[2016] UKFTT 291 (TC)

TC05064

Appeal number: TC/2012/09668

VALUE ADDED TAX – assessment – whether reason to assess trader – yes – whether any evidence to justify amendment of assessment – no – misdeclaration penalty: whether affected by other penalty assessment under Sch 24 FA 2007 – no – held, misdeclaration penalty properly imposed and no reason to adjust – Sch 24 penalty: held, invalid as expressed to cover period before legislation took effect – Direction under para 2 Sch 1 VATA 1994 that businesses to be treated as carrying on single business for VAT purposes: whether HMRC decision unreasonable – no – appeals dismissed but appeal against Sch 24 penalty allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

THE GRAND FOLKESTONE LIMITED (1)

THE GRAND FOLKESTONE (2) **Appellants**

- and -

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

TRIBUNAL: JUDGE JOHN CLARK
CLAIRE HOWELL

Sitting in public at The Royal Courts of Justice on 11 and 12 February 2016

Timothy Brown of Counsel, for the Appellants

Rita Pavely, Officer of HM Revenue and Customs, for the Respondents

DECISION

1. The Appellants appeal against the following decisions made by the Respondents ("HMRC") in relation to VAT:

(1) The decision to assess The Grand Folkestone Ltd ("TGF") in respect of under-declared output tax for the period from 1 April 2008 to 31 December 2011 inclusive, in the sum of £110,360.00 plus interest;

(2) The decision to issue a penalty under Schedule 24 to the Finance Act 2007 ("FA 2007") in the sum of £18,717.25;

(3) Subject to the granting of permission to make a late appeal, the decision to issue a misdeclaration penalty under s 63 of the Value Added Tax Act 1994 ("VATA 1994") in respect of periods 06/08 and 09/08 in the total sum of £5,188;

(4) The decision to issue a Notice of Direction under para 2 Sch 1 VATA 1994 that certain specified businesses trading from The Grand Folkestone are a single entity for VAT purposes, resulting in The Grand Folkestone being registered for VAT with effect from 11 July 2013.

The background facts

2. The evidence consisted of two bundles of documents. These included witness statements given for the Appellants by Ewa Kobylarz, Doris Stainer and Michael Stainer, and for HMRC by Paul Darler, an Officer of HMRC. All the witnesses gave oral evidence.

3. From the evidence we find the following background facts. We consider disputed matters in a later section of this Decision.

4. The premises known as The Grand Folkestone are situated on the sea front at Folkestone. They were built in the late 19th century as "gentlemen's residential chambers".

5. The freehold of the premises is owned by a company, Hallam Estates Limited.

6. Currently, and at the times relevant to this appeal, the premises are and were not licensed as a hotel. Various services are provided at the premises. There are four restaurants, cafes and bars. There are function rooms for events, including weddings. Entertainments are provided. In addition to the public rooms there are 117 apartments, of which 40 have yet to be refurbished. Short-term accommodation is provided in 18 apartments on a per day basis, for short breaks, per week or for longer. Other apartments are available on a long-term basis, and garages are available for rent.

7. The services are provided by a number of different entities. The one current entity originally registered for VAT was TGF. Its effective date of registration was 1

April 2007, following its application for registration made on 29 December 2006; this was received by HMRC on 3 January 2007.

8. Following a separate enquiry by HMRC in respect of PAYE relating to persons employed at the premises, ultimately leading to the recently released decision of the First-tier Tribunal in the appeal of *Grand UK Limited and others v Revenue and Customs Commissioners* [2016] UKFTT 0138 (TC), TC 04924, Mr Darler was asked to review the VAT position. He and another officer visited the premises on 9 May 2011, and he alone made a further visit on 19 July 2011.

9. As a result of his consideration of the records, Mr Darler concluded that the VAT returns for the periods 06/08 to 12/11 were incorrect. On 28 February 2012 he wrote to Mr Stainer to inform him of the outcome of the review of the VAT position of TGF and the other entities operating at The Grand Folkestone.

10. He indicated that he had concluded that there was a single business of a hotel-type establishment at The Grand. He stated that he had issued Notices of Direction to TGF, Kentish Cuisine Ltd, Keppels Cuisine Ltd, Grand UK Ltd and Mr and Mrs Stainer operating as a partnership. This meant that from the date directed in the Notices, the activities of these entities would be treated as a single business for VAT purposes and a new VAT registration would be set up. The existing registration would be cancelled. (Those Notices were issued to the relevant parties on 21 February 2012, from HMRC's Grimsby office.)

11. He referred to VAT liabilities up to that date for three of these traders. He then raised the question whether the returns for TGF were correct. He indicated that in his view they fell short in a number of respects, and explained these in further detail. This meant that output tax had been under-declared; for the sake of equity, input tax also needed to be re-calculated on a pro rata basis.

12. On 28 February 2012 Mr Darler wrote to TGF to inform it that on consideration of all the information provided to him during his visits and subsequently, he intended to issue an assessment for £125,430 output tax under-declared and taking account of £15,070 input tax under-claimed. He explained the basis for his calculations. A formal Notice of Assessment gave details, including allocations of under- and over-declarations to the respective periods covered by the assessment.

13. On 15 March 2012 Mr Darler wrote to TGF giving details of the penalty which HMRC intended to charge it; this was a grouped inaccuracy penalty under Sch 24 FA 2007. A penalty explanation schedule was attached.

14. In a letter dated 21 March 2012 Mr Stainer wrote to Mr Darler mentioning the notice of assessment and indicating that a review was being requested.

15. On 29 March 2012 another HMRC Officer, Mrs Castle, wrote to TGF on Mr Darler's behalf to notify it that HMRC had assessed it to a misdeclaration penalty of £5,188.

16. On 2 April 2012 HMRC sent TGF a further notification relating to the proposed penalty under Sch 24 FA 2007.

17. On 2 May 2012 Mr Stainer wrote to Mr Darler questioning the basis on which the proposed penalty was to be charged. Mr Darler acknowledged this on 9 May 2012 and stated that the penalty would be reconsidered in the light of Mr Stainer's comments. Mr Darler also asked Mr Stainer to state which type of review was being requested and which findings he wished to be reviewed. The review could relate to the Notices of Direction, or the assessment on TGF, or both.

18. According to Mr Darler's witness statement, the Notices of Direction (referred to by him as the "Notices of Decision") were reissued to the same entities on 11 May 2012 following amendment of the registered entity's name. No copies of those reissued Notices were included in the evidence before us. Despite this, we accept Mr Darler's evidence that the Notices were reissued on that date, in particular because the later review letter refers to the registration date of the registered entity as 11 June 2012, which was exactly one month after the reissue of the Notices. We have no direct evidence of the name of the registered entity as at that point.

19. On 11 July 2012 Mrs Reid, the HMRC Review Officer dealing with the requested review, sent an email to Mr Stainer following a telephone conversation concerning what was to be reviewed and the question of allowing an extension of time for the statutory review. On 18 July 2012 Mr Stainer emailed Mrs Reid; TGF's solicitors had advised that HMRC's request for extension of time for the statutory review should be granted.

20. On 14 August 2012 Mrs Reid wrote to TGF with the conclusions of her review. This review did not relate to penalties, as TGF had not requested a review of the misdeclaration penalty notified on 29 March 2012, and no penalty had been issued under Sch 24 FA 2007.

21. In relation to the Notices of Direction, she considered that further information was required to ascertain the relationships between the various entities. Consequently, she proposed to withdraw the present decision and Notices and to refer the case back to Mr Darler to arrange a meeting with TGF in order to make the relevant enquiries.

22. In relation to the assessment made by Mr Darler on TGF, her decision was that this should be upheld in full.

23. On 18 October 2012, TGF gave Notice of Appeal to HM Courts & Tribunals Service ("HMCTS"). The Notice referred to the amount of £110,360 assessed on TGF and also to the penalty under Sch 24 FA 2007 in the amount of £69,526.80 which HMRC had proposed in their penalty explanation schedule issued on 14 September 2012. (We note that at that point no assessment had been made on TGF in respect of the latter penalty, which raises a jurisdictional question considered later in this decision.)

24. Following the decision in Mrs Reid's review letter that the Notices of Direction should be withdrawn and that further enquiries were necessary, Mr Darler had written

to three individuals asking for a meeting. As he received no replies to these requests, on 17 October 2012 he wrote letters to Mrs Stainer and to Ramesh Pappuraj Babu (at that time a director of Keppels Cuisine Ltd and Grand-UK Ltd) at The Grand enclosing questionnaires.

25. On 26 October 2012 HMRC issued a notice of penalty assessment to TGF. The amount of the penalty under Sch 24 FA 2007 was £69,526.00.

26. Following correspondence, on 11 November 2012, HMRC wrote to TGF accepting that it would suffer hardship if it were required to pay the tax in dispute before its appeal was heard by the Tribunal.

27. On 29 January 2013, HMRC withdrew their Notices of Direction as proposed by Mrs Reid in her review decision.

28. HMRC made an erroneous application for the appeal to be struck out, leading to it being allowed, but subsequently successfully applied for reinstatement of the appeal in relation to the assessment and penalties.

29. Mr Stainer wrote to Mr Darler on 15 April 2013 with reference to the previous correspondence, and responded to points concerning the operation of activities at The Grand. Mr Darler replied on 23 April 2013, noting Mr Stainer's comments and requesting certain additional information.

30. On 11 June 2013, new Notices of Direction were issued to the same entities as previously. The Notices gave the recipients the option to make a joint nomination of the name in which the VAT registration was to be effected; in the absence of any such nomination, registration would be in the name "The Grand Folkestone".

31. In his letter dated 10 July 2013, Mr Stainer requested a review of the direction. He set out detailed information in support of this request.

32. On 2 August 2013, Mr Darler wrote to TGF to inform it that it would be receiving a notice of amended penalty assessment for the period 1 January 2009 to 31 December 2011. The reason for the amendment was that there had been an error in the amount of the penalty in the original assessment.

33. On 28 August 2013, HMRC wrote to TGF with a penalty calculation summary. This stated that it was not a penalty assessment or notice to pay. The calculation amended the basis of the penalty previously proposed under Sch 24 FA 2007. The total amount of the penalty on this basis was £18,717.25. A six month suspension of the penalty was proposed, subject to the meeting of specified conditions.

34. Following an agreed extension of the period for review in respect of the direction, Mr Waterhouse, the HMRC Review Officer dealing with the matter, wrote to Mr Stainer on 18 October 2013 with the results of the review. Under the heading "Conclusion of review", he set out his decision:

> "The decision maker has shown that links are in place showing that the activity at The Grand is one business that has been artificially separated.
>
> It is normal practice for hotels of this nature to provide food and drink at a cost additional to the accommodation but most will account for VAT on all sales as one VAT registered entity. It would be inequitable to allow a business to continue separating its business activities thereby avoiding having to account for VAT on all its supplies.
>
> The evidence in favour of there being a single business at The Grand is compelling, consequently I uphold the decision to require the businesses notified in the Notice of Direction to be registered for VAT as a single entity."

35. On 17 November 2013 (incorrectly dated 17 October 2013), The Grand Folkestone gave Notice of Appeal to HMCTS against HMRC's decision as upheld by Mr Waterhouse on review. Mr Stainer signed the form on behalf of The Grand Folkestone.

36. After delays resulting from possible ADR resolution and administrative changes within HMCTS, the appeal of The Grand Folkestone in respect of the direction and the appeal of TGF in respect of the assessment and the Sch 24 FA 2007 penalty were consolidated by Directions issued on 3 April 2014, and HMRC were directed to produce an amended and consolidated Statement of Case. HMRC did so on 28 April 2014. For various reasons which do not need to be recorded here, it has subsequently taken until February 2016 for the consolidated appeal to be heard.

Arguments for TGF and The Grand Folkestone

37. Mr Brown made submissions in support of TGF's application to make a late appeal in respect of HMRC's decision to impose a misdeclaration penalty on TGF. We consider this application at a later stage below.

38. The issues in the appeal were:

(1) The assessment on TGF in the sum of £110,360 plus interest. The burden of proof fell on TGF to show that the assessment was incorrect. Mr Brown indicated that he was not going to make submissions on "best judgment";

(2) Two penalty notices, one being a misdeclaration penalty under s 63 VATA 1994 in respect of VAT periods 06/08 and 09/08, and the other being the amended penalty under Sch 24 FA 2007 in the sum of £18,717.25;

(3) HMRC's decision to make the direction under para 2 Sch 1 VATA 1994 that The Grand Folkestone and other businesses named in the direction as a single taxable person carrying on the activities of the business described in the direction should be treated as a single taxable person carrying on the activities of the business described in the direction. In relation to this issue, the jurisdiction of the Tribunal was supervisory; the question was whether the decision was one that no reasonable body of Commissioners could have arrived

at, or whether HMRC had considered irrelevant matters or failed to take account of relevant matters.

39. Mr Brown made his legal and factual submissions after the hearing of the oral evidence and the case for HMRC. We deal with his submissions as to fact at a later point in this decision, together with those of Mrs Pavely for HMRC.

40. In his legal submissions, Mr Brown dealt first with the question of registration, then the assessment on TGF, and then the penalties imposed on TGF.

41. In respect of the registration direction, it was for HMRC to show that the separation was artificial. He referred to *Robert Mullis; Robert Mullis Restoration Services v Customs and Excise Commissioners* (2003) VAT Decision 18501 at [45]-[46]. (We note that these paragraphs are from Appendix 1 to the Decision, which were the submissions of Mr Robertson, who appeared for the appellant in that case. In the main decision at [27], the Tribunal stated that it accepted all of Mr Robertson's submissions. We comment that perhaps some caution is required in stating that the Tribunal endorsed the statements at paras 45-46 of Appendix 1 to the Decision.)

42. Mr Brown also referred to *Halifax and others v Commissioners of Customs and Excise* (Case C-255/02) at [73], which confirmed that taxpayers might choose to structure their businesses so as to limit their tax liability.

43. In the case of *A, D and J Forster v Revenue and Customs Commissioners* [2011] UKFTT 469 (TC), TC01319, the Tribunal had confirmed at [5]-[6] that the question was whether the decision of HMRC had been reasonable. Mr Brown commented that the jurisdiction was therefore supervisory and fell within the principles set out in *John Dee Ltd v Customs and Excise Commissioners* [1995] STC 941 (CA).

44. In relation to the assessment on TGF, the Tribunal had full appellate jurisdiction over the assessment as to the amount and other matters, and could adjust the assessment as appropriate.

45. Mr Brown's submission in respect of the penalties was that there should be none if the assessment were to be held incorrect.

46. The Tribunal could mitigate to zero the misdeclaration penalty under s 63 VATA 1994; this was by virtue of s 70 VATA 1994. In allowing for any mitigation, although the law had changed, Mr Brown submitted that it would be appropriate for the Tribunal to apply to the s 63 penalty the same level as it decided was appropriate under Sch 24 FA 2007. He referred to the three criteria to be taken into account under Sch 24, and also referred to HMRC's Compliance Handbook at CH82442. In *Mr E Kelly and Mrs S Kelly T/A Ludbrook Manor Partnership v Revenue and Customs Commissioners* [2015] UKFTT 632 (TC), TC04765 at [75]-[76] the Tribunal had agreed that HMRC might require too much if, without regard to the particular circumstances of the error, they required an admission of liability in order for there to be "telling". The Tribunal did not see that non-admission of culpability could of itself necessarily be a bar to being able to access a full reduction for disclosure.

47. In Mr Brown's submission, this had to be right, if the Appellant was straightforward; it was not appropriate to deny mitigation if there was no admission. Otherwise, if a party admitted culpability, how could that party pursue an appeal?

48. In relation to the misdeclaration penalty, he acknowledged that it was difficult to read across from Sch 24 FA 2007, but emphasised the Tribunal's discretion to reduce the penalty to zero.

49. The Tribunal had full appellate jurisdiction in respect of the penalties and could determine these without waiting for a further decision from HMRC.

Arguments for HMRC

50. Mrs Pavely referred to ss 73(1), 83(1)(p) and 84 VATA 1994, and to paras 1A(1) and (2) and para 2 Sch 1 VATA 1994. In relation to the penalty, the relevant parts of Sch 24 FA 2007 were paras 1, 3, 4, 5, 6, 9, 14 and 15.

51. The European authority for the making of the direction was Article 4(4) of the Sixth Directive. On the question whether separate businesses were being operated, Mrs Pavely referred to *Mr PC and Mrs V Leonidas v Customs and Excise Commissioners* (2000) VAT Decision 16588.

52. On the question of the assessment on TGF, Mrs Pavely cited *Van Boeckel v Customs and Excise Commissioners* [1981] STC 290, and *Commissioners of Customs and Excise v Pegasus Birds Ltd* [2004] STC 1509.

53. Mrs Pavely made submissions on issues of fact, which we consider below.

Discussion and conclusions

54. We consider in the following order the matters raised by the appeal:

(1) The application for an issue to be heard out of time;

(2) The assessment made on TGF;

(3) The penalties imposed on TGF;

(4) The direction under para 2 Sch 1 VATA 1994.

The application and related issues

55. The first matter considered at the hearing was the application on behalf of TGF for a late appeal to be admitted in respect of the decision of HMRC to impose a misdeclaration penalty under s 63 VATA 1994 for the VAT periods 06/08 and 09/08.

56. Mr Brown referred to the sequence of penalties issued by HMRC. The misdeclaration penalty had been issued on 29 March 2012. On 2 April 2012 HMRC had issued another penalty in respect of the assessment; the periods covered by the penalty notice included periods 06/08 and 09/08.

57. TGF submitted that the latter notice superseded the previous penalty notice; there could not be two penalty notices for the same period.

58. On 14 September 2012 HMRC had issued yet another penalty notice in respect of the same assessment and periods, stating that this replaced the previous penalty explanation schedule. This reduced the penalty to £69,526.80.

59. On 28 August 2013 HMRC had issued a penalty calculation summary (which was not a penalty assessment), reducing the amount to £18,717.25 for 1 January 2009 to 31 December 2011 inclusive.

60. TGF submitted that the penalty assessment issued on 29 March 2012 was superseded by the following penalties issued in respect of the same VAT assessment for identical periods, against which TGF had appealed in time. It followed that there was no decision to appeal against.

61. However, if the Tribunal held that the penalty was still extant, TGF sought permission to appeal out of time.

62. Mr Brown submitted that HMRC were not prejudiced by the late application. It had been HMRC who had issued the subsequent penalties and had not clarified the situation. The s 63 penalty, if it was still extant, was a tax-geared penalty and was therefore dependent on whether the appeal against the VAT assessment was allowed; if the appeal was allowed and as a result no tax was due, then no penalty would be due. The question did not turn on the conduct of TGF being deliberate or careless.

63. The reason for the late application was that TGF believed that the penalty for the period up to 31 December 2009 had been included in the notice dated 2 April 2012 and subsequent notices.

64. Mrs Pavely agreed that matters were quite confusing. HMRC had realised that the legislation had changed after 2009; anything before that was governed by s 63 VATA 1994. She referred to the penalty calculation summary issued on 28 August 2013. It had been hoped that HMRC would be able to suspend the penalty, as specified under the heading "Suspended penalties" in that summary, which listed three conditions. No response had been received. It was unfortunate that, as an appeal had then been received, no action was taken on that summary.

65. The technical position was that the appeal was against the penalty of £69,526.00 as shown in HMRC's records. However, HMRC's view was that the reduced assessment should apply. The existing penalty assessment was for the full period from 1 April 2008 to 31 December 2011.

66. HMRC's position was that the first notification relating to 2008 was still extant, but that the notification for the period from 1 January 2009 to 31 December 2011 was the further penalty.

67. Because of the confusion, HMRC had no objection to any out of time appeal.

68. Our conclusion at the hearing, on the basis of the parties' submissions, was as follows. To the extent that it proved necessary to do so, the appeal against the misdeclaration penalty was admitted out of time; thus TGF's late appeal was admitted.

69. At the hearing we did not consider the question of jurisdiction to hear the appeal against the penalty under Sch 24 FA 2007 (the "Sch 24 penalty"). The formal penalty assessment was not made until 26 October 2012, eight days after TGF's Notice of Appeal. At the time of that Notice, therefore, there was no formal HMRC decision against which TGF could appeal. It was not until the penalty assessment had been made that there was an appealable decision.

70. We consider it to be in the interests of justice for us to treat TGF's appeal as extending to that later formal assessment; both parties to that appeal proceeded as if the appeal had been duly made.

71. Since the hearing we have reviewed the position concerning the misdeclaration penalty and the effect of the complex correspondence concerning the Sch 24 penalty.

72. The first reference in the correspondence to the proposal to charge a penalty was a penalty explanation schedule dated 15 March 2012. This made clear that the penalty was not yet chargeable; HMRC stated that they would write again to let TGF know how much to pay and when to pay.

73. The penalty notice in respect of the misdeclaration penalty was issued on 29 March 2012, shortly after the start of correspondence concerning the Sch 24 penalty. This was headed "Notice of assessment of misdeclaration penalty", and stated that the penalty was due and should be paid immediately. No appeal was made by TGF against the misdeclaration penalty until Mr Brown's application considered at the hearing. (We consider below whether, in the light of the history of the Sch 24 penalty, the misdeclaration penalty is extant.)

74. In summary, the history of the Sch 24 penalty is as follows. The first penalty explanation schedule was issued to TGF on 15 March 2012. This was based on the amount of additional output tax. A revised version was issued on 2 April 2012. Each of these schedules specified the period covered by the penalty as 1 April 2008 [incorrectly stated as "208"] to 31 December 2011.

75. A further penalty explanation schedule was issued on 14 September 2012. This specified the potential lost revenue as £110,360, which was the amount of the VAT assessment after taking account of a recalculation of additional input tax allowable. The amount of the penalty was £69,526.80, and the period specified in the penalty table was 1 April 2008 to 31 December 2011.

76. The formal Notice of Penalty Assessment against TGF was issued on 26 October 2012. It followed the terms of the September 2012 penalty explanation.

77. The penalty calculation summary issued on 28 August 2013 emphasised that it was not a penalty assessment or a notice to pay. It calculated the penalty payable, if

TGF failed to comply with the suspension conditions, as £18,717.25. The applicable rate of penalty was 25.5 per cent of the potential lost revenue of £73,401.00. The schedule gave the tax period to which the proposed penalty applied as 1 January 2009 to 31 December 2011.

78. Our analysis is as follows. The only penalty actually assessed under Sch 24 FA 2007 is that imposed by the formal Notice of Penalty Assessment dated 26 October 2012 in the sum of £69,526.00, covering the period from 1 April 2008 to 31 December 2011. We do not consider that it is affected by the penalty calculation summary issued on 28 August 2013.

79. The period covered by the penalty assessment raises a significant issue. Although a new penalty regime was introduced by Sch 24 FA 2007, this did not begin immediately. The mechanism for its introduction was the FA 2007, Sch 24 (Commencement and Transitional Provisions) Order 2008 (SI 2008/568). Article 3 of that Order provided:

> "Notwithstanding article 2, no person shall be liable to a penalty under Schedule 24 in respect of any tax period for which a return is required to be made before 1st April 2009."

80. The penalty assessment purported to impose a penalty under Sch 24 for the period from 1 April 2008 through to 31 December 2011. That period included three VAT periods in 2008, namely 06/08, 09/08 and 12/08, for which the returns for TGF were clearly required to be made before 1 April 2009. The first period in respect of which TGF's return was required to be made after 31 March 2009 was 03/09.

81. The penalty assessment therefore contravened article 3 of the Order. We can see no basis for treating it as partially valid, as the penalty is calculated by reference to the whole period. As a result, the whole of the penalty assessment is invalid.

82. We do not consider that the position can be regarded as "cured" by the issue of the penalty calculation schedule. A penalty assessment which is invalid cannot be retrospectively validated by the issue of some later document, even if this correctly specifies the basis on which the penalty should have been calculated in the first place. In any event, the penalty calculation schedule makes clear that it is not a penalty assessment or a notice to pay.

83. It follows that we are not able to deal with the matter in the way suggested by Mrs Pavely, so as to treat the penalty as having been assessed in the sum of £18,717 and applying for the period from 1 January 2009 to 31 January 2011.

84. Although we have held that the penalty assessment is invalid, we consider it prudent to allow for the possibility that our conclusion might be overturned. We therefore consider below the issues relating to the calculation and imposition of the Sch 24 penalty.

85. As the Sch 24 penalty is invalid, it can have no effect on the misdeclaration penalty imposed under s 63 VATA 1994; we are satisfied that the latter penalty is

extant, and needs to be part of the subject matter of TGF's appeal. It is therefore necessary to consider the questions relating to that penalty, which we do in the relevant later section of this decision.

The assessment raised on TGF

86. The authorities referred to by Mrs Pavely in respect of the assessment were *Van Boeckel* and *Pegasus Birds*. In *Van Boeckel*, Woolf J made the following comments at 292-3:

> "The contentions on behalf of the taxpayer in this case can be summarised by saying that on the facts before the tribunal it is clear, so it is contended, that the assessment in question was not valid because the commissioners had taken insufficient steps to ascertain the amount of tax due before making the assessment. Therefore it is important to come to a conclusion as to what are the obligations placed on the commissioners in order properly to come to a view as to the amount of tax due, to the best of their judgment. As to this, the very use of the word 'judgment' makes it clear that the commissioners are required to exercise their powers in such a way that they make a value judgment on the material which is before them. Clearly they must perform that function honestly and bona fide. It would be a misuse of that power if the commissioners were to decide on a figure which they knew was, or thought was, in excess of the amount which could possibly be payable, and then to leave it to the taxpayer to seek, on appeal, to reduce that assessment.
>
> Secondly, clearly there must be some material before the commissioners on which they can base their judgment. If there is no material at all it would be impossible to form a judgment as to what tax is due.
>
> Thirdly, it should be recognised, particularly bearing in mind the primary obligation, to which I have made reference, of the taxpayer to make a return himself, 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 judgment, 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 judgment' 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. As long as there is some material on which the commissioners can reasonably act then they are not required to carry out investigations which may or may not result in further material being placed before them."

87. In *Pegasus Birds* at [16], Carnwath LJ referred to his judgment in "*Rahman (1)*" referring to *Van Boeckel* and other cases:

> 'The passages I have italicised show that the tribunal should not treat an assessment as invalid merely because it disagrees as to how the judgment should have been exercised. A much stronger finding is required; for example, that the assessment has been reached "dishonestly or vindictively or capriciously"; or is a "spurious estimate or guess in which all elements of judgment are missing"; or is "wholly unreasonable". . . Short of such a finding, there is no justification for setting aside the assessment.'

88. At [38] Carnwath LJ gave guidance to the tribunal:

> "In the light of the above discussion, I would make four points by way of guidance to the tribunal when faced with 'best of their judgment' arguments in future cases:
>
> (i) The tribunal should remember that its primary task is to find the correct amount of tax, so far as possible on the material properly available to it, the burden resting on the taxpayer. In all but very exceptional cases, that should be the focus of the hearing, and the tribunal should not allow it to be diverted into an attack on the Commissioners' exercise of judgment at the time of the assessment.
>
> (ii) Where the taxpayer seeks to challenge the assessment as a whole on 'best of their judgment' grounds, it is essential that the grounds are clearly and fully stated before the hearing begins.
>
> . . ."

(The remaining points are not relevant to the present appeal.)

89. Mr Brown stated when setting out the issues under appeal that he would not be making submissions on best judgment, and acknowledged that the burden of proof fell on TGF. It appears to us that in such circumstances, the Tribunal is not precluded from considering on the basis of the above principles the question whether HMRC have exercised their best judgment in making the assessment pursuant to s 73(1) VATA 1994. However, in the light of the comments made by Carnwath and Chadwick LJJ in *Pegasus Birds*, the principal question is likely to be whether the assessment should stand as made, or should be adjusted in the light of the Tribunal's findings of fact.

90. Mr Brown's submission in his skeleton argument in respect of the "assessment issue" was that the assessment was not proper to the Appellant, and in any event was incorrect in quantum.

91. Mrs Pavely submitted that Mr Darler had established from the information provided to him that TGF's VAT returns were incorrect in that they did not take into account the balance of any food, drink and any miscellaneous income not attributed to other entities as being attributable to TGF; the approach which Mr Darler had taken was reasonable. The method of calculation had been reasonable based on the information available to him at the time.

92. Mrs Pavely submitted that TGF had not provided sufficient evidence to satisfy HMRC's concerns.

93. We review the relevant evidence. In his assessment letter dated 28 February 2012, Mr Darler stated his view that the VAT returns for TGF fell short in a number of respects. He continued:

> "First, you advised me from the outset that this company was responsible for all food and drink not supplied by the other entities; the income for each of those entities could be obtained or deduced from the four café/bar sites. It became apparent that catering at functions and events, for example, had not been accounted for under any of these headings so it was assumed that any residue from the total Food and Drink income, after deducting the supplies made by the 4 other companies, was the income of [TGF]. Later discussions also indicated that other forms of income, such as tours, merchandise sales, jewellery commissions, corkage, use of equipment etc should be regarded as [TGF's] income. This means that output tax has been under-declared and, for the sake of equity, input tax needed to be re-calculated on a pro-rata basis too. Assessments will be notified to the company in due course under separate cover."

94. Mr Darler prepared a "Background report" following his two visits in May and July 2011. In this, under the heading "Build-up of VAT returns", he stated:

> "A global "VAT Return" is produced on the accounting system under the title of Kentish Estates Ltd;
>
> The sales figure on this global VAT return include [*sic*] only food and drink sales and ignores all other income;
>
> Mr Stainer prepares the VAT working papers for which he uses only food and drink sales from 4 specific sites (which are based on till readings), thus excluding food and drink at functions and all other forms of income;
>
> Mr Stainer deducts £70,000 from his sales total before calculating the output tax;
>
> Two calculations are carried out to obtain 2 pro-rata amounts of input tax representing VAT on overheads and VAT on bar stock.
>
> Regardless of whether there is a single or multiple businesses and whether any or all of the legal entities should be separately registered for VAT, the current method of calculating the output tax and input tax due for [TGF] is unacceptable as it does not reflect the actual supplies being made nor the costs incurred."

95. The documentary evidence included an annotated copy VAT return for the first VAT period in 2011, the date on the return being 29 April 2011. A separate document set out details for four businesses, which were Palm Court, Salon de Thé, Tudor Bar and Keppels. In the column headed "Jan-Mar", figures were included for each of these businesses, followed by a total figure of £129,643. Underneath that total there was a deduction of "£70", producing a net total of £59,643; it is therefore clear that "£70" was shorthand for £70,000". Below the £59,643, there was a note indicating that it was VAT inclusive, and a fraction of 20 divided by 120; the VAT was calculated as £9,940 and the net amount after VAT £49,703.

96. The figures from that document were carried into the annotations on the VAT return form, and further calculations based on these.

97. We are satisfied that the calculation of VAT was incorrect in treating the £70,000 as a deduction from the amount due. In Mr Darler's VAT Audit Report prepared following the visit on 9 May 2011, he recorded the following question and answer:

> "Why the £70,000 deduction from DGT in the VAT calculation?
>
> A – This is what he thought the VAT registration threshold was: his thinking was that the other companies can operate up to the threshold and anything else must go on the return."

The registration limit is purely for the purposes of establishing whether the turnover of a business is such that it is required to register; it is not some form of exemption or "nil rate band". It is clearly inappropriate and wrong for it to be deducted from turnover in arriving at the amount of output tax due.

98. For TGF, Mr Brown acknowledged that Mr Stainer had made errors, but submitted that Mr Stainer's clear evidence had been that all the supplies had been declared on the VAT returns. Mr Darler had produced schedules in a series of spreadsheets; the evidence of Mr Stainer and of Ewa Kobylartz had been that they could not understand these.

99. The evidence of Ms Kobylartz, who was head of the accounts department at The Grand, was that she had been unable to make any meaningful connection between the figures set out in Mr Darler's schedules and her department's records.

100. Mr Stainer gave an extensive critique of the investigation carried out by Mr Darler. We note that Mr Stainer did not comment on the question of the deduction of £70,000 in the VAT calculation. As an example of his criticisms of Mr Darler's approach, we set out the following from Mr Stainer's witness statement:

> "There do seem to be the most enormous variations in Mr Darler's turnover analysis . . .; as the business has been broadly consistent over the years he is reviewing, as demonstrated not only by the published accounts but also by a correct examination of the managing agents figures, and indeed by any other criterial one might care to choose, it is impossible for Mr Darler's figures to be correct."

101. We acknowledge that a degree of criticism of Mr Darler's approach may well be appropriate, but in the absence of a specific challenge based on failure to exercise best judgment, it is not appropriate for us to make findings as to the way he carried out his investigation. What is necessary for the purposes of deciding whether the assessment is correct in amount is to have evidence of what the assessable amounts should be, if it is contended that the amounts actually assessed are incorrect. Mere criticisms of the approach do not amount to evidence as to the amounts properly assessable.

102. No submissions were made on behalf of TGF as to the amounts by which the assessment needed to be adjusted. As Mrs Pavely argued, the burden of proof in

respect of the assessment falls on TGF. In the absence of anything to indicate the basis on which the assessment should be amended, we can do nothing other than confirm the assessment as made.

The misdeclaration penalty

103. As already indicated, the misdeclaration penalty totalling £5,188 is extant and requires to be considered as part of TGF's appeal.

104. Mr Darler's evidence in respect of this penalty was that it had been applied at the rate of 15 per cent to the under-declaration totalling £34,593 in the VAT periods 06/08 and 09/08. He found no reasonable excuse for the misdeclaration; in considering mitigation, he took the view that there had been insufficient co-operation in identifying and quantifying the under-declaration to justify allowance of any reduction in the penalty.

105. Mrs Pavely submitted that the penalty was appropriate. Misdeclaration penalties predated the introduction of the criteria for penalties under Sch 24. She commented that Mr Darler had not felt it appropriate to mitigate the penalty.

106. Mr Brown stressed the discretion provided by s 70 VATA 1994 for HMRC, or for a tribunal on appeal, to mitigate a misdeclaration penalty under s 63 VATA 1994 to such amount (including nil) as they thought proper. He submitted that in allowing for any mitigation, although the law had changed, the same level of mitigation as was decided for the Sch 24 penalty should be applied to the misdeclaration penalty.

107. Mr Brown provided copies of ss 63 and 70 VATA 1994. Neither he nor Mrs Pavely made any submissions as to the detailed application of s 63. It has therefore been necessary for us to consider the terms of this section following the hearing as part of the preparation of this decision.

108. The preconditions for a misdeclaration penalty are that the VAT return understates the person's liability to VAT and that the VAT which would have been lost if the inaccuracy had not been discovered exceeds the lesser of £1,000,000 and 30 per cent of the gross amount of VAT for the period.

109. Although Mrs Pavely submitted in general terms that the misdeclaration penalty had been correctly imposed and charged, she did not specifically demonstrate that these preconditions had been met.

110. We note from the notice of assessment of the penalty that the first paragraph makes the following statement:

> "The assessment of tax notified to you on 13.03.2012 has caused a breach of the objective tests for Misdeclaration Penalty under section 63, Value Added Tax Act 1994."

111. Mr Brown did not seek to challenge the basis of the misdeclaration penalty; his submissions concerning the penalties related to the overlapping periods and the

question whether there could be two penalties for the same period. We have addressed the latter issue.

112. We would have preferred to be provided with specific evidence that the necessary conditions had been fulfilled. However, we accept that Mrs Pavely had been put at a disadvantage as a result of the absence of any appeal by TGF against the misdeclaration penalty until that issue was raised in an application made two days before the hearing.

113. We are therefore prepared in the present case to accept that the statement made by HMRC in the notice of penalty assessment was correct. We make the general comment that in relation to penalties, it falls on HMRC to satisfy the Tribunal that the preconditions for making a penalty assessment have been satisfied, and that they should do so by providing specific evidence to that effect.

114. Under s 63(10)(a) VATA 1994, the person in question is not liable to a misdeclaration penalty if that person satisfies HMRC or, on appeal, the Tribunal that there is a reasonable excuse for the relevant conduct. TGF made no submissions concerning reasonable excuse, and thus there is no basis on which we can find that there is any such excuse.

115. We have considered Mr Brown's submission that mitigation in relation to the misdeclaration penalty should now be dealt with on a similar basis to that in respect of penalties under Sch 24. We do not consider that this is correct. We have reviewed HMRC's VAT Civil Penalties Manual at VCP10760-10799, which sets out HMRC's views as to the approach to be taken to mitigation of misdeclaration penalties. All the paragraphs in this part of the Manual make clear that there is a distinction between the penalty regime for accounting periods for which the due date is on or after 1 April 2009 and that for misdeclaration penalty, which applies where the due date is before 1 April 2009.

116. We find that there are no factors to justify mitigation of the penalty, whether as referred to in that section of HMRC's VAT Civil Penalties Manual, or otherwise.

117. We therefore confirm the misdeclaration penalty for periods 06/08 and 09/08 in the total sum of £5,188.

The Sch 24 penalty

118. We have concluded that the notice of penalty assessment issued on 26 October 2012 was not validly issued, as it covered a period for which a return was required to be made before 1 April 2009, and that the invalidity could not be cured by the issue on 28 August 2013 of the penalty calculation summary referring to a different tax period, different behaviour, and different potential lost revenue. In case for any reason our conclusion is found not to be correct, we consider the respective factors relevant to the calculation of the penalty under Sch 24 VATA 1994, as set out in HMRC's penalty explanation schedule.

119. The potential lost revenue set out in the penalty explanation schedule dated 14 September 2012 preceding the notice of penalty assessment dated 26 October 2012 was £110,360, ie in the amount of the VAT assessment dated 28 February 2012. This covered the whole of the period from 1 April 2008 to 31 December 2011.

120. The corresponding figure for potential lost revenue in the penalty calculation summary issued on 28 August 2013 was £73,401.00. The total amount of VAT forming the basis for the calculation of the misdeclaration penalty for periods 06/08 and 09/08 was £34,593. The combined total of these two figures is £107,994. If the latter figure is subtracted from the amount of the VAT assessment, the difference is £2,366. This equals the figure for under-declared VAT for VAT period 12/08, which was a period for which no Sch 24 penalty could be applied because the due date for the relevant return fell before 1 April 2009. HMRC did not seek to impose a misdeclaration penalty in respect of period 12/08.

121. We are therefore satisfied that the revised figure for potential lost revenue of £73,401.00 as set out in the penalty calculation summary was correct.

122. The behaviour referred to in the penalty explanation schedule dated 14 September 2012 was "deliberate"; this formed the basis of the penalty assessed by the notice of assessment dated 26 October 2012. The penalty range for deliberate inaccuracy with a prompted disclosure was from 35 to 70 per cent.

123. In the penalty calculation summary dated 28 August 2013, HMRC's view of the behaviour was stated to be "Failure to take reasonable care"; the information had been given to HMRC with prompting, so that the penalty percentage range became 15 to 30 per cent.

124. The next factor in the penalty explanation schedule dated 14 September 2012 was the reduction for quality of disclosure. No reduction was given for telling HMRC about the inaccuracy or for helping them to understand it. A reduction of 20 per cent was given for giving HMRC access to records.

125. In the penalty calculation summary dated 28 August 2013, the corresponding percentages were zero, zero and 30 per cent for giving access to records.

126. The resultant penalty percentage rate in the penalty explanation schedule dated 14 September 2012 was 63 per cent. The corresponding penalty percentage rate in the penalty calculation summary dated 28 August 2013 was 25.5 per cent. That summary proposed suspending the penalty for a period of six months, on the following conditions:

(1) TGF was to meet its payment, notification and filing obligations to HMRC (for example, submitting its VAT returns on time);

(2) TGF was to calculate output tax according to the actual turnover recorded in the accounting system less any turnover appropriate to other businesses;

(3) TGF was to calculate or apportion input tax according to the actual use in this business of the goods and services received.

127. TGF did not accept the suspension conditions.

128. On the assumption that the penalty assessment dated 26 October 2012 is not invalid (despite our above finding to the contrary), the penalty calculation summary dated 28 August 2013 constituted an invitation to TGF to agree the calculations and the amount of the penalty. Paragraphs on the first page of that summary document indicated that a notice of penalty assessment would follow agreement between TGF and HMRC, or in the absence of agreement.

129. It is clear from Mr Darler's letter dated 2 August 2013 that the intention was to issue a notice of amended penalty assessment:

> "The company will shortly receive a notice of amended penalty assessment with a reference number NPPS-159521.
>
> The amended Notice relates to the following tax period:
>
> 1 January 2009 to 31 December 2011
>
> This [*sic*] reason for the issue of the notice of amended penalty assessment is there was an error in the amount of the penalty in the original assessment."

130. There is no evidence in the documents before us of any such notice of amended penalty assessment. The appropriate course appears to us to be that we should consider the penalty as HMRC intended it to be amended, based on the penalty percentage rate of 25.5 per cent which they proposed.

131. HMRC's view of TGF's behaviour was "Failure to take reasonable care". We accept that this was the appropriate basis. In assessing any possible reduction for quality of disclosure, no reduction was allowed for telling HMRC or for helping them by clarifying or quantifying the under-declaration. We agree with that conclusion, and would not suggest any amendment to it. The reduction for giving access to records was 30 per cent for doing so when requested but not voluntarily. Again, we would not suggest any amendment to this.

132. The 30 per cent reduction has to be applied to the difference between the minimum penalty percentage of 15 per cent and the maximum percentage of 30 per cent, ie 15 per cent. The resulting reduction is 4.5 per cent. As a result, the penalty rate is 25.5 per cent of the potential lost revenue of £73,401, which is £18,717.25 as proposed in the penalty calculation summary. We find that, if the penalty assessment dated 26 October 2012 is valid, it is appropriate for it to be reduced to £18,717.25.

The Notices of Direction

133. The provisions authorising the making of directions that persons carrying on business are to be treated as a single entity for VAT purposes are paras 1A and 2 Sch 1 VATA 1994:

> "1A (1) Paragraph 2 below is for the purpose of preventing the maintenance or creation of any artificial separation of business

activities carried on by two or more persons from resulting in an avoidance of VAT.

(2) In determining for the purposes of sub-paragraph (1) above whether any separation of business activities is artificial, regard shall be had to the extent to which the different persons carrying on those activities are closely bound to one another by financial, economic and organisational links.

2 (1) Without prejudice to paragraph 1 above, if the Commissioners make a direction under this paragraph, the persons named in the direction shall be treated as a single taxable person carrying on the activities of a business described in the direction and that taxable person shall be liable to be registered under this Schedule with effect from the date of the direction or, if the direction so provides, from such later date as may be specified therein.

(2) The Commissioners shall not make a direction under this paragraph naming any person unless they are satisfied—

(a) that he is making or has made taxable supplies; and

(b) that the activities in the course of which he makes or made those taxable supplies form only part of certain activities … , the other activities being carried on concurrently or previously (or both) by one or more other persons; and

(c) that, if all the taxable supplies the business described in the direction were taken into account, a person carrying on that business would at the time of the direction be liable to be registered by virtue of paragraph 1 above; …

(d) …

. . .

(7) Where a direction is made under this paragraph then, for the purposes of this Act—

(a) the taxable person carrying on the business specified in the direction shall be registrable in such name as the persons named in the direction may jointly nominate by notice in writing given to the Commissioners not later than 14 days after the date of the direction or, in default of such a nomination, in such name as may be specified in the direction;

(b) any supply of goods or services by or to one of the constituent members in the course of the activities of the taxable person shall be treated as a supply by or to that person;

(c) . . .

(d) each of the constituent members shall be jointly and severally liable for any VAT due from the taxable person;

(e) without prejudice to paragraph (d) above, any failure by the taxable person to comply with any requirement imposed by or under

> this Act shall be treated as a failure by each of the constituent members severally; and
>
> (f) subject to paragraphs (a) to (e) above, the constituent members shall be treated as a partnership carrying on the business of the taxable person and any question as to the scope of the activities of that business at any time shall be determined accordingly.
>
> . . ."

134. Appeals against such directions may be made under s 83(u) VATA 1994:

> "(u) any direction or supplementary direction made under paragraph 2 of Schedule 1"

135. The jurisdiction of the Tribunal in respect of such appeals is set out in s 84(7) VATA 1994:

> "(7) Where there is an appeal against a decision to make such a direction as is mentioned in section 83(1)(u), the tribunal shall not allow the appeal unless it considers that HMRC could not reasonably have been satisfied that there were grounds for making the direction.

136. Thus (as Mr Brown acknowledged in argument) the Tribunal has supervisory jurisdiction in respect of this issue; the burden of proof falls on The Grand Folkestone to show that HMRC could not reasonably have been satisfied that there were grounds for making the Direction. If The Grand Folkestone can prove that HMRC could not reasonably have been so satisfied, then the Direction falls away and the situation of the affected parties reverts to what it would have been in the absence of the Direction.

137. The question for us to consider is not whether we would have arrived at the same conclusion as that reached by HMRC, but whether their decision was (to use a less than accurate shorthand term) "unreasonable".

138. The approach to be taken in such cases is set out in the context of a different legislative provision in the case of *John Dee Ltd*. Neill LJ commented at p 952:

> "In examining whether that statutory condition is satisfied the tribunal will, to adopt the language of Lord Lane, consider whether the commissioners had acted in a way in which no reasonable panel of commissioners could have acted or whether they had taken into account some irrelevant matter or had disregarded something to which they should have given weight."

139. Neill LJ also referred to another principle which tribunals should take into account:

> "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.
>
> . . .

> I cannot equate a finding 'that it is most likely' with a finding of inevitability."

140. The Grounds of Appeal contained in the Notice of Appeal by The Grand Folkestone dated 17 November 2013 included the following paragraph:

> "The notice is served on a building, not an individual taxpayer. The contention is that the building is a single business, but it is in multitudinous ownerships."

141. In our view, the explanation for the use of the name "The Grand Folkestone" is that, in default of any other nomination, the Direction took effect by putting the registration in the name of The Grand Folkestone, as specified in the letters giving notice to the relevant parties. Paragraph 2(7)(f) Sch 2 VATA 1994 makes clear that for the relevant purposes the "constituent members" are to be treated as a partnership carrying on the business of the taxable person, ie the single taxable person as specified in the Direction; that person is "The Grand Folkestone".

142. Before considering the detailed matters set out in the letters giving notice of the Direction, we address a broader issue, as it appears to raise a question as to the reasonableness or otherwise of HMRC's decision to issue the Notices of Direction dated 11 June 2013.

143. We consider it a material matter that in her review letter dated 14 August 2012, Mrs Reid stated:

> "Having looked at the evidence and noted your comments I consider that further information is required to ascertain the relationships between the various entities. In view of this I propose to withdraw the present decision / notices of directions and refer the case back to Mr Darler to arrange a meeting with you in order to make these enquiries.
>
> Please note that this does not prevent HMRC issuing another decision and / or Notices of Direction if it is considered appropriate."

144. The withdrawal of the Notices of Direction previously sent to the various business entities on 11 May 2012 was made by HMRC's letters dated 29 January 2013. (The reason for the length of the period between Mrs Reid's review letter and the issue of those letters is considered below.)

145. The wording of the Notices of Direction issued to the various business entities on 11 June 2013 is significant:

> "This notice is being re-issued as the name of the 'effective registration' previously advised is incompatible with our computer system."

146. As the letters dated 11 May 2012 had been, according to Mr Darler's evidence considered below, reissues of the Notices of Direction following amendment of the registered entity's name, it is not clear why there would have to be a further reissue of the Notices for the reason set out above.

147. With the exception of two matters, the wording of the respective original letters dated 21 February 2012 to each of the entities and the later letters dated 11 June 2013 is identical. (As we have indicated, the letters dated 11 May 2012 were not included in the evidence; we are therefore unable to compare the wording of those letters with that of the letters issued on the other dates.) The first exception is an amended reference in the later letters to bank account details. The second exception is the name given for the combined registration pursuant to the direction. In the original letters this was:

> "The Grand Folkestone Ltd & Grand UK Ltd & Keppels Ltd & Keppels Cuisine Ltd & Kentish Cuisine Ltd & Michael and Doris Stainer Partnership".

In the later letters this was:

> "The Grand Folkestone".

148. The reference in the 11 June 2013 letters to the notices being "re-issued" raises a difficulty. Are they to be construed as direct replacements for the 11 May 2012 notices? Or do they constitute completely new notices?

149. If the notices are replacements for the 11 May 2012 notices, this appears to disregard the requirement imposed by Mrs Reid in her review letter for a meeting to be arranged between Mr Darler and Mr Stainer. (The review letter was addressed "FAO Mr M Stainer" at The Grand Folkestone.)

150. Even if the notices are not replacements for the May 2012 notices, the same issue arises; why were the June 2013 notices issued without any meetings having taken place?

151. Mr Stainer's evidence was that there had been no such further meeting; we accept his evidence on this point. However, account must be taken of Mr Darler's evidence. In referring to Mrs Reid's review decision, he stated:

> "The advice was that all directors and partners of the entities involved should be interviewed to ascertain how their entities operated and to establish their views on the connections between the entities.
>
> Letters were then sent to Doris Stainer, Ramesh Pappuraj Babu and David William Webster on 14/09/12 asking them to contact me to arrange an interview.
>
> In the absence of any replies a second contact letter was sent on 17/10/12 to each person with a questionnaire listing the points I wished to cover. In the meantime I sought advice from our Policy unit on what to do if I failed to elicit a response; their guidance was that the artificial separation decision should be pursued and the Notices of Direction re-issued.
>
> Information Notices were sent to Doris Stainer and Ramesh Pappuraj Babu on 09/01/13 with a deadline of 09/02/13.
>
> The existing Notices of Direction were withdrawn on 29/01/13.

> As I had received no response to the Information Notices, on 11/03/13 I wrote to Mr Stainer summarising my previous decision on artificial separation and asking for his comments and details of any changes to the operation of the business.
>
> I received a letter from Mrs Stainer dated 16/04/13 stating that Mr Stainer had answered my questions but asking me to number them. On 23/04/13 I confirmed the reasons for my enquiry and supplied a numbered questionnaire.
>
> New Notices of Direction were issued on 11/06/13 to the same legal entities as before."

152. We have reviewed the correspondence referred to by Mr Darler in his evidence (with the exception of the Information Notices sent to Mrs Stainer and Mr Babu, which were not included in the evidence) and accept the extract from that evidence as set out above.

153. We find that, although it might otherwise have been unreasonable of HMRC to issue or reissue Notices of Direction in June 2013 without following Mrs Reid's instruction that a meeting should be arranged to make the relevant enquiries, the difficulties which were encountered in seeking to arrange such a meeting or to obtain the information in some other way justified the decision to issue those Notices in the absence of any meeting, and as a result that decision was not unreasonable. In the light of that finding, it is not necessary for us to consider whether HMRC's decision would inevitably have been the same if a meeting had been arranged or the information had been obtained in some other way.

154. We therefore consider the terms of those Notices, to determine whether on their terms HMRC could not reasonably have been satisfied that there were grounds for making the Direction.

155. In the Notices, HMRC stated:

> "Further to our enquiries into the organisation of your business activities, we have now concluded that the activities have been artificially separated because we have found organisational, financial and economic links between the separated parts of the business which have resulted in an avoidance of VAT.

156. In his review letter, Mr Waterhouse set out a verbatim extract from the Notices of Direction under the heading "The decision maker's case". This set out the details of the links found by Mr Darler. We address separately each of those three categories of links, in the order adopted by Mr Darler. We consider subsequently the general conclusions which Mr Waterhouse reached in upholding Mr Darler's decision to make the Direction.

(a) Financial links

157. Under this heading, the Notices stated:

> "Financial Links – all entities are financially interdependent, with income and costs shared:
>
> - Until recently there was only one bank account, in the name of Kentish Estates Ltd; Alternative bank accounts are said to have been arranged now but details of how these operate have not been provided.
> - Customer cheques are made out to The Grand Folkestone;
> - There is no cross-charging in reality between entities for goods and services, admin or management charges etc although the submitted annual accounts do show a cross-charge;
> - Until recently there was only one credit card account. Alternative credit card facilities are said to have been arranged now but details of how these operate have not been provided."

158. Under the heading "Review" Mr Waterhouse commented in relation to financial links:

> "It is understood that there are a number of bank accounts but information on the account holder and type of account is not known.
>
> It is fact that most payments are made by credit card of which there is only one account.
>
> Although there are entries in the accounts for the individual companies, there is no evidence to suggest that money is actually transferred from one company to another."

159. Mr Stainer's argument, in his letter dated 10 July 2013 requesting the review, had been as follows:

> "Financial links – sales for each individual enterprise are credited to that enterprise, and direct costs are directly charged to them; only common costs of the premises are shared through the maintenance fund, as is normal practice for large buildings in multi occupation.
>
> - There are in fact a variety of bank accounts, but sales are typically collected by credit card where there are volume economies (not to mention the difficulties of small operators with perhaps less than a prefect [ie perfect] credit record having access to such a facility.
> - Customer cheques go through the same system as the credit cards.
> - Maintenance costs are split in predetermined apportionments.

160. According to the handwritten notes taken at the time of Mr Darler's visit to the premises on 9 May 2011, Mr Stainer informed him that profits and losses were kept within the companies, and (other than for main losses, which were borne by Hallam Estates Ltd), inter-company loan accounts were used to deal with other losses. Mr Stainer did not think that any of the companies other than TGF were going over the VAT threshold. Mr Darler asked him whether he was making an effort to keep the other companies below the VAT threshold; his reply was that this was the intention

because they could not function if they were over that threshold as they would not have the income to support it.

161. At the end of the meeting Mr Darler explained to Mr Stainer that VAT registration was normally based on a legal entity and that all such entity's business activities had to be accounted for on the VAT returns. However, if HMRC regarded several entities as operating a single business, the registration could be applied to all those entities. Mr Darler emphasised that he was not giving a ruling at that stage.

162. On 19 July 2011 Mr Darler made a further visit to the premises. He asked Mr Stainer a series of questions, and again made handwritten notes of the meeting. The different companies were allocated areas of activity. There was currently no division of turnover in the accounting system between companies (or entities). There was a till-led system which should split bar and food. Mr Darler asked various other questions concerning matters such as the split of food and drink within room hire in the case of functions, and its allocation between entities.

163. We accept Mr Darler's handwritten notes as evidence of the matters dealt with at those meetings.

164. We also accept Mr Darler's evidence in his witness statement that, after considering all the information which he had available following these two visits, he confirmed his view that there was a single business and that there was an artificial separation of activities to avoid VAT.

165. He referred to the main factors supporting this view, of which the following related to financial links:

(1) There was one bank account;

(2) There was one credit card account;

(3) All customer cheques were made out to The Grand.

166. He considered factors contradicting that view; as these relate mainly to the other categories, we consider these as a later point.

167. The initial Notices of Direction dated 21 February 2012 were issued following Mr Darler's decision.

168. Mr Stainer's letter dated 5 March 2012 set out his initial statement of his reasons for disagreement with the Direction. In his letter dated 15 March 2012, Mr Darler indicated that the points set out in the Notices of Direction answered most of the points which Mr Stainer had made.

169. We have set out the history of the Notices of Direction and their withdrawals and replacements, culminating in the issue of the final version of the Notices of Direction dated 11 June 2013. No further input to the decision-making process was made subsequently to Mr Darler's decision which had led to the initial issue of Notices of Direction in February 2012.

(b) Economic links

170. On this subject, the Notices stated:

> "Economic links – the business provides a complete package of catering, accommodation, entertainment etc to a targeted clientele:
>
> - There is a single website which makes no mention of the different entities operating;
> - Press advertising is all under a single heading of "The Grand";
> - There are different trading names which in some cases correspond to a specific legal entity but in other cases do not;
> - There is a single corporate entity or profile – the average customer will recognise only The Grand Folkestone."

171. In his review letter, Mr Waterhouse commented under this heading:

> "Although it is not possible to purchase all services at the point of booking accommodation, this is standard practice within the hotel trade.
>
> Outward appearance of the business is that of a hotel providing all the services that a hotel would ordinarily provide, i.e. accommodation, food and drink."

172. The factors under this heading referred to by Mr Darler in his witness statement were broadly the same as those mentioned in the Notices of Direction.

173. In his letter dated 10 July 2013, Mr Stainer stated that no "packages" had ever been offered; anyone wishing to patronise those various services needed to make separate arrangements for each component with each of the relevant suppliers, as indeed would be the case in a typical town centre or shopping centre.

(c) Organisational links

174. On the subject of organisational links, the Notices stated:

> "Organisational Links – all entities are linked by directors, management staff, accounting systems & methods etc:
>
> - Either Mr or Mrs Stainer is a director, the company secretary or partner in each of these entities;
> - All day-to-day accounting is done by Kentish Estates Ltd (directors Michael & Doris Stainer), which has no trading activity;
> - All staff are paid by Kentish Estates Ltd; The PAYE scheme is in the name of The Grand Folkestone Ltd;
> - All sales invoices and till receipts are issued in the name of The Grand Folkestone Ltd but fall short of being tax invoices;

- Purchase invoices are in the majority of cases addressed to The Grand Folkestone;
- There is no differentiation in the accounting system between the different legal entities;
- Separate annual accounts are submitted for each company for CT purposes for which Mr Stainer carries out his own attribution of income and costs;
- All bar and food stock is ordered and received centrally;
- The General Manager oversees the day-to-day running of all activities;
- There is a complicated historical background to the growth and activity of most of the entities involved but they are now all under one control."

175. Mr Darler referred in his witness statement to the above matters, and also to the following matters:

(1) Alleged cross-charging was not supported with evidence;

(2) All entities were under the practical control of Mr or Mrs Stainer;

(3) All outputs and inputs were posted to a single company;

(4) Licences were all in one name;

(5) The indeterminate nature of the supplies made by TGF, which was apparently a nominal proportion of the supplies made by the other companies.

176. Mr Darler listed the factors contradicting his view that there was a single business and that there was an artificial separation of activities in order to avoid VAT. These were that there were separate legal entities, separate year-end accounts produced for Corporation Tax and Income Tax purposes, different trading names, and the piecemeal history of the relevant entities.

177. In his letter dated 11 July 2013, Mr Stainer commented:

> "Organisational links – it is indeed so that common services are provided by my accountancy practice assisted by my wife, but as previously indicated each of the enterprises has its own staff as well as its own shareholders. I correct various misapprehensions under this head:
>
> - As previously indicated, Kentish Estates Ltd deals with receipts and payments of the various enterprises; although the PAYE scheme is in the name of The Grand Folkestone Ltd, the cost is charged to the appropriate entity.
> - Only sales invoices relating to The Grand Folkestone Ltd are issued in that name, with a full VAT invoice being rendered if required; the other businesses do not use that name.
> - 'The Grand Folkestone' would appear on most invoices as the delivery address.

- The accounting system credits all sales to the appropriate entity; specific purchases relative to an individual entity are so charged, but general maintenance items are apportioned on a fixed formula.
- I certainly use one accounting system for all clients, as indeed would all managing agents in similar circumstances.
- Certain common deliveries are made to the goods received areas, but the paperwork is appropriately allocated to the individual enterprises.
- The General Manager does indeed oversee the day to day activities of the various tenants as indeed would he do for any shopping centre, for the overall benefit of both the landlord and the tenants.
- Although it is stated that all the entities involved "*are now under one control*", that has never been the case. The various individual company tenants included in the direction are all independent of one another, and are likely to remain so for the time being as they all have historic losses which could be lost if the undertakings were to be transferred."

178. In his review letter dealing with organisational links, Mr Waterhouse expressed the following views:

> "It is a fact that individual businesses are linked either by a common director or company secretary. This would not be expected in a normal landlord tenant relationship. It is therefore possible for one entity to exert control over the others to the benefit of the landlord and the business as a whole.
>
> It is acknowledged that there are areas where the individual companies are semi-autonomous, such as engaging their own staff, however the accounting system and areas such as invoicing and deliveries would appear to be shared."

(d) The general conclusion in Mr Waterhouse's review

179. Mr Waterhouse's conclusions are set out verbatim at paragraph [34] above.

180. The question for us to determine is whether we consider that HMRC, through Mr Darler in his decision upheld on review by Mr Waterhouse, could not reasonably have been satisfied that there were grounds for Mr Darler to make the Direction dated 11 June 2013.

181. In support of HMRC's submission that the Direction had been correctly made, Mrs Pavely referred to the factors set out above. She drew attention to the page on the website for The Grand which stated:

> 'The Grand is a magnificent suite hotel on The Leas in Folkestone "indisputably the finest marine promenade in the world".'

It had not been surprising for HMRC to conclude that there was a single business being operated; everything was under one banner, with all services being provided. The website was a single corporate site. There was no advertising by the individual entities; this was an indication of a single business.

182. She emphasised that there were common directors; the staff might be separate, but the directors were the link. Kentish Estates Ltd did all the accounting and paid the staff. Purchase invoices in the majority of cases were addressed to TGF. Bar takings etc were all taken to one account. There was a central reception desk, with diaries.

183. Corporation Tax was dealt with on a separate basis, using Mr Stainer's attribution of income and costs.

184. Taking all matters into account, including Mrs Stainer's acceptance in her oral evidence that Mr Stainer was in control of the companies, Mrs Pavely submitted that it was all one economic unit artificially separated, and that therefore the conditions for making the Direction were fulfilled.

185. Mr Brown made two submissions on the question whether HMRC's decision to make the Direction was or was not reasonable. The first was that the fact that HMRC had issued determinations and assessments in respect of PAYE and National Insurance Contributions ("NICs") on the relevant entities separately made the decision to issue the Direction unreasonable on its own. We return to this after considering his second submission.

186. His second submission was that, looking at everything "in the round", the decision had been unreasonable in taking into account irrelevant considerations. He listed a series of separate reasons relevant to the question whether or not the decision had been reasonable.

187. The first related to Mr Waterhouse's review letter, in which he had stated in the introduction to his section headed "Review":

> "Where for example, the relationships between businesses are not what one should expect from normal, independent but nevertheless associated trading entities, and where several business activities are operated from the same premises or adjoining premises but where the existence of one guarantees or underpins the viability of the other, HMRC can consider treating them as a single entity."

188. Mr Brown had asked Mr Darler in cross-examination whether there had been evidence of guaranteeing in the context of the entities involved; Mr Darler had been unable to think of any such evidence.

189. Secondly, Mr Waterhouse had referred to it not being possible to purchase all services at the point of booking accommodation; this was standard practice if the operation was through separate businesses.

190. Thirdly, the Appellants had stated throughout that The Grand was not a hotel; Mrs Pavely had drawn attention to the only reference to it as a hotel. Mr Darler had accepted in cross-examination that The Grand had never been licensed as a hotel.

191. Fourthly, Mr Brown submitted that the outward appearance was a completely irrelevant consideration; either the businesses were separated or they were not.

192. Fifthly, in the context of organisational links, the director or secretary was not a single person. Mr Waterhouse had referred to the possibility of one entity exerting control over the others; however, the test was not whether this was possible. HMRC had to show that it was a single person exerting control. Mr Brown contended that Mr Darler had accepted in evidence that it was not Mr Stainer; we have no record in our notes of Mr Darler having done so. There had to be proof that the entities did operate as a single business. In the section of his review letter quoted above, Mr Waterhouse had used the words ". . . would appear to be shared"; this did not amount to proof.

193. Mr Brown argued that of these reasons, most were irrelevant and should not be part of the test whether HMRC had shown that they were satisfied that the conditions set out in para 2(2) Sch 1 VATA 1994 had been fulfilled. He submitted that the conclusion of the review had certainly not been compelling.

194. Before considering the general question, we first deal with Mr Brown's specific points.

195. In relation to the first point, we do not construe Mr Waterhouse's letter as referring to formal guarantee arrangements. In our view, he was commenting on the existence of one business underpinning or guaranteeing the viability of the other. Put another way, he was saying that the respective businesses were interdependent for the purposes of together seeking commercial success.

196. On the second point, we think that Mr Waterhouse was saying that inability to purchase all services at the time of booking accommodation was a standard feature of the hotel trade, and thus that this did not preclude the conclusion that there were economic links between the entities providing the various services.

197. On the third issue, whether The Grand had been described as a hotel, we do not consider that this is a significant question. The test under para 2(2)(b) Sch 1 VATA 1994 is whether the activities of the respective entities form only part of the relevant activities. The description of the activity does not affect the application of this test.

198. Mr Brown's fourth point was that the outward appearance was an irrelevant consideration. We do not accept this submission. In our view the question of the outward appearance is directly relevant to the test under para 2(2)(b) Sch 1 VATA 1994; it is appropriate to enquire whether in the minds of potential customers there is an appearance of a single business, in order to establish whether as a matter of commercial reality the separate operators are in combination carrying on a single business.

199. On Mr Brown's fifth point, we find that the evidence of Mrs Stainer that Mr Stainer exercised control over the business, which we prefer to any suggestion to the contrary that Mr Darler may have made in cross-examination, indicates that there was a controlling link between the entities. For example, it was Mr Stainer who dealt with the VAT returns and the cross-charging as between entities.

200. Mr Brown argued that it was for HMRC to prove that the entities did operate as a single business. We do not think that this is correct. What is required by para 2(2) Sch 1 VATA 1994 is that HMRC must be satisfied as to all the matters referred to in that sub-paragraph. If they are so satisfied, they have the power to make a direction. Once such a direction has been made and (where relevant) confirmed on review, the question in any appeal to the Tribunal is whether the Tribunal considers that HMRC could not reasonably have been satisfied that there were grounds for making that direction. As we have already mentioned, the burden of proof as to this falls on the taxable person. Having made the direction, HMRC are not required to prove that the entities covered by it are operating as a single business; it is for the taxable person to show that this is not the case.

201. We return to Mr Brown's first submission concerning the separate determinations and assessments in respect of PAYE and NICs. We do not accept that this rendered the decision to issue the Direction unreasonable. The Direction is made for the purposes of VAT, which is an entirely separate tax. The considerations giving rise to the Direction are entirely different from those relevant to the decision to require payments of PAYE and NIC's from the respective entities.

Our general conclusion on the Direction

202. We do not consider that The Grand Folkestone has succeeded in discharging the burden of proving that HMRC could not reasonably have been satisfied that there were grounds for making the Direction. We emphasise the words of the Tribunal in *A, D and J Forster v Revenue and Customs Commissioners* [2011] UKFTT 469 (TC), TC01319 at [6]:

> ". . . it is not sufficient that we might ourselves, considering the matter at large, have reached a different conclusion . . ."

Results of the appeals

203. We summarise the results of the appeals:

(1) TGF's appeal against the VAT assessment is dismissed;

(2) TGF's appeal against the misdeclaration penalty under s 63 VATA 1994 is dismissed and the penalty confirmed;

(3) TGF's appeal against the Sch 24 penalty is allowed;

(4) The appeal of The Grand Folkestone against the Direction under para 2 Sch 1 VATA 1994 is dismissed.

Right to apply for permission to appeal

204. 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.

JOHN CLARK
TRIBUNAL JUDGE

RELEASE DATE: 27 April 2016