issues before us:

(1) What was the nature of the supplies which were made by In Tandem to its customers?

(2) Which is the VATable consideration for those supplies?

(3) Were the assessments made to HMRC's best judgment?

(4) Did the assessments overcharge the appellant and if so, what is the amount of that overcharge?

(5) If the supplies were of labour and so the relevant VAT returns were inaccurate, were those inaccuracies deliberate, careless or just simple errors?

8. For the reasons given later in this decision we have come to the conclusion that:

(1) The Company supplied labour to its customers.

(2) The VATable consideration included the wages paid by the customers to the employees

(3) The assessments were made to best judgment;

(4) The assessments do not overcharge the appellant.

(5) The inaccuracies in the returns were a result of careless and not deliberate behaviour on the part of the Company.

9. Finally, the Company has accepted that the assessments are accurate insofar as they relate to any over recovered input tax. So it accepts that, subject to the assessments being made to best judgment, it is liable to pay those elements of the assessments which relate to over recovered input tax. However the Company maintains its position regarding penalties and says that the over recovered input tax was a result of careless and not deliberate behaviour.

## The evidence and certain findings of fact

10. We were provided with bundles of documents. Mr Purkiss gave oral evidence at the February 2019 hearing on which he was cross examined by Mr Golder. Oral evidence was given for HMRC by Officer Suzanne Roberts of HMRC's Fraud Investigation Unit. The evidence can be conveniently broken down into two parts: that relating to the supplies made by In Tandem; and that relating to the penalties.

*The supplies made by In Tandem*

11. Although we set out the relevant law in more detail later in this decision, it is worth saying now that one of the crucial aspects of these type of cases concerns the contractual relationship between the relevant parties (in this case between In Tandem and its customers). Prior to the hearing in February 2019 we were provided with 12 such contracts (the "**contracts**") entered into by the appellant and various of its customers between September 2012 and September 2015. These contracts are in identical form save as to the parties and the dates. At the hearing in February 2019 Mr Purkiss gave evidence about these contracts. We found him to be an honest and reliable witness. He recognised that the strategy which the Company had adopted (detailed below) may have had unforeseen and unfortunate VAT consequences, but he accepted that might be the case. He did not try, in our view, to tailor his evidence to better his case.

12. From this evidence we find the following as facts:

(1) The Company was incorporated and registered for VAT in June 2012. It described its intended business activities as the provision of staff.

(2) In Tandem was the brainchild of Mr Purkiss. It was he who conceived its business model. However the accounting package used by the Company was designed by John Davies ("**Mr Davies**") a former associate of Mr Purkiss. The accounting package was cloud-based with support provided from the USA where Mr Purkiss lived, and from India.

(3) Mr Purkiss had spotted that larger companies (i.e. those with significant (in the thousands) number of employees) were far better placed to obtain benefits for its employees at a lower cost than employers with fewer employees. He thought that if he could aggregate employees from a number of employers under the In Tandem banner, In Tandem could then obtain these benefits for those employees at a lower cost. The savings could be passed back to the participating employers. In Tandem would charge a fee to those employers but even then, the employers would make a saving compared with the costs that they would have incurred in supplying those benefits to their employees without the benefits of the reduced price facilitated by the involvement of In Tandem.

(4) The main benefits which could be provided at this lower cost included pensions, well-being platforms and shopping discount vouchers.

(5) However the pension and benefit packages relied on In Tandem having employees on its books. This could be checked by the provider via the real time information ("**RTI**") system.

(6) And so, in order to demonstrate that it had sufficient employees on its books, the appellant needed to actually employ the relevant employees. However, self-evidently, those employees had to continue to carry on providing their labour to their original employer.

(7) Having come up with the idea, Mr Davies and another associate of Mr Purkiss, Chris Pearson (who had contacts in the automotive and coach industries) approached those contacts and managed to get 12 to 15 employers (most if not all of whom then became customers) together to participate. In total, this meant that In Tandem had between 1200 and 1500 employees on its books and could therefore approach service providers for reduced cost benefits.

(8) So what essentially happened was that the employees were transferred by the participating employers to In Tandem and then supplied back to the relevant employer. In practical terms the employee would have seen no practical difference to the way in which they were treated after they had been transferred to In Tandem, save that they had the benefit of the fringe benefits which they hadn't had before.

(9) It is now convenient to look at one of the contracts. We put the contract between In Tandem and its customer Mike de Courcey Travel Ltd dated 1 November 2013 to Mr Purkiss. What we now set out are terms of that contract together with Mr Purkiss's comments on those contractual terms. Mr Purkiss had explained that he thought the source of each of these contracts was the Internet.

He thought that Mr Davies would have downloaded a pro forma contract, made certain changes to it, and then used it as the basis for the contracts between In Tandem and its customers. He thought that Mr Davies had taken no legal advice on the terms of the contract, and he, Mr Purkiss, certainly hadn't.

(10) The contract describes In Tandem as the Service Provider, and Mike de Courcey Travel Ltd as the Client.

(11) The recitals to the contract provide as follows:

> "WHEREAS
>
> (1) The Service Provider is in the business of providing services in relation to the outsourcing of employees.
>
> (2) The Client wishes to engage the Service Provider to provide the Services described in Schedule 2 to this Agreement.
>
> (3) The Service Provider has agreed to accept the engagement, subject to the terms and conditions of this Agreement.
>
> (4) To that effect it is the intention of both The Service Provider and The Client that this document constitutes a joint venture between them the purposes of such joint venture being to enable the Client to better perform its business activities. To that end it has been agreed that the Service Provider will assume responsibility for the statutory employment and remuneration and provision of employment associated benefits of the Clients employees, whilst at the same time recognising that the management and control of those employees will remain under the total control of The Client. For those purposes The Client will act as agent of The Service Provider insofar as, but only insofar as, this is legally required by the terms of TUPE or any other relevant regulations."

(12) Mr Purkiss had the following comments on these provisions. In recital (1) the services were the provision of payroll services and benefits for the customers and staff. In recital (3) it was more correct to say that the Client wanted to participate in the scheme to garner the benefits of the economies of scale for the benefit of its employees. In recital (4) this was a joint venture, but although In Tandem became the employer of the employees, the Client remained responsible for managing the staff and making sure that they were paid. It was correct to say that In Tandem would assume responsibility for the statutory employment and remuneration and provision of employment associated benefits. And that nothing really had changed after the transfer of the employees other than the master/servant relationship.

(13) Clause 1 of the contract is entitled "**TRANSFER OF EMPLOYEES**". It then goes on to provide as follows:

> "1.1 The parties believe that the commencement of the Services on 8

November 2013 (the "Commencement Date") by the Service Provider shall constitute a relevant transfer for the purposes of the Transfer of Undertakings (Protection of Employment) Regulations 2006 ("Transfer Regulations"). As a result on the Commencement Date the contracts of employment of the employees of the Client as identified in Schedule 1 to this Agreement (the "Transferred Staff") shall transferred to the Service Provider.

1.2 The Client and the Service Provider shall use all reasonable endeavours to ensure the smooth transfer of the contracts of employment of the Transferred Staff to the Service Provider and to comply with their respective obligations pursuant to the Transfer Regulations.

1.3 If the Client (acting in its capacity as the Service Providers agent under clause 7.1) recruits any new personnel to be engaged in the provision of the Services, then from the date selected by the Client the Service Provider shall employ such new personnel.

1.4 The expression Transferred Staff relates to any new personnel engaged in the provision of the Services pursuant to clause 1.3. Any person leaving the employment of the Service Provider other than pursuant to clause 10.3 shall from the date of the termination of their employment no longer be Transferred Staff."

(14) Schedule 1 is entitled "Transferred Staff", and then reads "As per attached staff details list". We were not provided with a specific list of Transferred Staff for this contract but two lists were tendered in evidence and it is clear to us that there would have been a list of staff identified with each of these contracts.

(15) Importantly, Schedule 2 is entitled "Services" and reads "Provision of Labour a facilitated by the Transferred Staff"

(16) Clauses 2 and 3 of the contract, which Mr Purkiss confirmed reflects what actually happened in practice set out below.

"2. PAYMENTS TO TRANSFERRED STAFF

2.1 "Payday" means the last Friday of each month for Transferred Staff who are paid monthly and every Friday for Transferred Staff who are paid weekly.

2.2 In the case of Transferred Staff who are paid monthly not less than 14 days prior to Payday each month and in the case of Transferred Staff who are paid weekly not less than (4) days prior to Payday each week the Client will provide to the Service Provider full details of hours worked (and applicable pay rates for such hours) bonuses earned by each member of the Transferred Staff and any other issues which may affect the pay due to any member of the Transferred Staff in respect of the relevant forthcoming Payday. The Service Provider will process the pay and notify the Client of

the net pay of each member of the Transferred Staff and the client will ensure that the Transferred Staff are paid on the relevant Payday according to the Client's normal practice.

2.3 In the case of Transferred Staff who are paid monthly not less than 7 days prior to the relevant Payday each month and in the case of Transferred Staff who are paid weekly not less than (2) days prior to the relevant Payday each week the Service Provider will provide the Client with a statement (the "Statement") in respect of each member of the Transferred Staff who has been in the Service Provider's employment since the date of the previous Statement (or in the case of the first such Statement or in the case of Transferred Staff who have become Transferred Staff since the date of the previous Statement since employment with the Service Provider commenced) setting out in respect of each member of the Transferred Staff the gross pay, deductions for income tax and employees national insurance contributions and the consequent net pay applicable to them in respect of the relevant forthcoming Payday.

3. CLIENT'S PAYMENTS

3.1 No more than [7] days after Payday each week or month (as appropriate), and subject to the Service Provider first having provided an invoice to the Client in respect of the relevant sums, the Client shall pay to the Service Provider by electronic transfer using the bank details provided by the Service Provider from time to time:

3.1.1 a sum equivalent to the total of the Transferred Staff's employees' gross pay + 4% + VAT less the amount paid to staff under Clause 2.2 (The Fee).

3.2 On each Payday the Client shall pay to each member of the Transferred Staff the applicable net pay related to them for the previous month, as set out in the Statement.

3.3 In addition the Client shall pay to the Service Provider within 30 days of receiving the Service Provider's relevant invoice:

3.3.1 the reasonable costs incurred by the Service Provider in complying with any mandatory statutory or common law requirements in respect of the provision of the Services, subject to the Service Provider informing the Client in writing and as soon as is reasonably practicable of the need to incur such costs, and provided for the avoidance of doubt that no costs related to the Transferred Staffs employees' national insurance contributions, employer's national insurance contributions, pension contributions and income tax shall be payable by the Client hereunder; and

3.3.2 the cost of any additional services provided by the Service Provider which have been approved by the Client in writing in

advance, which costs may include but will not be limited to the costs of training of any Transferred Staff, the costs of Transferred Staff obtaining any relevant qualifications, the costs of Transferred Staff obtaining or retaining memberships of any relevant bodies, the costs of staff incentive or employee benefit packages, the provision of pension payments and any associated costs in respect of the Transferred Staff, and the costs of any advertising and recruitment services which the Client may from time to time request from the Service Provider.

3.4 The Service Provider reserves the right to charge interest at the rate of 8% above Lloyds Bank base rate from time to time on any invoiced sums that remain unpaid by the Client from the due date to the date of payment.

3.5 VAT will be applied to The Fee and all other service charges at the prevailing rate set by the government, currently 20%."

(17) In conjunction with the Mike de Courcey contract, there was provided in one of the bundles, a document which is expressed to be the Statement of Main Terms and Conditions of Employment for Brian John Lyons (the "**Statement**"). In that document Mr Lyons main base of work is the Mike de Courcey Travel Coventry Depot, hence the reason for using the Mike de Courcey contract as the exemplar put to Mr Purkiss.

(18) The Statement reads thus:

"This document sets out the main particulars for the Terms and Conditions of your Contract of Employment. Main contractual terms are included at the end of this document.

This is a contract between: In Tandem Resources Limited whose registered address is 500 Avebury Boulevard, Central, Milton Keynes MK9 2BE and:-

| | |
|---|---|
| Name of employee: | Brian John Lyon |
| of: | 21 Westfield Road |
| | Maypole |
| | B14 4PN |
| Date on which employment started: | 11th March 2015 |
| Date on which current contract starts: | 11th March 2015" |

(19) As well as setting out the main base of work for the employee, clause 1 of the Statement goes on to indicate that the employee may also be required on reasonable notice to work from one of "our" other locations. The job title for Mr

Lyons is that of “Coach Driver”, and that he is “Responsible to: Head of Department”; and that his “Responsibilities: See Job Description at Appendix A”.

(20) The Statement runs to some 13 pages. There were two other such statements in the bundle. They are identical save as regards the identity of the employee, the date of commencement and the job title. It is clear that in similar fashion to the contracts between In Tandem and its customers, these statements of terms are a standard form document. We suspect (but we cannot say for certain) that these would be the statement of terms of each of the participating employers. But what is clear is that the day to day management of Mr Lyons is envisaged to be carried out by Mike de Courcey. Booking holiday, absence through sickness, dress code, drugs, alcohol and smoking policies, disciplinary and grievance procedures, are all consistent with this, and the Head of Department (i.e. a member of the customers staff) is the person to whom Mr Lyons reports/is responsible.

(21) There is an oddity about this statement since it describes the date on which Mr Lyon’s employment started as being 11 March 2015, when the Mike de Courcey contract, which refers to the TUPE transfer, is dated 1 November 2013. There is no explanation for this.

(22) The statement at paragraph 30 includes an acknowledgment of receipt pursuant to which the employee states that:

> “I acknowledge receipt of this Statement Main Terms and Conditions of Employment and agree to be bound by the terms and conditions herein.”

(23) There are then lines for including the name, the date and the signature, of the employee. In the copy that we have, these have not been completed. Furthermore, it provides for the acknowledgment to be signed (on behalf of the company) and the name of that signatory and the date on which it is signed may also be included. Again, these have not been included in the copy that we have seen.

(24) But what seems clear to us is that the Transferred Staff and In Tandem both recognised that the Transferred Staff’s employment had changed from that with the customer to one with In Tandem.

(25) The invoicing arrangements between In Tandem and its customers dovetails with the provision of information and payments set out in clauses 2.2 and 2.3 of the contracts between them. Invoices for the services were raised by In Tandem either weekly or monthly depending on the client and was raised only once money had been received into In Tandem’s bank account pursuant to clause 2 of the contract. The invoices describe (in the vast majority of cases) the services which are supplied by In Tandem to its customer. Firstly “As per contract” which is the commission or charge made by In Tandem for, in its eyes, the VATable services which it provides; namely outsourced payroll, pension, employee benefit and compliance services. It has accounted for output tax on these amounts. Secondly “Disbursements to HMRC”. This comprises the income tax and

National Insurance Contributions for the employees which In Tandem has agreed with its customers will be paid to it by those customers and which it, in turn, will pay over to HMRC. No VAT is charged on these amounts, and HMRC accept that this is correct.

*Best Judgment*

13. Officer Roberts gave evidence as to the basis on which the assessments had been raised. This was not challenged by the appellant. Her evidence was that the output tax due on the net pay was calculated by reference to In Tandem's RTI returns, as this contained In Tandem's own figures for the value of wages paid to workers. Another HMRC officer, Officer Matthews had identified the cost of salaries and wages declared in In Tandem's corporation tax accounts and compared this to the gross cost of payroll for the same period as declared on In Tandem's RTI returns. He calculated that In Tandem's own directly employed workers accounted for 11.9% of the gross payroll cost. A reduction was therefore applied to the monthly net pay figures to exclude directly employed workers. VAT was then applied to the remaining net pay. The VAT fraction of 1/6 was used to identify the VAT element of the VAT inclusive amount. The additional VAT due was calculated therefore as being 1/6 of the net cost of payroll, adjusted to exclude the directly employed workers. The total additional output tax calculated to be due, using this method, for the period from April 2013 to February 2016 was £5,059,396.12. The total input tax to be denied was calculated by adding the total input tax claims In Tandem's VAT returns for the periods 02/13 to 08/15. This was calculated to be £4,140,589.

*The penalties*

14. In their statement of case and skeleton argument, HMRC set out what they considered to be the "factual background". It comprises a synopsis of the correspondence between the parties and records of meetings (or postponed or cancelled meetings). It is set out below. We find that the contents of the emails, records of meetings, and letters, to be accurate and find them as facts. However the interpretation of those facts and the emphasis which HMRC has placed on certain aspects of them is seriously challenged by the appellant (i.e. by Mr Purkiss), and we deal with this challenge hereafter.

*The documentary evidence*

15. HMRC became aware of potential discrepancies in the tax affairs of In Tandem in March 2015. In particular, the VAT input tax claimed by In Tandem appeared to be overstated and the output tax understated for a company whose principal activity was the provision of labour to its clients.

16. By letter dated 5 March 2015 HMRC gave notice to In Tandem that it intended to carry out an inspection of the business records at the registered business address. That inspection was to take place on 21 April 2015.

17. By letter and e-mail of 8 April 2015 In Tandem advised HMRC that it was moving to new offices and requested alternative dates for the inspection to take place.

18. By e-mail of 13 April 2015 HMRC provided to In Tandem a new date of the inspection being 14 May 2015.

19. By letter and e-mail dated 7 May 2015 In Tandem advised HMRC that it was not in a position to accommodate the visit on 14 May 2015 as they were still not in their new premises, had no power and no IT.

20. In a telephone call to In Tandem on 20 May 2015 HMRC arranged to visit In Tandem's premises on 22 July 2015 to complete the inspection.

21. By e-mail dated 15 July 2015 In Tandem again wrote to HMRC to advise that the 22 July date was no longer convenient as Mr. Wojcik, a director, was off work with a 'slipped disc'. In Tandem advised that they had also experienced further delays with the office move.

22. By e-mail dated 20 July 2015 Mr Wojcik confirmed that a new date for the inspection had been agreed in a telephone call with HMRC and that the new date for the inspection had been agreed as 9 September 2015.

23. By letter dated 21 July 2015 HMRC wrote to In Tandem confirming the date and indicating that any failure of the inspection to take place as agreed would result in HMRC disallowing In Tandem's claim for input tax and raised the possibility of a penalty being imposed.

24. On 9 September 2015 HMRC officers attended the new business premises to carry out their inspection of Company records as agreed. They met Mr Purkiss who advised the officers that it was not possible for them to examine In Tandem's records as those records were with their accountants in London. HMRC officers suggested that they could go to London to inspect the records there but Mr Purkiss assured them that In Tandem's records were in the process of being moved to the new premises.

25. At that meeting Mr Purkiss advised HMRC officers that he was to be appointed as a director of In Tandem. Companies House records indicated that he was so appointed on 15 September 2015.

26. By letter dated 28 September 2015 HMRC notified In Tandem of a new date for the inspection of its records, that date being 28 October 2015.

27. By letter dated 23 October 2015 In Tandem formally notified HMRC of Mr Purkiss' appointment as a director and the resignation of Mr. Wojcik as director. The letter also indicated that Mr Purkiss was to be in the United States until mid-December and that the meeting arranged for 28 October 2015 should not go ahead until he returned to the UK.

28. An e-mail to HMRC dated 26 October 2015 from In Tandem's accountants confirmed their view that the inspection scheduled for 28 October 2015 should not go ahead without Mr Purkiss being present.

29. On 26 October 2015 an officer from HMRC telephoned In Tandem and spoke to

Lindsay Treasure ("**Miss Treasure**") who had been appointed as a director of In Tandem in March 2015. Miss Treasure confirmed that In Tandem's records were now held at the new business premises.

30. HMRC's officers asked Miss Treasure to allow them to inspect those records on 28 October 2015 as arranged. Miss Treasure however, would not agree to this and insisted that the inspection take place in the company of Mr Purkiss when he returned to the UK.

31. By letter dated 29 October 2015 HMRC advised In Tandem that it had 10 days to produce all of the records which had been requested for inspection or that HMRC would take action to deny In Tandem's claim for input tax on the basis that no evidence had been provided to support its claim. HMRC also stated that it would consider action to make a best judgment assessment of understated output tax. HMRC's letter also raised again the possibility of penalties.

32. By letter dated 5 November 2015 Mr Purkiss wrote to HMRC to advise that In Tandem's accountants had been working to reconstruct the Company records as it appeared that its VAT returns had been completed using US tax rules. He suggested that had resulted in an overstatement of both output tax and input tax. Mr Purkiss suggested that there would in any event, be no loss of tax to the Exchequer. Mr Purkiss asked HMRC to allow him a further 14 days to give him time to send In Tandem's records.

33. By letter dated 9 November 2015 HMRC advised In Tandem that in the circumstances it was unreasonable to request further time to provide the records requested for inspection and unreasonable only to allow that inspection in the presence of Mr Purkiss. HMRC again asked for the records requested to be sent as soon as possible.

34. By letter to In Tandem dated 20 November 2015 HMRC provided:

- An analysis of Pay as You Earn ("**PAYE**") for tax years ending 2013/14 to 2015/16;

- An analysis of VAT input/output tax for periods ending February 2013 to August 2015;

- Corporation tax turnover; and

- A computation for proposed denial of In Tandem's input tax claim and an assessment of understated VAT based on the difference between VAT turnover and the gross costs of In Tandem's payroll.

35. In the letter of 20 November 2015 HMRC sought In Tandem's comments on discrepancy between In Tandem's gross cost of payroll from PAYE which was significantly greater than the turnover declared in In Tandem's company accounts.

36. By 12 January 2016 no records for the Company or explanations for discrepancies

had been received by HMRC from In Tandem. HMRC therefore made an authorised and unannounced visit to In Tandem's registered premises for the purposes of carrying out an inspection of Company records. As no directors were available to meet with HMRC's officers, a Notice to Produce Documents pursuant to Schedule 36 of the Finance Act 2008 was left with In Tandem's receptionist.

37. On 1 February 2016 HMRC made a further authorised but unannounced visit to In Tandem's premises. Initially HMRC's officers were told that no directors were available; however Miss Treasure later appeared and spoke to officers who handed her a letter showing the visit was authorised. Miss Treasure retired to consider it and returned a few minutes later to advise officers that the visit was 'not convenient'.

38. On 3 February 2016 HMRC telephoned In Tandem and again spoke to Lindsay Treasure. She stated that she had spoken to Mr Purkiss and that a letter had been sent to HMRC which addressed some of the outstanding issues.

39. That letter was received by HMRC on 4 February 2016. The letter explained that all of In Tandem's records had been passed to its accountants so that they could be reconstructed and reconciled. The letter expressed surprise that HMRC had not yet made assessments which In Tandem could then appeal. It was suggested that an active appeal would set a timetable that In Tandem would be bound to adhere to. The letter made further representations about the corruption of software which had led to VAT being accounted for in accordance with US not UK tax rules.

40. HMRC replied to that letter by letter of 8 February 2016 stating that HMRC were in the process of preparing assessments. In the meantime, the letter again asked In Tandem for a convenient date for when inspection of records might take place.

41. On 17 February 2016 a meeting took place at In Tandem's registered premises between HMRC's officers and Mr Purkiss and Miss Treasure. At the meeting Mr Purkiss explained that

- In Tandem had operated its accounts by transferring records electronically to the US where accounts were prepared before being sent electronically back to the UK.

- In Tandem was aware that this approach left the Company vulnerable and that it was therefore looking to adopt a more traditional approach to accounting.

- The In Tandem business model took workers from In Tandem clients under TUPE (Transfer of Undertaking Protection of Employee Regulations 2006) (**"TUPE"**) so In Tandem is the employer.

- In Tandem maintained the payroll for these 'employees' but did not pay the employees. The pay for the employees was paid by In Tandem's clients direct to their employees.

- The net pay of In Tandem employees was therefore not included as turnover

for VAT purposes.

- HMRC's proposed denial of input tax and further assessments for output tax were flawed when considering the way the Company operates.

42. At the meeting on 17 February 2016 Mr Purkiss advised that he would provide a detailed written explanation of how In Tandem operates to HMRC within 14 days.

43. By letter dated 18 February 2016, HMRC confirmed what had been agreed at the meeting the previous day and again requested that copies of Company records be made available for inspection. Additionally, HMRC also requested evidence of the contractual arrangements that existed between In Tandem, its clients and the employees.

44. By 30 March 2016 no correspondence had been received from In Tandem whatsoever so HMRC wrote to In Tandem to remind them of what they had agreed to provide.

45. HMRC eventually received a reply to its letter of 18 February 2016 by letter dated 27 April 2016 from Mr Purkiss. It apologised for the delay in response which was caused by Mr Purkiss' ill-health. The letter explained that Miss Treasure had resigned as a director and that HMRC's requests for information had been passed to In Tandem's accountants.

46. By 2 June 2016 HMRC had received no response from the accountants and so by e-mail sent that day, requested a response. The accountants replied by email on 7 June 2016 asking for HMRC's enquiries to be made in writing. HMRC refused this request by e-mail dated 9 June 2016.

47. No further evidence or representations had been received by HMRC from In Tandem or its accountants. HMRC having considered that their meeting with Mr Purkiss on 17 February 2016 provided sufficient evidence to justify the making of an assessment, issued an assessment notification to In Tandem on 9 August 2016 for understated VAT and interest in the sum of £9,646,150.09.

48. HMRC considered that In Tandem's failure to submit accurate tax returns was deliberate.

49. By letter from In Tandem to HMRC dated 30 August 2017 In Tandem formally appealed that assessment notification and appealed by notice to this Tribunal dated 24 October 2017.

50. Given that In Tandem had repeatedly stated that further evidence would be provided to HMRC, by letter dated 4 November 2016, HMRC invited In Tandem to apply to undertake Alternative Dispute Resolution ("**ADR**").

51. In Tandem agreed but ADR failed to result in a settlement of outstanding issues. On 19 July 2017 both parties to the ADR signed an 'exit agreement' allowing them to rely on certain documents in the appeal proceedings which were presented to HMRC

by In Tandem during the ADR process.

52. By letter dated 25 January 2017 HMRC sent to In Tandem a Notice of Penalty Assessment for inaccuracies contained in the tax returns provided by In Tandem to HMRC for tax in the period 27 June 2012 to 29 November 2016.

53. This penalties were imposed pursuant to Schedule 24.

54. By letter to the Tribunal of 13 June 2017 In Tandem applied to have the penalties included in this Appeal. HMRC did not object to that application.

*The oral evidence*

55. At the February 2019 hearing, Mr Purkiss tendered a witness statement which he adopted. He had also, through the appellant's skeleton argument (which he had compiled) provided further evidence. He was cross examined in a firm but fair way by Mr Golder who put, squarely, to Mr Purkiss that he and the appellant must have known that the appellant was not entitled to recovery of the input tax and had to account for output tax on the supplies of labour; and so failing to do so meant that the relevant returns were deliberately inaccurate. This was absolutely the proper thing to do given that the concept of deliberate means, in our view, that a taxpayer, knowing that a document is incorrect, nonetheless submits it to HMRC with the intention that HMRC relies on it as being accurate. It is tantamount to dishonesty.

56. Mr Golder also put to Mr Purkiss a number of inconsistencies between the documentary records (inter se) and the documentary records and his adopted witness statement.

57. The main thrust of Mr Golder's position, and his cross examination, was that the Company and Mr Purkiss had not cooperated with HMRC and indeed had done everything in their power to avoid providing the Company's documentary records of the relevant transactions, to HMRC. It was Mr Golder's view that this evidenced an acknowledgment that the Company knew that its VAT position was wrong.

58. For example, on 9 September 2015, Officer Matthews visited In Tandem's offices where he spoke to Mr Purkiss who (as Officer Matthews' records) told him that In Tandem's accountants had the Company's books and records "and they were in London". How then, asked Mr Golder, can Mr Purkiss say at his meeting with Officer Matthews on 17 February 2016 that (as reported by Officer Matthews) firstly "all of ITR's records are "in the cloud""; and secondly "that everything is scanned into the Company's electronic systems and until recently had been sent over to the US (which is where he spends the majority of his time); records are prepared there and sent electronically back to the UK following which VAT returns are completed and filed"?

59. Furthermore, in Mr Purkiss' witness statement he indicates that "the reconstruction of the records is costly and time consuming and due to monetary restraints and my own ill-health we have not undertaken any further reconstruction at this stage and agree there has been slippage" (that was in his witness statement of 4 January 2018).

60. But this is seemingly inconsistent with Mr Purkiss' comments in his letter to Officer Matthews dated 5 November 2015 where he says that “I understand that the accountants have now completed the reconstruction of records on the non-corrupted programme as we discussed…..... it would appear that the VAT returns may have been completed using American sales tax rules and consequently whoever stated both output and input (inclusion of bureau work) ……”

61. It was Mr Purkiss’ evidence that in his view HMRC had all the relevant information to understand In Tandem’s business model and to analyse its VAT position. HMRC had the names of the clients and had the Company's bank statements. In Mr Purkiss' view HMRC could have “followed the money”. It had all the information relevant to In Tandem's business model.

62. Mr Purkiss explained that the main problem that the Company faced arose from Mr Davies being charged with murdering his wife in 2013. Mr Purkiss was asked to assist the police in that prosecution and was a prosecution witness at Mr Davies' trial which resulted in a conviction for fraud and a sentence of 8 years imprisonment. During the period of the trail and its immediate aftermath, however, In Tandem suffered a number of data purges and other “glitches” that appeared to indicate that their system was not secure. Simply stated, Mr Davies sabotaged the Company's accounting records and notwithstanding that there might have been inconsistencies in his story regarding their reconstruction, the truth of the matter was that it was not possible to provide reconstructed records within the time requested by HMRC. As he said in his witness statement, reconstruction is costly and time consuming. In answer to the statement in the letter of 5 November 2015 that he understood the accountants had completed the reconstruction of records, Mr Purkiss said that was indeed his understanding. He was not saying there that the accountants had definitively completed the reconstruction.

63. Mr Golder put to Mr Purkiss that it would have been comparatively simple to check whether the accountants had completed the reconstruction of the records, and so why didn't he. Mr Purkiss responded by confirming that he hadn’t checked, but whilst it would be fair to say that he wanted HMRC off his back at that time, it was still his understanding. He was not lying to HMRC. But he did think that reconstructing the records to check that the Company had undertaken the right VAT treatment was something that he wanted to do.

64. He told us that the Company’s records were in the cloud. They had been uploaded there by people in India, who did a good job, but when the Company wanted people in the USA to do the same, they only did an incomplete job. It was Mr Purkiss’ evidence that the records had been corrupted in the cloud. The truth of the matter was, however, that there were very few paper records. Sales invoices go out via the computer, purchase invoices come in and are scanned.

65. When it was put to him about the accountants having the books and records of the Company in London, it was Mr Purkiss’ position that he interpreted books and records not as physical books and records but as the records of the Company irrespective of the medium in which they were held (whether written, in the cloud or whatever).

66. Mr Golder put to Mr Purkiss that sometime between 9 September 2015 and 17 February 2016 Mr Purkiss destroyed the Company records. Mr Purkiss denied this and said that the records were destroyed or corrupted by Mr Davies.

67. Mr Golder also cross-examined Mr Purkiss on the transfer of employees from the customers to In Tandem. Mr Golder thought it was inconceivable that this had not happened without consultation with those employees and that there would be records of such consultation. Mr Purkiss said that he had no idea whether any such discussions or consultation took place, but the fact was that the employees were transferred. The employers (he thought) wanted to ensure that the employees were safeguarded and that the most appropriate way of doing this was to ensure that their contracts of employment were transferred across to In Tandem under TUPE. He had experience of a transfer of undertaking being completed in 5 days on a liquidation so it was clear that it could be done quickly and there were no unions involved.

68. Mr Golder (out of a sense of some frustration, it must be said) put to Mr Purkiss that this matter could have been put to bed some time ago if the Company and Mr Purkiss had provided the relevant documents, but Mr Purkiss responded that he could not provide documents that did not exist.

69. Furthermore, said Mr Golder, Miss Treasure, a director of the Company had made an admission on a call with Officer Matthews of 26 October 2015 where she said that the Company was an outsourcing company and "eventually admitted that it did indeed supply workers to third party clients". Given that she was director, how was this consistent with the Company's current position which was that the Company did supply labour?

70. Mr Purkiss accepted that the Company was supplying labour but did not accept that it was supplying a VATable supply of labour. It was not an employment agency who would have interviewed the employees, something which the Company did not do.

71. Mr Purkiss had undergone treatment for liver cancer in 2015/2016 and was unable, therefore, to deal with matters (in his words) “adequately”, but he did explain the working model of In Tandem, along with some examples, at the meeting with HMRC on 17 February 2016.

72. Mr Purkiss accepted that In Tandem and the customers were not joint employers. He accepted that In Tandem was the only employer. He accepted that the obligation to pay the wages of the employees was that of In Tandem.

73. However, if there was a dispute, (for example involving an employee if a customer didn’t pay an employee), it was Mr Purkiss’ firm view that the employee would have a claim not against In Tandem but against the customer. That was what was always intended. A claim would be made by a driver against the customer and not against In Tandem.

74. As regards the claim for (in HMRC’s view) over recovered input tax Mr Purkiss explained that this was something which resulted from the use of American sales software which was used to submit the VAT returns (the Tribunals' understanding is

that the payments to HMRC of PAYE and NIC's were treated as including VAT by that sales software. That VAT was treated as input VAT and recovered/claimed by the Company). Mr Purkiss' position was that as soon as he understood what had happened, he corrected the position.

75. Mr Purkiss accepted that he was a tax inspector until 1977 when he left the Inland Revenue and he has since been involved in many companies. But there is a difference between being inefficient and being dishonest. He accepts the former but not the latter. He said he had never lied to HMRC officers even to get them off his back. In hindsight he accepts that the input tax recovery was wrongly claimed, but this was because of an incorrect methodology rather than dishonesty.

76. Mr Golder put to Mr Purkiss that neither the contracts nor Mr Purkiss' oral evidence could be relied upon as being an accurate reflection of the way in which In Tandem's business operated. Mr Purkiss responded by saying that he has given evidence on oath. His view is that no VAT was due on the wages but "if I'm wrong, I'm wrong".

77. Finally, Mr Purkiss said, that he was not sure what records would have added anything to the evidence there was before the Tribunal today. The contracts, HMRC's records and the bank statements should have been enough for HMRC to understand the nature of In Tandem's business and to analyse the VAT consequences of its method of trading.

78. He accepted that the history of the Company's interaction with HMRC set out above does not paint him in the best light, and it was not his finest hour when dealing with HMRC's officers but there were reasons (basically Mr Davies' sabotage, and his own ill heath) which had a profound influence on his ability to provide HMRC with the information that they requested. The position was a great deal more complicated than that which is being suggested by Mr Golder and this can be seen not just from his oral testimony but also from the records.

79. In Tandem had hoped to resolve the dispute with HMRC through ADR, but this proved not to be the case and the ADR ended without agreement.

80. Mr Purkiss' position was that In Tandem was a victim of a "wilful and malicious attack by disgruntled and bitter convicted criminal that prevented him from discharging their normal obligations to HMRC" and this was something which should have been taken into account by HMRC when considering reductions in the penalties, A reduction of 5% did not reflect that or the "extraordinary circumstances the company found itself in".

81. Mr Purkiss very fairly said that he and the Company found the original HMRC officers fair and open minded who wanted to get the tax right, and this was something that Mr Purkiss was trying to assist in as the documentary evidence showed.

## The relevant legislation and case law

82. There is no dispute between the parties as to the applicable legislation and case

law which we set out below.

*The assessments*

83. Article 1 of the Principal VAT Directive (Directive 2006/112) (“**PVD**”) establishes a common system of VAT and Article 1(2) provides,

> “The principle of the common system of VAT entails the application to goods and services of a general tax on consumption exactly proportional to the price of the goods and services, however many transactions take place in the production and distribution process before the stage at which the tax is charged.
>
> On each transaction, VAT, calculated on the price of the goods or services at the rate applicable to such goods or services, shall be chargeable after deduction of the amount of VAT borne directly by the various cost components”.

84. Article 2(1) of the PVD provides that VAT is charged on, among other things, supplies of goods and services for consideration by a taxable person acting as such.

85. Article 9(1) of the PVD provides as follows:

> “Taxable person shall mean any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity.
>
> Any activity of producers, traders or persons supplying services, including mining and agricultural activities and activities of the professions, shall be regarded as ‘economic activity’. The exploitation of tangible or intangible property for the purposes of obtaining income therefrom on a continuing basis shall in particular be regarded as an economic activity”.

86. Article 24 of the PVD defines the “supply of services” as “any transaction which does not constitute a supply of goods”.

87. Article 73 of the PVD defines the taxable amount as,

> “in respect of the supply of goods or services,...the taxable amount shall include everything which constitutes consideration obtained or to be obtained by the supplier, in return for the supply, from the customer or third party,...”

88. The PVD is implemented into UK law by VAT Act 1994, which must be interpreted as far as possible to comply with the PVD. The relevant provisions of the VAT Act 1994 are provided as follows:

89. Section 4(1) provides that VAT shall be charged on any supply of goods or services made in the UK, where there is a taxable supply made by a taxable person in the course or furtherance of any business carried on by him.

90. By virtue of section 25(2) and (3), a taxable person who has paid VAT to his suppliers which is allowable Input tax by virtue of section 26 VAT Act 1994, may claim

a deduction of this Input Tax from any Output Tax due to them or recover that amount from HMRC.

91. By virtue of the VAT Regulations 1995, Regulation 29(1) and (2), a taxable person may not make any claim for a deduction of Input Tax unless he holds the required documentary evidence.

*What did In Tandem supply to its customers?*

92. The leading authority on the legal test to be applied when considering the identity of the person to whom supplies are made by taxpayers (in the context of input tax recovery by that person) is the Supreme Court decision in *Airtours Holidays Transport Ltd v Revenue and Customs Commissioners* [2016] UKSC 21 (*"Airtours"*). It is also very helpful in identifying the test to be applied when determining whether a payment should be treated as consideration for a supply. In his leading judgment Lord Neuberger said

> "46 Lord Hope made the same point in para 110 in remarks which are perhaps particularly germane for present purposes: "I think that Lord Mille went too far at p 418G when he said that the question to be asked is whether the taxpayer obtained 'anything—anything at all' used or to be used for the purposes of his business in return for that payment. Payment for the mere discharge of an obligation owed to a third party will not, as he may be taken to have suggested, give rise to the right to claim a deduction. A case where the taxpayer pays for a service which consists of the supply of goods or services to a third party requires a more careful and sensitive analysis, having regard to the economic realities of the transaction when looked at as a whole.
>
> 47 This approach appears to me to reflect the approach of the Supreme Court in the subsequent case of WHA Ltd v Revenue and Customs Comrs [2013] UKSC 24; [2013] 2 All ER 907 where at para 27, Lord Reed JSC said: "The contractual position is not conclusive of the taxable supplies being made as between the various participants in these arrangements, but it is the most useful starting point". He then went on in paras 30–38 to analyse the series of transactions, and in para 39, he explained that the Tribunal had concluded that "the reality is quite different" from that which the contractual documentation suggested. Effectively, Lord Reed JSC agreed with this, and assessed the VAT consequences by reference to the reality. In other words, as I said in Secret Hotels2 Ltd v Revenue and Customs Comrs [2014] UKSC 16; [2014] 2 All ER 685, para 35, when assessing the VAT consequences of a particular contractual arrangement, the court should, at least normally, characterise the relationships by reference to the contracts and then consider whether that characterisation is vitiated by [any relevant] facts.
>
> 48 The same approach was adopted by the Court of Justice in Revenue and Customs Comrs v Loyalty Management UK Ltd and Baxi Group Ltd (Joined Cases C-53/09 and C-55/09) EU:C:2010:590; [2010] ECR I-9187; [2010] STC 2651, paras 39–40, where they stated, citing previous judgments: "consideration

of economic realities is a fundamental criterion for the application of the common system of VAT", and added that that issue involved consideration of "the nature of the transactions carried out" in the particular case. To much the same effect, in Tolsma v Inspecteur der Omzetbelasting Leeuwarden (Case C-16/93) EU:C:1994:80; [1994] ECR I-743; [1994] STC 509, para 14, the Court of Justice said that "a supply of services is effected 'for consideration' … only if there is a legal relationship between the provider of the service and the recipient pursuant to which there is reciprocal performance", which it explained as meaning "the remuneration received by the provider of the service constituting the value actually given in return for the service supplied to the recipient". In the context of the supply of goods, the court made the same point in Primback Ltd v Customs and Excise Comrs (Case C-34/99) EU:C:2001:271; [2001] ECR I-3833; [2001] 1 WLR 1693, para 25, where it described "the determining factor" as "the existence of an agreement between the parties for reciprocal performance, the payment received by the one being the real and effective countervalue for the goods furnished to the other".

49 In Revenue and Customs Comrs v Newey (trading as Ocean Finance) (Case C-653/11) EU:C:2013:409; [2013] STC 2432, para 40, the Court of Justice again emphasised: "that a supply of services is effected 'for consideration', within the meaning of article 2(1) of [the Sixth] Directive, and hence is taxable, only if there is a legal relationship between the provider of the service and the recipient pursuant to which there is reciprocal performance, the remuneration received by the provider of the service constituting the value actually given in return for the service supplied to the recipient." In para 41, the court went on to explain: "the term supply of services is therefore objective in nature and applies without regard to the purpose or results of the transactions concerned and without its being necessary for the tax authorities to carry out inquiries to determine the intention of the taxable person." The court then observed in paras 42–43 that: "consideration of economic and commercial realities is a fundamental criterion for the application of the common system of VAT." and that: "the contractual position normally reflects the economic and commercial reality of the transactions." An exception to the normal rule that the contractual relationship is central was then identified by the court as being where: "those contractual terms constitute a purely artificial arrangement which does not correspond with the economic and commercial reality of the transactions." (Para 45.)

50 From these domestic and Court of Justice judgments, it appears clear that, where the person who pays the supplier is not entitled under the contractual documentation to receive any services from the supplier, then, unless the documentation does not reflect the economic reality, the payer has no right to reclaim by way of input tax the VAT in respect of the payment to the supplier."

*Best Judgment*

93. By virtue of section 73(1) of the Value Added Tax Act 1994 ("**VAT Act**"), where it appears to HMRC that tax returns made by a taxpayer are incomplete or incorrect, HMRC may assess the amount of VAT due from him to the best of their judgment and

notify it to him.

94. Section 83 VAT Act provides:

> "Subject to section 84, an appeal shall lie to a tribunal with respect to any of the following matters..."
>
> There is then set out a series of actions, decisions, and other matters arising under the Act listed under paragraphs (a) to (z). Paragraph (p) is as follows:

95. An assessment −

> (i) under section 73(1) or (2) in respect of a period for which the appellant has made a return under this Act....
>
> or the amount of such an assessment."

96. In *Van Boeckel v Customs and Excise Commissioners* [1981] AER 505 ("*Van Boeckel")* the High Court (Woolf J as he then was) considered the application of best judgment.

> "..It should be recognised...that the Commissioners should not be required to do the work of the taxpayer in order to form a conclusion as to the amount of tax which, to the best of their judgement is due. In the very nature of things frequently the relevant information will be readily available to the taxpayer, but it will be very difficult for the commissioners to obtain that information without carrying out exhaustive investigations. In my view, the use of the words 'best of their judgment' does not envisage the burden being placed on the commissioners of carrying out exhaustive investigations. What the words 'best of their judgement' envisage, in my view, is that the commissioners will fairly consider all material placed before them and, on that material, come to a decision which is one which is reasonable and not arbitrary as to the amount of tax which is due"

97. Generally, the burden lies on the taxpayer to establish the correct amount of tax due:

> "The element of guesswork and the almost unavoidable inaccuracy in a properly made best of judgment assessment, as the cases have established, do not serve to displace the validity of the assessments, which are prima facie right and remain right until the taxpayer shows that they are wrong and also shows positively what corrections should be made in order to make the assessments right or more nearly right." (Bi−Flex Caribbean Ltd v Board of Inland Revenue (1990) 63 TC 515, 522−3 PC, per Lord Lowry)."

*The penalties*

**Schedule 24 Finance Act 2007**

98. The provisions of Schedule 24 that are relevant to this case are as follows:

(1) The respondents may assess a taxpayer for a penalty if a tax return contains a deliberate inaccuracy (paragraphs 1 and 3).

(2) The penalty for an inaccuracy which is deliberate but not concealed is capped at 70% of the potential lost revenue (paragraph 4).

(3) This can be mitigated to 35% if a taxpayer makes a prompted disclosure (paragraphs 9 and 10).

(4) The penalty for a careless inaccuracy is capped at 30% but can be mitigated to 15% if a taxpayer makes a prompted disclosure (paragraphs 4, 9 and 10).

(5) The respondents may reduce the penalty for special circumstances (paragraph 11).

(6) A taxpayer may appeal against a penalty assessment (paragraph 15).

(7) On an appeal, the Tribunal may affirm HMRC's decision or substitute for it another decision that HMRC had the power to make (paragraph 17(2)).

(8) If the Tribunal substitutes its own decision it can rely on paragraph 11 (i.e. special circumstances) to a different extent to HMRC but only if HMRC's decision in respect of the application of paragraph 11 is flawed.

## Burden and standard of proof

99. The burden of showing that the assessments are valid in time best judgment assessment lies with HMRC.

100. The burden of showing that any inaccuracies in the relevant VAT returns were deliberate inaccuracies also lies with HMRC.

101. In each case the standard of proof is the balance of probabilities or that it is more likely than not.

102. The burden of showing that the assessments are incorrect and that they overcharge the appellant lies on the appellant who must also establish the extent of this overcharge i.e. what, on the balance of probabilities, the correct amount should be.

## Discussion

*Submissions*

103. In broad terms, and subject to what we say at [150] below, Mr Golder submits as follows:

(1) The evidence provided by the appellant as to the contractual arrangements and the history of dealings between In Tandem, the workers and the customers is unsatisfactory. The appellant has not shown, to HMRC's satisfaction, that the picture painted by Mr Purkiss in his evidence is correct.

(2) However, the appellant made supplies of labour to its customers and not just of the outsourced services as claimed by the appellant.

(3) Since the workers were employees of In Tandem and not of its customers, it was In Tandem's legal responsibility to pay them their wages.

(4) Although actual payment of these wages was made by the customers (and not paid to In Tandem who then paid the workers) that payment is still consideration for a VATable supply of labour by In Tandem to its customers.

(5) The assessments were made to best judgment.

(6) The appellant accepts that the assessments are correct to the extent that they relate to input tax recovered by the appellant; the appellant is only disputing the under declared output tax in the assessment.

(7) The inaccuracies in the relevant VAT returns were deliberate for the following reasons:

(a) Mr Purkiss is a director of In Tandem and has been a director of many companies. He was also an Inspector of what was the Inland Revenue. In Tandem must have been fully aware of its responsibilities to submit accurate VAT returns to HMRC.

(b) In Tandem has now conceded its input tax claim since it is unable to provide evidence to support that claim in the form of invoices. This is something that In Tandem must have known about when submitting its returns claiming the input tax deduction.

(c) Mr Purkiss must have known (and the Company must have known) that the tax returns were submitted to HMRC containing inaccuracies.

(d) The Company has failed to provide evidence to HMRC of its claim in respect of the output tax liability which it is obliged to do (and it is aware of those obligations).

(e) In Tandem has repeatedly told HMRC that evidence concerning its output tax position would be provided to HMRC but no adequate evidence has been so provided.

(f) The Company has persistently failed to allow HMRC access to carry out an examination of its business records.

104. The appellant submits, subject to what is said at [150]below, as follows:

(1) The documentary and oral evidence shows that the workers were first employed by the customers but were then transferred to In Tandem under TUPE. They were then employed by In Tandem who in turn supplied to them the customers who were responsible for the day to day control of the workers and for actually paying them. This might have been a supply but it is not a VATable one.

(2) The services provided to customers did not involve recruiting staff (like a

recruitment agency). In Tandem did not control, command or insure the individual workers (which was undertaken by the customer). In Tandem dealt with accounting, taxation, national insurance, pension, compliance and other government subscriptions in order to simplify pension auto-enrolment and other similar governance functions required by its customers.

(3) As such In Tandem was correct to account for VAT on only its commission and the income tax and national insurance for the workers which were recharged to its customers.

(4) The inaccuracies in the VAT returns might have resulted from careless behaviour but not from deliberate behaviour. HMRC was made aware of the over recovery of input tax as soon as Mr Purkiss became aware of it. It resulted from a misunderstanding caused by American software. Corrective returns have been submitted as part of the ADR process. HMRC have, in any event, suffered no loss.

(5) HMRC should have taken into account the malicious behaviour of Mr Davies when considering reductions to the penalties.

***The first issue: what was supplied by In Tandem to its customers***

105. The contracts clearly describe the services which In Tandem supplied to its customers as "Provision of labour facilitated by the Transferred Staff". Mr Purkiss does not deny that In Tandem supplied labour but says it was not a VATable supply. Mr Golder submits that In Tandem supplied labour. So there seems to be a consensus that In Tandem supplied labour to its customers. But in order to do so it must have acquired the function of supplying labour and/or the Transferred Staff from somewhere. It required workers. It did not go out and recruit them and grow its business organically. Mr Purkiss says that did not happen and we believe him. In Tandem's contention is that the Transferred Staff were employees of its customers which were transferred from its customers to In Tandem under TUPE. In Tandem needed those employees to be legally employed by it so it could obtain the benefits of scale when purchasing fringe benefits, for the mutual benefit of In Tandem, the customers and the employees.

106. The contracts record that the Transferring Staff were transferred under TUPE. Slightly oddly (in our view) Mr Golder did not accept this at face value and suggested that there might not have been any such transfer. This seemed to us a bit of a foot shooting exercise since if his case was that In Tandem provided labour, then in the absence of a TUPE transfer (and any evidence that In Tandem had recruited over a 1,000 or so employees itself - it denies doing so which we accept) we are uncertain as to how he would show that In Tandem had the wherewithal to supply labour to its customers.

107. But he did not press this point.

108. Parties to a contract cannot by themselves simply bring themselves within the jurisdiction of TUPE by saying so. Whilst we have accepted that In Tandem and its customers believed that the employees were transferred under TUPE, we have

considered whether this is a realistic claim. We consider that it is. Under regulation 3 of TUPE, there can be a relevant transfer if either (a) there is a transfer of an undertaking which is an economic entity which retains its identity after the transfer; or (b) there is a change of service provision where activities cease to be carried out by a client on his own behalf and are then carried out by another person on his behalf.

109. From a review of European and domestic case law, it seems perfectly feasible to us that the drivers transferred under the Mike de Courcey Travel contract (which is the paradigm for all the contracts) could fall within the definition of an economic entity which retained its identity after its transfer to In Tandem. And it also seems, in the alternative, that the change of service provision mentioned above, which is intended to cater for "outsourcing", could also apply.

110. And so we find as a fact that the Transferred Staff were transferred from the customers to In Tandem under TUPE as evidenced by Mr Purkiss' oral testimony and the terms of the contracts (in particular recital (4) and operative clauses 1.1 and 1.2). The transfer was either of the function of providing labour, or of the individual workers themselves.

111. This in turn enabled In Tandem to supply labour back to the customers. The description of the services as being the Provision of labour as facilitated by the Transferred Staff seems to be an entirely accurate reflection of what happened in practice.

112. Under TUPE, and in accordance with the terms of recital (4) of the contracts, In Tandem became the employer of the employees. It assumed responsibility for the "statutory employment and remuneration and provision of employment associated benefits of the Client's employees". With effect from the date of the transfers, In Tandem, therefore, assumed the legal responsibility for payment of the employee's wages. This is also confirmed by the statement of terms of employment which were given to the Transferred Staff by, we believe, In Tandem. The legal obligation to pay the employees would have transferred under TUPE in any event.

113. However, actual payment of the employee's wages was made by the customer. Mr Purkiss' oral evidence, confirmed that the arrangement for payment of these employees set out in clause 2 of the contract was correct. This was not challenged by Mr Golder. So the customer would tell In Tandem about hours worked, bonuses due and any other information which might affect the employee's pay. In Tandem would then process that information, tell the customer what amounts should be paid to the employee, what deductions should be made in respect of tax and national insurance and that the deductions for tax and national insurance should be paid to In Tandem. The net salary was then paid to the employee by the customer. In Tandem would then pay the tax and national insurance to HMRC.

114. All of this is consistent with there being an initial transfer of workers from the customers to In Tandem under TUPE; the consequential change of their employment from the customer to In Tandem along with the legal obligation to pay their wages; and the supply of their labour back to the customer under the contracts.

115. We therefore find as a fact that In Tandem supplied the labour of the Transferred Staff to the customers as described in the contract.

116. Under the provisions of *Airtours* we must then look at all of the surrounding economic circumstances to check whether or not the contract reflects economic reality. It will be apparent from the discussion above that we consider that it does.

***The second issue: what is the VATable consideration for those supplies***

117. Mr Golder's view is that the consideration includes the payment of the wages made by the customers to the workers supplied by In Tandem. Mr Purkiss says the supply of labour is not a VATable supply, implying that those wages do not comprise consideration for the supply.

118. In its skeleton, In Tandem cites the F-tT case of *Lloyds Banking Group* [2017] UKFTT 0835 ("**Lloyds**") in support of their proposition.

119. In that case, a member of the Lloyds Banking VAT Group closed its business in Ireland and transferred the operation of the winding down of that business and its employees to a company called Certus. It paid Certus redundancy payments which it (Lloyds) was obliged to pay to those employees. The question was whether those redundancy payments were consideration for a supply of services by Certus on which (because of the reverse charge mechanism) Lloyds was required to account for VAT.

120. At paragraph 113 of her decision, Judge McKeever said that:

> "113 the fundamental question is whether BOS made the Redundancy Payments *in return for* the services provided under the Service Agreements so that there was that "direct link" between the supply of services and the payment for them, required by the authorities in order to render the payment "consideration" for the supply for VAT purposes."

121. The same is true in this case. In accordance with the principles set out in *Airtours*, we start with the contract.

122. As set out in [112] above, the legal obligation to pay the employees was transferred to In Tandem along with those employees under TUPE. However, actual payment of the wages was made by the customers. We note Mr Purkiss' evidence (which we accept) was that if there were any unforeseen liabilities such as redundancy payments, the employee would have been expected to take those up with the customer and not with In Tandem. We observe, however, that whilst that might have been the anticipated position as far as In Tandem and the customer was concerned, we do not know what an employees' position would be. We suspect in practice he or she would bring an action against both and get the relevant court to sort out who his or her cause of action was against.

123. So by taking on the employees and becoming their legal employer, In Tandem also took on the legal obligation to pay them. In fact it procured that they were paid rather than paying them itself. It achieved this through the contracts. It is Mr Golder's

position that the wages are VATable consideration for the supply of labour. He cites the breadth of Article 73 of the PVD as supporting this. The wages, he says, are consideration obtained by the supplier in return for the supply by In Tandem to its customers. We are not entirely clear of the precise nature of his submission. At one stage he said that In Tandem is relieved of the obligation to pay the employees because they are now paid by the customer. By relieving In Tandem from that obligation, they are providing consideration for the supply of labour. At another time he said supply that procuring payment to the employees was consideration.

124. We are sympathetic with either view. Under the contracts, and as stated in evidence by Mr Purkiss, it was a term of the deal that the wages would be paid by the customer. The commercial benefit of this, of course, was financial continuity for the employees. In practical and physical terms he or she turned up to work at exactly the same place the day after the transfer as he or she had done on the day before. The same goes for the work carried out by that individual. Ensuring payment was made in precisely the same way before and after the transfer would have been consistent with this approach (namely to worry the employees as little as possible about the transfer, which is consistent with the overriding commercial objective of the parties which was to simply aggregate employees for the benefit of obtaining reduced cost fringe benefits).

125. We do not think that the deal would have happened if the parties had not come to some arrangement about payment of the employees wages. In our view these payments and the arrangements for it can comprise consideration for services supplied under the contracts. To do so, however, there must be a "direct link" between the supply of the services (the labour) and the payment of the wages.

126. Clearly if the wages had been paid to In Tandem by the customer, who had then gone on to pay them to the workers, that would have been VATable consideration for the supply. There could be no suggestion that In Tandem was acting as agent or nominee of the customer given that it was legally obliged to pay the workers as their legal employer. Similarly there can be VATable consideration for a supply if payment is not made to the supplier but, at his request, to a third party. If a supplier tells a customer that it will supply them with goods for £100 if the customer pays the supplier's sister, that is just as much a supply for £100 as if the supplier had insisted on payment to itself. There is a clear and direct link between the supply made by the supplier and the payment by the customer. The fact that the payment is not made to the supplier does not affect this.

127. In Tandem suggest (we think) that the wages paid to the workers are akin to the redundancy payments paid by Lloyds to Certus. We do not think that they are.

128. The main reason we say that is that the question of whether a payment is consideration for a supply will depend upon the terms of the contract measured against economic reality. The terms of the contracts in Lloyds were very different from the terms of the contracts in this case. So too was the economic background. In Lloyds it was held that there was no clear link between the supply of services by Certus and the redundancy payments. Importantly, the charges for the services paid pursuant to the charges clauses in the Lloyds contracts comprised the full consideration for the services.

The redundancy payments were not part of those charges. They were paid for a number of reasons including to satisfy an undertaking given by a member of the Lloyds Group to, inter alia, the union UNITE under a legal framework agreement. This committed Lloyds to pay the redundancy payments (over 80 million euros) which was the only basis on which Certus would agree to provide the services given that under TUPE the obligation to pay redundancy payments to the transferring employees would have transferred to it. The redundancy payments were also largely quantifiable at the date of transfer.

129. This is very different from the present case. In the case of In Tandem, an analysis of the contracts tested against the economic reality is that the deal between In Tandem and the customer was, essentially, that In Tandem would supply labour to the customers and the customers would pay a commission to In Tandem and would also pay the wages of the employees which, legally, In Tandem had the obligation to pay.

130. The meaning of "consideration" for the purposes of Article 73 of the PVD (and indeed in section 19 VAT Act where it is used in 19(2)) is not statutorily defined.

131. In the case of *Naturally Yours Cosmetics Limited v Customs & Excise Commissioners* (230/87), the Advocate General said "the fact that the scope of that expression [consideration] is not defined shows, of course, that it was intended that term should be given the broadest possible meaning".

132. This is consistent with Mr Golder's submissions in this case.

133. The ECG case of *Tolsma v Inspecteur De Omzetbelasting Leeuwarden* (Case C-16/93) ("**Tolsma**") is the leading and important case on this area. The court said:

> "…. The basis of assessment for a provision of services is everything which makes up the consideration for the service and that a provision of services is therefore taxable only if there is direct link between the services provided and the consideration received......
>
> It follows that a supply of services is effected "for consideration……. and hence is taxable, only if there is a legal relationship between the provider of the service and the recipient pursuant to which there is reciprocal performance, the remuneration received by the provider of the service constituting the value actually given in return for the service supplied to the recipient."

134. Applying these principles to the supplies made by In Tandem, it is clear to us that the wages do comprise consideration for the supply of labour by In Tandem to its customers. There is clearly a legal relationship between In Tandem and its customers. There is a direct link between the services of labour provided by In Tandem and payment of the wages by the customers to the employees which discharges In Tandem's legal obligation to make those payments as the employees' employer. Those payments are value given in return for the supply of labour. They comprise VATable consideration. As such, HMRC are correct in their assertion that In Tandem is liable to pay VAT on the wages paid by the customers to the employees.

### *The third issue: were the assessments made to HMRC's best judgment?*

135. The basis on which the assessments were made was clearly set out by Officer Roberts. Her evidence was not challenged by In Tandem. The legal test for a valid best judgment assessment is set out in *Van Boeckel*. The threshold that HMRC have to surmount is a low one. On the basis of the evidence, our view is that HMRC have come to a decision which is reasonable and not arbitrary. Indeed, as explained by Mr Golder, it may under assess the appellant since it does not include any employer National Insurance contributions which were paid by the customer. Strictly speaking this is a cost for which In Tandem should be liable as employer, and so by relieving In Tandem from the burden of payment, it is additional consideration. But HMRC are content not to assess this. It is our conclusion that assessments were made to best judgment.

### *The fourth issue: do the assessments overcharge the appellant?*

136. The principle, as set out in the *Bi Flex Caribbean* case (see [96]) is that it is for an appellant to show that a best judgment assessment overcharges it and also what corrections should be made in order to make the assessments right or more nearly right. In this case In Tandem have made no submissions that the assessments overcharged them save their submission that the wages are not consideration for a supply.

137. Given that we have found that they are, it is our view that the assessments do not overcharge the appellant and that, numerically, they are correct.

### *The fifth issue: the penalties*

138. As mentioned above, HMRC's view is that the failure to complete the VAT returns correctly, by understating the output tax liability and overstating the input tax recoverability stems from deliberate behaviour. The definition of deliberate behaviour is not defined in Schedule 24 but we derived help in interpreting the phrase, firstly from the case of *Auxilium Project Management v HMRC* [2016] UKFTT 0249, where Judge Greenbank said as follows:

> "62. Schedule 24 Finance Act 2007 does not further define the word "deliberate". HMRC's manuals state that "a deliberate inaccuracy occurs when a person gives 5 HMRC a document that they know contains an inaccuracy" (HMRC Compliance Handbook CH81150). We adopt a similar approach.
>
> 63. In our view, a deliberate inaccuracy occurs when a taxpayer knowingly provides HMRC with a document that contains an error with the intention that HMRC should rely upon it as an accurate document. This is a subjective test. The question is not whether a reasonable taxpayer might have made the same error or even whether this taxpayer failed to take all reasonable steps to ensure that the return was accurate. It is a question of the knowledge and intention of the particular taxpayer at the time.
>
> 64. The test of deliberate inaccuracy should be contrasted with that of careless inaccuracy. A careless inaccuracy occurs due to the failure by the taxpayer to take reasonable care (see paragraph 3(1)(a) of Schedule 24 Finance Act 2007 and

*Harding v HMRC* [2013] UKUT575 (TCC) at [37]).”

139. And secondly, from *HMRC v Raymond Tooth* [2018] UKUT 38 in which (and oddly enough the paragraphs are exactly the same as in *Auxilium*). The Tribunal said as follows:

> “62. Assuming, for this purpose, that the Return and the Computation were inaccurate within the meaning of section 118(7) TMA, the next question is whether such (putative) inaccuracies were deliberate.
>
> 63. It is clear that, in terms of the applicable time limits, the relevant legislation contains a hierarchy based upon culpability. As was set out in paragraph 25 above in the case of discovery assessments, the normal period is one of 4 years, increasing to 6 in the case of carelessness and to 20 in the case of deliberation. An allegation of deliberately bringing about a tax loss is a serious one, tantamount to an allegation of fraud.
>
> 64. Self-evidently, the mere completion of a return – whilst a deliberate act, in the sense that the taxpayer deliberately fills it in and submits it – cannot of itself amount to a deliberate inaccuracy in a document. The deliberation must relate to the inaccuracy, not merely the completion and submission of the document.”

*Careless*

140. It is open for us, if we decide that the behaviour was not deliberate, to come to a decision that the behaviour was, however, careless. We deal with this in more detail at [154ff] below.

141. In the First-tier Tribunal case of *Mr J R Hanson v HMRC* [2012] UKFTT 314, Judge Cannan set out what he considered the test for carelessness (or failing to take reasonable care.). We set it out below.

> “19 In my view carelessness can be equated with “negligent conduct” in the context of discovery assessments under section 29 Taxes Management Act 1970. In that context, negligent conduct is to be judged by reference to the reasonable taxpayer. The test was described by Judge Berner in Anderson (deceased) v Revenue and Customs Commissioners [2009] UKFTT 206 at [22], cited with approval by the Upper Tribunal in Colin Moore v Revenue and Customs Commissioners [2011] UKUT 239 (TCC):
>
> > “*The test to be applied, in my view, is to consider what a reasonable taxpayer, exercising reasonable diligence in the completion and submission of the return, would have done.*””

142. Although Judge Cannan’s view is not binding on us, we agree with it and adopt it as the test which is to be applied in the case of In Tandem.

143. We had almost completed our review of our draft Decision in this matter when the Upper Tribunal released its decision in the case of *Ritchie* on 12 March 2019

(*HMRC v William Ritchie and Hazel Ritchie* [2019] UKUT 0071).

144. In our draft decision we had considered whether, if In Tandem had over recovered input tax and/or underpaid output tax, its returns reflecting this contained a deliberate inaccuracy, as submitted by HMRC. We had also considered, if we found that the inaccuracies were not deliberate, whether they might have resulted from a failure to take reasonable care (careless).

145. It was our view that it is open to us to consider whether the inaccuracies were careless given the provisions of paragraphs 15(2) and 17(2) of Schedule 24 to the Finance Act 2007 which permits us to substitute for HMRC's decision (i.e. deliberate) another decision which HMRC had power to make (i.e. careless).

146. However, having read *Ritchie* it was our view that we could not consider the issue of carelessness unless HMRC specifically allege, as an alternative to deliberate behaviour, that the appellant had submitted inaccurate returns as a result of carelessness; and if they do, that the appellant has then been given an opportunity to make submissions and provide evidence that that is not the case.

147. The relevant extract from *Ritchie* is set out below:

> "37. These sources make clear that in determining what arguments the tribunal may permit to affect its decision the guiding principle must be fairness in the circumstances of the case. Fairness does not require formality, and Rule 2(2)(b) expressly requires formality to be avoided. Fairness does not require, for example, that to advance an argument not present in its statement of case or the notice of appeal a party must always formally apply to amend its earlier pleading. On the other hand it does require that the other party is given adequate opportunity in the circumstances to meet the point, whether by argument or with evidence.
>
> 38. If a new argument is a pure point of law it might be addressed, as the case may be, after: a few minutes' thought; an evening's consideration; or one or more days' research. Provided that the other party has an appropriate opportunity to meet the point, it would generally not be unfair for the tribunal to take that argument into account.
>
> 39. When the argument gives rise to the possibility that it may be rebutted by further evidence, the other party must have a fair opportunity to bring that evidence to the tribunal. Depending on the circumstances that may mean no more than asking a few extra questions of a witness who is at the hearing in any event; or it may mean arranging for documents to be provided, or further evidence called, the next day; or seeking a longer adjournment. We do not wish to be thought to be laying down any particular rules, as what fairness requires will depend on all the circumstances of the case, and cases in the FTT vary enormously from informal appeals that take a very short time to elaborately argued cases that last for many days.
>
> 40. On the other hand, there will be circumstances where it is simply too late for a point to be raised. Where it is not reasonably possible in the circumstances

of the case – having regard in particular to the resources of the parties and the need to avoid delay – for the other party to have a fair opportunity to rebut a new point, that is likely to mean that it would be unfair for a new point to be taken."

148. We had trawled through the statement of case, the parties respective skeleton arguments and their witness statements. We could not find any submissions from HMRC that as an alternative to alleging deliberate behaviour, they allege carelessness. They have plumped for deliberate and have not suggested carelessness as a fall back.

149. In these circumstances, and given *Ritchie*, we did not feel that we could, of our own volition, consider carelessness without having given the parties the opportunity to put forward their submissions and evidence on the point. It would not have been fair to either party to do so.

150. We therefore issued directions seeking an indication from HMRC as to whether they alleged careless inaccuracies by the appellant and if so, their submissions in this regard. HMRC did make that allegation, to which the appellant responded. HMRC's submissions were not directed exclusively at careless behaviour. Mr Golder, perhaps seeing the writing on the wall, sought to burnish his deliberate behaviour credentials and repeated most of his submissions made at [99] above. However he also submitted that a prudent and reasonable taxpayer would keep proper records of their business operation and allow HMRC to see those records in order to ascertain the true tax position. In response, the appellant commented on HMRC's submissions but made no positive submissions of its own save to submit that if the standard for careless conduct is what a reasonable person would do, then given all the circumstances in this case "I am not sure what more any reasonable person would have been able to do other than the reconstructions carried out and submitted".

151. We have taken these further submissions into account when discussing the issue of penalties below.

*Special circumstances*

152. Finally, HMRC do have the ability to reduce a penalty if it considers that there are special circumstances which justify a reduction.

153. There have been a number of cases on special circumstances from which we derive the following principles (see *Bluu Solutions Ltd v Commissioners for Her Majesty's Revenue & Customs* [2015] UKFTT 0095 and the cases cited therein):

(1) While "special circumstances" are not defined, the courts accept that for circumstances to be special they must be "exceptional, abnormal or unusual" (Crabtree v Hinchcliffe [1971] 3 All ER 967) or "something out of the ordinary run of events" (Clarks of Hove Ltd v Bakers Union [1979] 1 All ER 152).

(2) HMRC's failure to consider special circumstances (or to have reached a flawed decision that special circumstances do not apply to a taxpayer) does not mean the decision to impose the penalty, in the first place, is flawed.

(3) Special circumstances do not have to be considered before the imposition of the penalty. HMRC can consider whether special circumstances apply at any time up to, and during, the hearing of the appeal before the Tribunal.

(4) The Tribunal may assess whether a special circumstances decision (if any) is flawed if it is considering an appeal against the amount of a penalty assessed on a taxpayer.

(5) The Tribunal should assess any decision (or failure to make one) in light of the principles applicable to judicial review.

(6) Failure to have considered the exercise of its discretion to reduce a penalty by virtue of special circumstances, in the first place, or failure to give reasons as to why, (if HMRC has made a decision), special circumstances do not apply, can render the "decision" flawed.

(7) We can allow the taxpayer's appeal if we find that HMRC's decision is unreasonable unless it is inevitable that HMRC would have come to the same decision on the evidence before him (as per Lord Justice Neill) (*John Dee Limited v Commissioners of Customs and Excise* 1995 STC 941).

> "I turn therefore to the second matter raised in the appeal, I can deal with this very shortly.
>
> It was conceded by Mr Engelhart, in my view rightly, that where it is shown that, had the additional material been taken into account, the decision would inevitably have been the same, a Tribunal can dismiss an appeal. In the present case, however, though in the final summary the Tribunal's decision was more emphatic, the crucial words in the Decision were:
>
>> "I find that it is most likely that, if the Commissioners had had regard to paragraph (iii) of the conclusion to Mr Ross' report, their concern for the protection of the revenue would probably have been fortified."
>
> I cannot equate a finding "that it is most likely" with a finding of inevitability.
>
> On this narrow ground I would dismiss the appeal."

(8) In deciding whether HMRC's decision was unreasonable, we should follow the approach summarised by Lord Greene MR in *Associated Provisional Picture Houses Limited v Wednesbury Corporation* [1948] 1 KB 223:

> "The court is entitled to investigate the action of the local authority with a view to seeing whether they have taken into account matters which they ought not to take into account, or, conversely, have refused to take into account or neglected to take into account matters which they ought to take into account. Once that question is answered in favour of the local authority, it may be still possible to say that, although the local authority have kept

within the four corners of the matters which they ought to consider, they have nevertheless come to a conclusion so unreasonable that no reasonable authority could ever have come to it."

(9) As Lady Hale has said in *Braganza v BP Shipping* [2015] UKSC 17 at [24], this test has two limbs:

"The first limb focuses on the decision-making process - whether the right matters have been taken into account in reaching the decision. The second focusses upon its outcome - whether even though the right things have been taken into account, the result is so outrageous that no reasonable decision-maker could have reached it. The latter is often used as a shorthand for the Wednesbury principle, but without necessarily excluding the former."

(10) Having undertaken that assessment:

(a) if the Tribunal considers the decision is flawed, it may itself consider whether there are special circumstances which could justify substituting it's decision for that of HMRC unless it considers that HMRC would inevitably have come to the same decision on the evidence before them.

(b) if the Tribunal considers that HMRC have properly exercised its discretion in relation to special circumstances, it cannot substitute its own decision for that of HMRC when considering by what amount, if any, it should reduce a penalty.

*The application of the foregoing principles to the facts in this case*

154. HMRC's notice of penalty assessment dated 24 January 2017 and penalty explanation letter dated 14 December 2016 do not appear to distinguish between the penalties which relate to the under declaration of output tax and the over recovered input tax. It is our view that there is a difference between the two.

*Output tax*

155. As regards the under declared output tax, it is our conclusion that In Tandem has submitted its returns carelessly but not deliberately.

156. The burden of establishing deliberate behaviour rests with HMRC. As can be seen from [138] and [139] above, this is a difficult burden to discharge. HMRC must show that the appellant knew that the output tax was due and, knowing that, still submitted the VAT returns without declaring that tax, intending HMRC to rely upon them. It is tantamount to fraud.

157. We found Mr Purkiss to be an honest and reliable witness. He was disarmingly frank about the VAT consequences of the arrangements; he readily accepted that if there was a VAT detriment to In Tandem by engaging in the arrangements with its customers, then In Tandem should face the consequences. He did not seek to tailor his evidence to better his VAT position.

158. It seems clear to us, notwithstanding comments made by Mr Golder to the contrary, that these arrangements were not designed to glean any illegal, immoral, or unconscionable VAT benefit for either In Tandem or its customers.

159. At the first hearing, in response to a question from the Tribunal, an HMRC officer appeared to accept that it was likely that the customers made taxable outputs. Mr Golder said, on the second day of the hearing, that that was speculation. But looking at the contracts and the nature of the businesses conducted by the customers, it seems to us to be a reasonable supposition.

160. So if In Tandem had correctly understood the VAT position and charged its customers VAT on the employee's wages, its customers might well have recovered that VAT. So no loss to HMRC.

161. Our finding that the wages are subject to VAT means that HMRC might receive a windfall. Output tax will now become due from In Tandem. That should be input tax in the hands of its customers provided In Tandem can recharge and invoice them for it. We understand that is practically unlikely.

162. But the point is that the strategy adopted by In Tandem and its customers may well have been VAT neutral for all parties had the VAT on the wages been properly charged.

163. This is a difficult and complicated area of VAT law as evidenced by the length and complexity of this decision and the fact that *Airtours* was decided on a majority in both the Supreme Court and the Court of Appeal. We do not think that In Tandem knew that VAT was due on the employee's wages and deliberately failed to report that in its tax returns.

164. We come to this conclusion notwithstanding Mr Golder's submissions. We accept that Mr Purkiss has been an officer of a number of companies. We also accept that he was an inspector of what was the Inland Revenue. We suspect that he has a working knowledge of VAT. But, as it is a complicated area of VAT law, we do not think that simply being a director of a number of companies with a working knowledge of VAT means that he knew that output tax was payable on the employees wages. As regards the failure to cooperate with HMRC, Mr Purkiss accepts this this was not In Tandem's finest hour. Nor indeed his. But we also agree with him that an examination of the facts shows that the position is more subtle than the picture painted by Mr Golder. The impact of Mr Davies sabotage was considerable. In our view the alleged non-cooperation by In Tandem does not show evidence of behaviour which is "tantamount to..... fraud".

165. We have the power to replace an allegation of deliberate behaviour with a finding of carelessness and we do so. Mr Purkiss' frankness about his naïveté regarding VAT does not protect In Tandem from having carelessly submitted the VAT returns as regards the failure to report the output tax. Mr Purkiss is an ex-Inland Revenue Inspector of taxes. If he was not sure about the VAT treatment of the arrangements with his customers, there was a wide variety of information available to him on professional and HMRC websites. He could readily have contacted HMRC to check on the VAT

position. He could have obtained specialist VAT advice. This was a substantial commercial venture. It was not one that either In Tandem or its customers had experience of. In these circumstances we would have expected a reasonable taxpayer in In Tandem's position to research the VAT position and to take specialist advice. It seems to us that In Tandem simply overlooked the VAT consequences of the arrangements until it was too late. The returns were submitted carelessly as regards the failure to report output tax on the employees wages.

*Input tax*

166. The position regarding the over recovered input tax is more difficult for In Tandem. We say this for two reasons. Firstly, as Mr Golder submits, there were no purchase invoices provided to In Tandem in respect of this input tax and In Tandem should have known that it could not recover the input tax without such invoices. Secondly In Tandem has readily conceded its claim for input tax. Whilst it has corrected the position by resubmitting corrective VAT returns, it should not have claimed recovery of input tax in the first place.

167. The input tax over recovery appears, oddly to our minds, to stem from the payments made to HMRC of the income tax and national insurance contributions on the employees wages. The justification for this set out in Mr Purkiss witness statement and In Tandem's statement of case was that the VAT returns submitted originally would "appear these were prepared using American sales software and, as a result, using American rules…….". And "examination of the bank records and invoices showed that mistakes had been made in the company's VAT returns which had been calculated on a "Gross out Gross in" basis as per US sales tax."

168. This explanation was not seriously challenged by Mr Golder at the February 2019 hearing. His focus was on the ostensible lack of cooperation by In Tandem with HMRC's enquiries and his submission that that lack of cooperation evidenced a realisation that it had deliberately incorrectly submitted its VAT returns.

169. We find this to be much more finely balanced than the position with the under declared output tax. Whilst the technicalities of that under declaration are complicated, valid recovery of input tax depends on a taxpayer having VAT invoices for that tax which In Tandem plainly did not have.

170. However, it is our view that HMRC have failed (but only just) to discharge their burden that the appellant knew that it was not entitled to claim the input tax in its returns yet still did so. We say this for the following reasons

(1) As noted above, although the history of interaction between In Tandem HMRC during the latter's enquiry was not In Tandem's finest hour, it can be justified by the explanations given by Mr Purkiss whose evidence we accept; namely that it was difficult to reconstitute the company's records following sabotage by Mr Davies; Mr Purkiss himself suffering from ill health; and his explanations regarding differences of interpretation put on various statements made by Mr Purkiss to HMRC.

(2) Mr Purkiss view, which we accept, was that initially he considered that the US software overstated the input tax recovery position but also overstated the output tax position so that HMRC should not have been worse off. We can understand why Mr Purkiss came to this view.

(3) Mr Golder has not mounted any serious challenge to the explanation given by Mr Purkiss regarding the application of the US sales software.

(4) Once it became clear to Mr Purkiss and to In Tandem, part of the ADR process, that the input tax had been over recovered, In Tandem submitted corrective VAT returns.

171. However, for the same reasons that we regard In Tandem's failure to properly account for output tax on the employees wages as being careless, we also find that In Tandem's VAT returns which identified that it was entitled to input tax recovery were submitted carelessly. If there was any doubt as to whether input tax was properly recoverable, In Tandem should have checked with HMRC or a professional adviser. It should also checked that the US sales software was appropriate for UK tax (and in particular VAT) returns. It does not appear that they undertook any such checks.

*Discount*

172. In the calculation of the penalties, HMRC have given a discount of just 5% to In Tandem. They have given no discount for telling, 5% for helping and no discount for giving. They justify this on the basis that In Tandem has refused to admit that there was any error in their returns, no help had been given to quantify the inaccuracies (but one meeting has been attended) and no records were produced to support company trading.

173. The appellant considers that a greater discount should be applied to the penalties. We do not agree. It would have been difficult for in Tandem to admit that there was an error in the face of its assertion that no tax was due on the employees wages. We also accept that little information, or little substantive information, was supplied by In Tandem to HMRC during the course of their enquiry. Mr Purkiss' justification for this was that HMRC had the names of the clients and In Tandem's bank statements and thus had all information relevant to In Tandem's business model. But it is our view that as a matter of fact, few records were made available by In Tandem to HMRC. We accept Mr Purkiss' justification for this regarding the sabotage by Mr Davies. And that means that he was not able to provide the records. But as far as discount for penalties is concerned, the truth of the matter was that no, or no worthwhile, records were produced by In Tandem to HMRC.

174. HMRC's penalties have been calculated on the basis of prompted disclosure and we agree with this analysis. But our finding that the penalties result from careless rather than deliberate behaviour means that the penalty range is not between 70% and 35% (which it is a deliberate behaviour) but is between 30% and 15%.

*Special circumstances*

175. We have set out at [152] and [153] above the legal principles which applies to

special circumstances.

176. If, as we have in this case, we substitute our decision on the penalties for that originally made by HMRC, we can also then reduce those penalties further if we consider that there are special circumstances, but only if HMRC's decision not to reduce the penalties for special circumstances, was flawed.

177. In their penalty explanation letter of 14 December 2016 HMRC state that "based on the information we have, we do not consider there are any special circumstances which would lead us to further reduce the penalty."

178. Furthermore, in response to a request from the Tribunal regarding the reasons for this decision, Mr Golder indicated that "HMRC can find no document to explain its decision regarding a reduction penalty because of special circumstances. I am advised that HMRC merely considered that no special circumstances were identified and that a reduction was not therefore considered to be appropriate."

179. It is our view that there are special circumstances in this case. The sabotage perpetrated by Mr Davies on In Tandem's records is something which is clearly out of the ordinary run of events. It is something which HMRC should have taken into account when considering special circumstances. They did not do so. Furthermore they have not given any reasons as to why they did not do so.

180. In our view this renders HMRC's decision not to reduce the penalties for special circumstances, flawed, and so we can consider whether the penalties should be further reduced for special circumstances. It is our view that they should be.

181. In Tandem does not appear to use the sabotage by Mr Davies as justification for incorrectly completing its VAT returns. However it is used as justification for failure to provide HMRC with the records sought by HMRC. It is HMRC's view that this failure means that no reduction should be applied to the penalties for giving since no records were produced by the company. As a matter of fact, this is correct. And so HMRC's failure to allow a deduction for giving is also correct.

182. But given that this arises from the special circumstances mentioned above, it is our decision that a further discount of 20% should be applied to the reduction of the penalties for disclosure, to reflect those special circumstances.

*Conclusion on the penalties*

183. It is our conclusion therefore that the penalties are a result of careless not deliberate behaviour, and that the percentage of the potential lost revenue which should be applied to calculate the penalties is not 68.25% as used by HMRC in their penalty assessments, but is 26.25% to reflect special circumstances.

## Decision

184. For the reasons given above, it is our decision that:

(1) The appellant's appeal against the assessments is dismissed.

(2) Its appeal against penalties for submitting deliberately inaccurate VAT returns which understated its liability to pay output tax is allowed.

(3) Its appeal against penalties for submitting deliberately inaccurate VAT returns which overstated its right to recover input tax is allowed but we have decided that such returns were submitted carelessly. We have therefore reduced those penalties taking into account our view that special circumstances apply.

## Appeal rights

185. 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.

**NIGEL POPPLEWELL**

**TRIBUNAL JUDGE**

**RELEASE DATE: 8 October 2019**