TC04163

Appeal number: TC/2013/05026

VAT – assessment to recover input tax claimed in respect of supplies for which no payment made within six months of relevant date – s 26A VATA – whether such payment had been made – no – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

HEANOR MOTOR COMPANY LTD **Appellant**

-and-

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

TRIBUNAL: JUDGE KEVIN POOLE
MR RICHARD LAW FCA

Sitting in public at Priory Court, Birmingham on 12 November 2014

John Hamilton FCA for the Appellant

Joshua Shields of counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This decision relates to an assessment issued by HMRC pursuant to section 26A Value Added Tax Act 1994 ("VATA") to recover input tax which had been claimed by the appellant in respect of supplies made to it by an associated company pursuant to a property lease, in a situation where HMRC were not satisfied that the consideration for those supplies had in fact been paid by the appellant before the end of six months after the "relevant date" specified in section 26A VATA.

The facts

2. We received a witness statement from Officer Russell White of HMRC and a short statement described as an "affidavit" from Mr Hamilton, the appellant's accountant. We also heard oral testimony from both of them and from Mr Zahir Malik, the Managing Director of the appellant. Finally, we were provided with a bundle of documents.

3. Based on this evidence, we find the following facts.

4. Mr Zahir Malik ("ZM") established the appellant as a business for his younger brother Nasar Malik in about 2000. He provided much of the finance for it by means of a loan account. It carried on business as a motor dealer.

5. The business did not prosper and was consistently loss making. In September 2010, the appellant ceased to trade.

6. ZM also had another much larger company, Resurrection Developments Limited ("RDL"). He funded that company in a similar way (by loan finance, on director's loan account). That company was a property developer. RDL went into liquidation in September 2010.

7. RDL had owned the property used as the business premises of the appellant. There was apparently a lease entered into in about 2004 between the two companies, regulating the appellant's occupation of the premises. No copy of that lease was before us.

8. We were told that the lease provided for the appellant to pay rent to RDL in respect of its occupation of the premises. There was no evidence before us as to the amount of rent provided for in the lease (beyond the amounts of the invoices referred to below). It seems however that RDL had elected to waive exemption from VAT in relation to the property in question, as a result of which the rent carried VAT.

9. Mr Hamilton, the appellant's accountant, had no knowledge of this lease until some time in 2011. Accounts for the appellant had been prepared without any reference to a rental expense, though ZM maintained that the expense may well have been included in the overall "purchases" figures in the various accounts.

10. After the appellant's business had been closed down and RDL had gone into liquidation, ZM decided he needed to "tidy up" the affairs of the appellant. He gave evidence that whilst he was going through the records of the appellant, he came across some old invoices for rent that had been received from RDL which included VAT which had never been claimed by the appellant as input tax. He claimed to have contacted HMRC's helpline to ask about what he should do, and was told that as the VAT registration of the appellant was still extant, he could reclaim the VAT as input tax on a final VAT return, but only in relation to supplies that were less than four years old. At another point, he claimed to have been given that advice by his VAT advisers, The VAT People. Mr Hamilton was not involved.

11. In any event, in early January 2012 he submitted a VAT return for the appellant in respect of the three month period ended 31 December 2011, in which he claimed input VAT of £10,397.50 in respect of the VAT charged on property rent over the period since 1 March 2008. This was the only entry on the VAT return, so the return itself generated a repayment claim of that amount.

12. HMRC arranged to visit the appellant to verify the repayment claim, and the visit took place on 1 February 2012. ZM told Mr White (the visiting officer) that the rental invoices had come to light when Mr Hamilton was checking the appellant's records.

13. Following the meeting, Mr White wrote to the appellant, requesting copies of the appellant's bank statements to confirm that the rental payments had been made. In reply, Mr Hamilton wrote on 22 February 2012, saying that the invoices had "come to light" after the accounts for the year ended 31 December 2010 had been completed, and they would be reflected in the 2011 accounts, which were "currently being prepared". He went on to say that "as the Company did not have sufficient funds to pay any of these invoices, the amounts have been cleared by crediting the Directors Current Account which at the beginning of the accounting period stood at £220,362."

14. Officer White asked, in a letter dated 28 February 2012, for a copy of ZM's loan account with the appellant showing the credit entry, and "evidence that payment from Mr Malik was actually made to Resurrection Developments Limited".

15. In reply, in his letter dated 10 April 2012, Mr Hamilton said that "the accounting entries in the books of Heanor Motor Company Limited will be made in the accounting period to 31 December 2011 however these Accounts have not been completed." He went on to say that "the reverse entries in the books of Resurrection Developments Limited would have been made after 31 July 2009. The balance showing to the credit of the Directors Current Account of Mr Z Malik as at 31 July 2009 as shown in the accounts, was £448,897 which is sufficient to cover these costs."

16. After a further inconclusive exchange of correspondence, the appellant appointed The VAT People to advise. In their letter dated 17 May 2012, they asked Mr White, in view of the liquidation of RDL, to contact the liquidator himself to obtain details of whether RDL had accounted for output tax on the rent invoices.

They provided what purported to be a copy of "a journal entry made showing netting off in the accounts of the transaction". This journal entry only showed that the amount of the rent (including VAT) was to be credited to ZM's loan account in the accounts for 2011. It included the note: "To account for the rent not charged by the landlord for the period from 1st March 2008 to 31 August 2010".

17. Mr White contacted the liquidators of RDL and reviewed the records they held. He could find no evidence to show that any output tax had been charged or accounted for by RDL in connection with the invoices that had been raised. He also checked the VAT returns of RDL over the relevant periods and found that "in many of the periods when output tax should have been accounted for on rental supplies there was either no output tax or insufficient output tax declared to cover the supplies." He informed the appellant of this in his letter dated 12 July 2012.

18. In his letter dated 27 November 2012, Mr White asked The VAT People why the appellant's accounts for 2007 and 2008 contained no reference to any rent expense. In reply, they said that "it was decided between the two companies that HMC was not charged rent by RDL as HMC's trading position was poor". It was only when RDL's own trading position worsened that the rental charge was reinstated, "and can be seen in the accounts".

19. Mr White remained unsatisfied that the VAT on the rental invoices had been paid by the appellant, and the attempts of The VAT People to persuade him that this had been achieved by means of the accounting entries were unsuccessful.

20. Before us, ZM gave evidence that he believed the rental invoices had actually been paid (rather than being settled through a set of accounting entries). He had no evidence to support that assertion, however, nor did he have any evidence that RDL's accounting records showed either the issuing of the rental invoices or receipt of payment for them.

21. We found ZM to be an unreliable witness of fact. Even during the hearing his account of certain matters changed (see [10] above) and his only explanation for the fact that The VAT People had given an explanation that was entirely inconsistent with his own was that they had "got it wrong". Having seen him give evidence, we do not accept this.

22. It is not necessary for us to determine whether the invoices in question were fabricated by ZM, as may have been implied in some of the submissions before us. All that is necessary is for us to determine whether the consideration for the supplies they represent was paid by the appellant within the appropriate period.

23. We find that no actual payment was made by the appellant to RDL in respect of the invoices. When ZM presented them to Mr Hamilton, he did his best to incorporate them into the 2011 accounts which he was in the course of preparing, and as the appellant had no funds to pay the invoices, they were "cleared" by crediting them to ZM's loan account (increasing the amount owed to him by the appellant on his loan account by a corresponding sum).

24. Eventually, Mr White wrote to the appellant on 18 June 2013, notifying it that HMRC had raised an assessment in respect of VAT accounting period 06/12 to recover the input tax wrongly claimed in period 12/11. This decision was upheld by statutory review issued on 26 July 2013 and the appellant appealed to the Tribunal by notice of appeal dated 31 July 2013.

The law

25. There was no dispute about the law. The relevant provision is section 26A VATA which provides, so far as relevant, as follows:

> "**26A – Disallowance of input tax where consideration not paid**
>
> (1) Where –
>
> (a) a person has become entitled to credit for any input tax, and
>
> (b) the consideration for the supply to which that input tax relates, or any part of it, is unpaid at the end of the period of six months from the relevant date,
>
> he shall be taken, as from the end of that period, not to have been entitled to credit for input tax in respect of the VAT that is referable to the unpaid consideration or part.
>
> (2) For the purposes of subsection (1) above, "the relevant date", in relation to any sum representing consideration for a supply, is –
>
> (a) the date of the supply, or
>
> (b) if later, the date on which the sum became payable."

Discussion and conclusion

26. In the letter dated 17 May 2012 referred to at [16] above, the appellant's advisers made it clear that the accounting entries which they claimed to amount to "payment" of the rent had already happened prior to that time. The making of those entries obviously implies it was accepted that the sums in question were due for payment by the time the entries were made.

27. There is no evidence to support ZM's assertion that the invoices might have been actually paid at the time they were supposedly issued in 2008-2010, and we have found that the appellant did not at any stage make actual payment of the rent in respect of which it has claimed the input tax (see paragraph [23] above).

28. We find that the making of an internal entry of the type referred to in that paragraph in the accounts of the appellant without the agreement of the creditor (RDL) cannot amount to "payment". Clearly RDL did not give such agreement, as it was by then under the control of its liquidators, who knew nothing of the "debt".

29. It follows that by 18 June 2013 (the date on which HMRC notified the appellant it had raised the assessment) the consideration for the supply to which the claimed input tax relates had clearly remained unpaid at the end of the period of six months after the "relevant date".

30. The appellant is not therefore entitled to credit for the input tax comprised in the rental invoices and HMRC were correct to raise the assessment that they did to recover that input VAT.

31. The appeal must therefore be dismissed.

32. 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.

KEVIN POOLE
TRIBUNAL JUDGE

RELEASE DATE: 2 December 2014