



Neutral Citation: [2023] UKFTT 747 (TC)

Case Number: TC08927

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

Birmingham

Appeal reference: TC/2021/02722

*VAT – input tax – whether appellant making taxable supplies despite delays in pursuing debts
– yes – appeal upheld*

Heard on: 16 February 2023

Judgment date: 01 September 2023

Before

**TRIBUNAL JUDGE ANNE FAIRPO
DEREK ROBERTSON**

Between

HEARTLANDS HOUSE LIMITED

Appellant

and

THE COMMISSIONERS FOR HIS MAJESTY’S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Mr Edwards of MHA MacIntyre Hudson LLP

For the Respondents: Ms Gordon, litigator of HM Revenue and Customs’ Solicitor’s Office

DECISION

Introduction

1. This is an appeal against a decision by HMRC to disallow three input tax repayment claims submitted by the appellant for the VAT periods 09/19, 06/20 and 09/20. The input tax repayment was refused as HMRC considered that the appellant had not provided sufficient evidence to support the claim that it had made or had the intention to make taxable supplies.
2. The appellant accepted that the assessments for 06/20 and 09/20 were correct, as the VAT had been claimed in error in respect of purchases relating to exempt supplies. The dispute for this Tribunal to consider was the 09/19 assessment for a total of £28,221.96.
3. The production of this decision was delayed by administrative problems relating to the provision of the appellant's skeleton argument, which had not been made available to the panel before the hearing and was not located by the administration centre until some considerable time later.

Background

4. The appellant is a company in the construction sector. The company secures projects and then uses subcontractors to carry out the works.
5. The company registered for VAT in October 2018, with the registration backdated to 9 June 2016, following advice from new accountants. The first period VAT return, for the period 09/19, was selected for verification by HMRC as were the returns for the periods 06/20 and 09/20. All three returns were repayment claims. Mr Rehman explained that the change of accountants was because the previous accountants had failed to register the company for VAT and CIS, despite telling the directors that the registrations had been made.
6. The company engaged in four projects in the period under appeal; it was the input VAT reclaimed in respect of three of these which led to the assessment.

Project 1 - RPH Developments

7. This 2016 project was the construction of a double storey extension to a residential property. The appellant was contracted by RPH Developments to do the work and in turn contracted with Caihma Construction Limited to deliver the work.

Project 2 - Offices for the appellant

8. The appellant contracted with Caihma Construction Limited to construct offices for its own use during 2018.

Project 3 - Countrywide Estate Partnership

9. This 2018 project was for the internal refurbishment of commercial premises. The appellant was contracted by Countrywide Estates and again contracted with Caihma Construction Limited to carry out the works.

Project 4 – not undertaken

10. A contract for a further project, for a company described on the tender document as Easy Décor Limited, was entered into in August 2019 but no work was undertaken in respect of this project as it was put on hold and then further delayed by the coronavirus pandemic. HMRC noted that no such company existed on Companies House but also noted in correspondence that the name may contain a typographical error. The appellant noted in the hearing that there was such an error and the company was listed at Companies House as EasyDecors Limited.

Appellant evidence

11. We heard evidence from a director of the appellant, Mr Rehman, who had previously developed properties on his own account. His role in the business was to secure work and source contractors to carry out the work. Mr Rehman had originally been a shareholder but not a director of the appellant. The company had previously had another director, Mr Chand, who was no longer with the business. Mr Rehman became a director when Mr Chand resigned in 2018. Mr Chand had been more involved in the day to day management of projects and workers as he had more construction experience.

12. Documents in respect of each of the projects were provided as follows.

Project 1 - RPH

13. The project opportunity came from a contact of Mr Chand, a director of the appellant at the time. The tender proposal was signed by Mr Chand and RPH Developments, dated 4 September 2016. This was considered to be the contract for works. The total contract fee was £67,750 (excluding VAT).

14. Two stages of the contract were completed by 2 April 2017. The contract fees for these were £19,375 and £10,416.25 (excluding VAT).

15. The subcontractor, Caihma Construction Limited, issued invoices for work done on this project as follows:

- (1) £15,500 (plus VAT) on 16 October 2016
- (2) £8,333 (plus VAT) on 16 March 2017

16. The appellant issued documents each marked as “pro forma invoice” to RPH Developments on 1 November 2016, for £19,375 plus VAT and on 2 April 2017, for £10,416.25 plus VAT. Mr Rehman understood that these were invoices, and was not aware that the words “pro forma” had any particular meaning.

17. These amounts were not paid. The appellant continued to work on the project for a while despite the lack of payment because they did not want to lose workers to another project, as it might be difficult to get them back. It was a calculated risk to pay the subcontractor whilst waiting for the client to pay. The client had explained that they had cashflow issues.

18. Mr Rehman explained that they had spoken to the client and received assurances of payment. He had trusted that the payments would be made, as he had invested a lot of personal money in the business. Eventually, the appellant ceased work on the project because the client ceased to respond to attempts to communicate and obtain payment.

19. Although they had an address for the client, it was a large office block that acted as an accommodation address for many businesses and they were unable to contact the client. Mr Rehman agreed that the statutory demand for payment was issued only after the HMRC enquiry commenced. He had never previously had to issue a statutory demand, He had eventually found someone who knew the client and acted as an intermediary to reach a settlement. Having taken legal advice, Mr Rehman had concluded that it was best to cut their losses and take what was available.

20. A statutory demand for £35,749.50 was served on RPH Developments on 27 November 2020. An invoice for £6,600 (£5,500 plus VAT) was raised by the appellant on 22 September 2021 with a settlement date of the same date. The VAT in respect of this invoice was accounted for in the appellant’s 09/21 VAT return.

Project 2 - offices for the appellant

21. Caihma Construction Limited issued an invoice to the appellant for work done on this project for £28,250 (plus VAT) on 6 February 2018. Payments were made in various tranches to Caihma Construction Ltd for this invoice. The project was completed around July/August 2018.

Project 3 - Countrywide

22. The tender proposal signed by Mr Rehman and Countrywide Estate Partnership, dated 21 September 2018 with a start date of 1 October 2018. This was considered to be the contract for works, with a total fee of £73,600 (excluding VAT).

23. The project was to take place in four stages with a stage payment for each stage. A number of snagging issues arose on the project which needed to be resolved before the client was prepared to release payment. In the event, only the first two stages were undertaken. The contract fees for these two stages were £15,750 and £35,050 (excluding VAT).

24. Caihma Construction Limited issued invoices to the appellant for work done on this project as follows:

- (1) £13,333 (plus VAT) on 2 October 2018 (for site setup and materials)
- (2) £29,208 (plus VAT) on 19 November 2018

25. The client complained that the workmanship was inadequate, although Mr Rehman thought that this was an excuse to delay payment, Caihma had agreed to rectify the problems and undertook remedial works, which Mr Rehman thought had resolved the issues, but the client continued to raise more issues. The appellant eventually ceased work on the project because they had paid Caihma but the client continued to refuse to pay.

26. Mr Rehman could not recall whether any invoices had been issued to Caihma but stated that if no invoices had been provided then it was likely that none had been raised.

27. Having taken legal advice, a settlement was eventually reached on 10 November 2020 under which Countrywide paid an amount of £9,250 on 11 November 2020, on completion of a deed of termination in respect of the contract. Mr Rehman agreed that this was after HMRC had refused the input tax claims and explained that he had initially been trying to get Caihma back to do more remedial works, and then had been trying to discuss payment with the client. The pandemic had also complicated matters. The output tax for this amount was accounted for in the appellant's 12/20 VAT return.

Project 4

28. Mr Rehman explained that this project had never started; even after the pandemic delays, no work had been done on it and the appellant was no longer expecting to do any work on it.

Suppliers & purchases

29. The appellant stated in correspondence that they carried out due diligence on trading partners, checking VAT numbers and incorporation certificates. Bank details were obtained and websites and letterhead checked. The directors met with the suppliers.

30. The main supplier, Caihma Construction Limited (Caihma), had been engaged by a previous director of the appellant (Mr Chand). Mr Rehman said that he had not checked the Companies House records for Caihma, but the company name indicated that it was a construction firm and the workers appeared to know what they were doing. Mr Rehman thought that there would have been contracts with Caihma for the work subcontracted to them, but he did not remember any details. Caihma was dissolved in September 2019 by compulsory strike off. It filed no corporation tax or VAT returns with HMRC.

31. The appellant also claimed VAT in respect of purchases from other suppliers, including the following during 2019:

- (1) Pass & Co: for plastering and skimming
- (2) Truvision Fire & Security: for alarm and fire systems
- (3) Bifolds 4 U Ltd: double glazing windows and doors

32. The appellant purchased goods from Camber Best, a builders merchant. Fees were paid to an architect, Lever Turner & Cowdell in 2018. The appellant's bank statement also showed payments to this firm in 2019. The bank statements also showed payments to other construction suppliers.

33. In correspondence, the appellant confirmed that it had no connection to any of the suppliers. This was not challenged by HMRC.

Appellant submissions

34. The appellant contended that it had provided clear evidence of taxable supplies, in particular the tenders in respect of the work carried out which were signed as contracts, and it was also clear from the invoices and bank statements that the input tax had been incurred in respect of those supplies.

35. Caihma's tax compliance failures were not relevant to the input tax claim unless HMRC were raising a Kittel argument, which needed to be specifically pleaded and no such argument had been raised or in any way put to Mr Rehman. Further, over 30% of the amount in dispute related to purchases from construction-related suppliers other than Caihma.

HMRC evidence and submissions

36. Officer Holder provided evidence, adopting the witness statement of an earlier HMRC officer. Officer Holder could not see that there was any real evidence of taxable supplies having been made in the period covered by the first VAT return, as there had been no demand for payment and could not see that any payments made by the appellant were connected to taxable supplies. HMRC would have expected invoices to be raised earlier.

37. HMRC submitted that the appellant had provided insufficient evidence of taxable supplies. The pro forma invoices issued in respect of Project 1 did not correlate to invoices from Caihma, and they considered that it would be reasonable to expect that the invoice to the client would reflect the work done. Further, HMRC contended that there was no planning permission for some of the projects and no correspondence or invoices that would make it clear what the clients were paying for.

38. HMRC further contended that it was not credible that the appellant undertook several stages of work for clients without being paid. There was no evidence of reasonable steps being taken to pursue payment until after HMRC had issued their decision to refuse the input tax claim.

39. HMRC also considered that the lack of information available with regard to Caihma cast doubt on the appellant's evidence, as almost 68% of the input tax claimed related to Caihma. They submitted that it was reasonable to expect that due diligence would have been undertaken. HMRC further contended that the failure of the appellant to register for CIS, even though it was acting as a contractor, cast doubt on the validity of the claims as the payments to Caihma were not declared through CIS returns.

Relevant law

40. s26(1) VAT Act (VATA) 1994 states that the amount of input tax for which a taxable person is entitled to credit at the end of any period is so much of the input tax for the period as

is allowable by or under regulations as being attributable to taxable supplies made by that person.

Discussion

41. HMRC did not dispute that the purchases had been made, and the VAT incurred, nor contend that the appellant did not the necessary evidence to support deductions. The question for us was whether the purchases had been made in connection with actual or intended taxable supplies.

42. We find that the appellant provided clear evidence of payments to a number of suppliers in connection with construction, and also provided contracts under which it was engaged for three construction projects, one of which did not proceed. The other project was for its own offices, to be used in making taxable supplies. The suppliers had no connection to the appellants, nor was there any submission that the engager clients in the construction projects were connected to the appellant. Although a substantial proportion of the VAT reclaimed related to purchases from Caihma, over 30% was not so related.

43. HMRC's contention that the invoices raised for Project 1 did not reflect the work done, as they did not correlate to the invoices from Caihma at the relevant dates, appears to us to overlook the fact that the invoices are for the amounts agreed in the contract to be the relevant stage payments. Even if work had been accelerated, it is unlikely that the client would have expected the invoice to be for anything other than the agreed stage amount.

44. HMRC also noted that the appellant was not referred to in planning permission documents where these existed. HMRC did not explain why the appellant (which was not the architect or even the main contractor) should be referred to in planning documents which were submitted some time before they were engaged. We do not consider that lack of reference to the appellant in the planning documents has any relevance to the question of whether the appellant was making taxable supplies. The lack of provided planning documents in respect of other projects also does not mean that the appellant was not intending to, or making, taxable supplies.

45. Both RPH and Countrywide eventually made payments to the appellant, albeit for amounts which were considerably less than the project fees contracted for. The delays in pursuing enforcement no doubt contributed to that. We consider that it is not credible that either of these companies would have made any payments and entered into a deed of termination in the case of Countrywide, if no supplies at all had been made to them by the appellant. Indeed, we consider that, having entered into contracts with the appellant, the clients would have been more likely to have sued the appellant for breach of contract if they had failed to even attempt to make the supplies contracted for as they would have needed to engage other providers.

46. Given that it was accepted that the appellant had made the purchases and incurred the VAT claimed, and HMRC did not contend that the appellant and its clients were involved in any failures on the part of Caihma, we are puzzled as to why HMRC continued to consider that the appellant would have incurred construction-related costs and why the appellant and its clients would have entered into construction contracts if the appellant did not intend to make taxable supplies.

47. Whilst there was undoubtedly poor management of the business in failing to ensure that it was registered for CIS and VAT at the appropriate time, in taking far longer than it should have done to take steps to enforce payment amid misplaced optimism that the clients would pay without legal action, in possibly failing to raise invoices at all in respect of Countrywide, and in failing to understand that a pro forma invoice is not the same as a stage payment invoice,

that is not enough to outweigh the evidence above that supplies were made. Poor management does not mean that there was any lack of intention to make taxable supplies.

48. In correspondence during the enquiry, an HMRC internal email noted that “concerns still exist on the overall credibility of the company and the missing supplier links for output tax which indicates towards potential VAT fraud”. HMRC did not allege in these proceedings that the appellant knew or should have known that Caihma were a defaulting trader. It was accepted, and we so find, that there was no connection between the appellant and Caihma or, indeed, the other suppliers and clients. HMRC submitted that the appellant should have undertaken due diligence on Caihma, although it did not make the same submissions with regard to other suppliers, and that the lack of information available in respect of Caihma cast doubt on the appellant’s evidence.

49. We consider that a failure to undertake rigorous due diligence is not sufficient evidence of a lack of intention to make taxable supplies. Any such failure is consistent with the general poor management of the appellant business but does not mean that the appellant’s evidence should be discounted, and we found Mr Rehman to be a reliable witness.

50. We consider that the appellant has provided sufficient evidence of an intention to make taxable supplies and in fact provided evidence that it did make supplies (albeit that the projects were not necessarily completed).

Decision

51. We consider that the appellant has provided sufficient evidence of an intention to make taxable supplies and in fact provided evidence that it did make supplies (albeit that the projects were not necessarily completed).

52. The appeal is therefore upheld.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

53. 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.

**ANNE FAIRPO
TRIBUNAL JUDGE**

Release date: 01st SEPTEMBER 2023