TC07692

VAT—Appeal against best of judgment assessment

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2018/05210

BETWEEN

KELVIN LAMB
T/A THE DOLPHIN **Appellant**

-and-

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

TRIBUNAL: JUDGE CHRISTOPHER STAKER
LESLIE BROWN

Sitting in public at Newcastle on 11 November 2019

Mr Matterson for the Appellant

Miss McLaughlin, litigator of HM Revenue and Customs' Solicitor's Office, for the Respondents

DECISION

INTRODUCTION

1. The Appellant appeals against an assessment made under s 73 of the Value Added Tax Act 1994 ("VATA") in respect of an under-declaration of VAT in periods 03/04 to 09/17 inclusive.

2. The Appellant acknowledges that there have been under-declarations and irregularities with his VAT returns. He does not dispute that he is liable to an assessment, but disputes the quantum of the assessment that HMRC have made.

3. The Tribunal gave an oral decision at the hearing on 11 November 2019, dismissing the appeal. The Appellant has since asked for full written reasons for the decision, which are now provided.

BACKGROUND

4. The Appellant is a sole-trader landlord of a pub in Sunderland called The Dolphin Pub ("the pub"). The pub has a main bar and a lounge bar, each of which has a till. There is a fruit machine in the main bar.

5. On 16 February 2017, HMRC carried out a routine compliance check into the Appellant's VAT returns. In the course of that check, it became apparent that there was a disparity between the Appellant's VAT returns and his annual accounts.

6. In an e-mail to the Appellant's agent dated 17 February 2017, HMRC requested the Appellant's agent to look into that discrepancy. On 17 March 2017, the agent replied that "It appears the takings given to us for the VAT are under declared, the discrepancies picked up when the final accounts are prepared."

7. There were various subsequent exchanges between the parties, and the Appellant and his agent subsequently provided various further information and documents to HMRC.

8. On 23 February 2018, HMRC Officer Carroll and a colleague had a meeting with the Appellant and his agent. In a subsequent letter of the same date, HMRC Officer Carroll sent the Appellant written notes of the meeting, and asked the Appellant to sign and return them if he thought they were a fair summary of the questions and answers given. The Appellant subsequently signed and returned the notes. These notes indicate that at the meeting, the Appellant accepted that his VAT returns had been inaccurate and that he had understated his VAT liability since he was VAT registered as The Dolphin Public House, that his accountant had told him on a regular basis that his takings were understated on his VAT returns, and that he accepted that his actions had been dishonest.

9. At the end of the 23 February 2018 meeting, Officer Carroll then gave the Appellant by hand a VAT assessment.

10. On 20 March 2018, the Appellant's agent appealed against the assessment.

11. On 24 April 2018, HMRC issued a reduced assessment, after the Appellant provided evidence of the date on which he had purchased the till in the main bar.

12. On 29 June 2018, HMRC issued a review conclusion letter, upholding the assessment.

13. On 25 June 2018, HMRC issued the penalty associated with the assessment.

14. On 23 July 2018, the Appellant brought the present Tribunal appeal.

15. On 1 May 2019, HMRC (Officer Carroll) issued a further reduced assessment (with a consequential reduction in the penalty), as a result of fruit machine takings having become VAT exempt on 1 February 2013.

THE HMRC METHODOLOGY

16. The papers indicate, and HMRC Officer Carroll confirmed in his evidence, that the best of judgment assessment has been calculated by HMRC on the following basis.

17. The Appellant's turnover was calculated on the basis of (1) takings from the main bar, (2) takings from the lounge bar, and (3) takings from the fruit machine.

18. As to the main bar, its till was installed on 16 December 2016, and HMRC extracted data from it on 23 August 2018. The extracted sales records covered 251 days. The figure of the total sales shown on that till (£347,179.91) was divided by 251 to give a daily average, and that figure was then multiplied by 91 to produce a figure of estimated average quarterly sales from that till (£125,870). That estimated average quarterly figure was then applied to every VAT period included in the assessment.

19. As to the lounge bar, HMRC determined that sales in VAT period 06/17 were £882.90 (being takings recorded on 8 April 2017), that sales in VAT period 09/17 were £1,130 (being takings recorded on 19 August 2017), and that sales in all other VAT periods covered by the assessment were £2,679.35 (being the total takings as recorded by the lounge till between 20 February 2017 and 8 April 2017.

20. As to the fruit machine, the Appellant's agent provided records of fruit machine takings covering the whole period 1 March 2013 to 31 August 2017, so that HMRC were able to apply the actual fruit machine takings figure to every period from 06/13 onwards. For VAT periods prior to 06/13, HMRC have applied an average of the quarterly takings in the 1 March 2013 to 31 August 2017 period.

21. Having calculated takings on the above basis, HMRC made an allowance for input tax on purchases that the Appellant would have had to make in order to achieve the sales figures. As the Appellant had not provided any purchase records as evidence of a specific amount of input tax, HMRC applied the relevant flat-rate scheme percentage to each VAT quarter.

22. Although the calculations for all VAT periods were derived from evidence relating to periods no earlier than 2013, and although most of this evidence was from 2017, HMRC made no retail price index (RPI) adjustments when making the assessments for VAT periods extending as far back as 03/04. HMRC's reasons for this, as stated in e-mails from Officer Carroll to the Appellant's agent dated 16 and 21 May 2018, and the 29 June 2018 review conclusion letter, were that the Appellant's declared outputs had been relatively constant with little variation during the whole of the periods covered by the assessment, and that the fruit machine takings that had been provided also showed little variation. One possible explanation for the consistency in turnover was considered to be that the Appellant had confirmed that he discounted his prices to remain competitive with competing establishments.

THE ISSUES

23. As noted above, the Appellant does not dispute that he is liable to an assessment, but disputes the quantum of the assessment made.

24. The Appellant has not appealed against the consequential "dishonesty" penalty imposed by HMRC under s 60 VATA, nor the "deliberate" penalty imposed by HMRC under Schedule 24 to the Finance Act 2007. Nevertheless, HMRC acknowledge that the making of an

assessment to cover periods as far back as period 03/04 is dependent on the Appellant's behaviour being deemed to have been dishonest, and during later periods, deliberate. HMRC submit that his conduct was relevantly dishonest (relying on *Ivey v Genting Casinos (UK) Ltd t/a Crockfords* [2017] UKSC 67) and deliberate (relying on *Auxilium Project Management Ltd v Revenue and Customs* [2016] UKFTT 249 (TC)).

25. At the end of the hearing, the Tribunal was satisfied that the Appellant was not seeking to appeal against the penalties (except to the extent that any reduction in the VAT assessment would lead to a consequential reduction in the penalties), and did not take any issue with the right of HMRC to make assessments covering the periods 03/04 to 09/17 inclusive. Given the Appellant's admission referred to in paragraph 8 above, the Tribunal is in any event satisfied that the understatement of VAT liabilities was relevantly dishonest and deliberate and that HMRC were entitled to make assessments extending back to period 03/04.

26. The sole issue in this appeal is accordingly the quantum of the assessments. The Appellant has not suggested that the amount of the assessment is not the figure that would result from a correct application of the HMRC methodology. Accordingly, the sole issue in this appeal is in fact a challenge to the methodology employed by HMRC in determining the amount of the assessment.

RELEVANT LEGISLATION

27. The main legislative provisions of relevance to this appeal are ss 60, 73 and 77 VATA and Schedule 24 to the Finance Act 2007.

28. Given the limited scope of the issues in this appeal, it is unnecessary to set out the details of these provisions.

THE EVIDENCE OF THE APPELLANT

29. The content of the Appellant's evidence is set out in his submissions below. At the hearing, the Appellant further stated that his main competitor, the Farringdon Club, began closing in the afternoons in February 2014, and closed completely in February 2018.

THE EVIDENCE OF HMRC OFFICER CARROLL

30. In his witness statement, Officer Carroll set out the procedural history of the case.

31. In examination in chief, Officer Carroll accepted that the lounge bar of the pub was hardly used as it was in disrepair, and expressed the view that the assessment had been generous to the Appellant.

32. In relation to the stocktaker reports relied upon by the Appellant, he stated as follows. He placed no reliance on the stocktaker reports at all. He had seen dozens of reports like these. Stocktakers often produce two reports, one for the customer and one for HMRC. In any event, the stocktaker only reports what is in front of them. The Appellant never kept invoices and the stocktaker reports were generated after the HMRC investigation.

33. In cross-examination, Officer Carroll further defended the methodology he had used in calculating the assessments, and in particular, his reasons for finding stocktaker reports to be unreliable.

THE APPELLANT'S SUBMISSIONS

34. The HMRC methodology is based on till readings from two tills, one in the main bar of the pub, and one in the lounge bar. These bar till readings covered a very limited period of trade. Most of the turnover was derived from the readings of the till in the main bar, and the Appellant had purchased that till only some 6 months previously.

35. The Appellant does not accept that these till readings were correct, and the kind of turnover suggested by the HMRC methodology was simply not achievable. This was a 2 room pub on a council estate. HMRC have accepted that the lounge bar was used entirely for functions and that it was closed at the time for renovations.

36. HMRC were wrong to conclude that the level of turnover that the Appellant was found to have had in 2017 had been consistently at the same level for all periods going back as far as VAT period 03/04. The Appellant had previously had competition from another pub called the Farringdon Club. In 2014, the Farringdon Club had ceased opening in the afternoons, and in 2018 it closed completely. The Appellant gained a significant amount of the Farringdon Club's former trade, such that his turnover in recent times was higher than it had previously been.

37. Furthermore, customers have had more money to spend in recent years than they did at the time of the 2008 financial crisis. HMRC have also not given the Appellant credit for building up trade, especially in the early years.

38. Additionally, HMRC have not allowed for price and duty increases over time, and the introduction and sustained use of "happy hours" in certain periods. MRC have also made no allowance for discrepancies such as over rings.

39. The Appellant also believes that he was robbed by certain former members of staff, which led to a higher level of takings after those members of staff left his employment.

40. The Appellant began using a professional stocktaker, who provided professional stocktaker reports. These showed that the Appellant used 6 to 7 barrels per week. To achieve the levels of turnover used by HMRC, it would be necessary to use 12 barrels per week. Given the size and location of the pub, that was not possible.

41. The assessment is not to best judgment. HMRC examined only a small period in detail and from this data, extrapolated backwards to the Appellant's date of registration. The assessment is excessive.

HMRC'S SUBMISSIONS

42. HMRC made a best judgment assessment, based on available material. While HMRC might have applied a different methodology, the approach adopted was perfectly reasonable, fair and honest. Officer Carroll believed that the takings put through the pub's tills were the most accurate basis on which to raise a VAT assessment. The main bar till's takings, and the fruit machine's takings, were responsible for the vast majority of the takings in the pub. By establishing an opening and closing date of the till in the main bar, and the takings therein, Officer Carroll was satisfied he had used the most accurate information available on which to make a best judgment assessment. The extrapolation back to the date of registration was based on the following facts: the pub is situated on an estate and has regular patrons, the Appellant has admitted to discounting drinks to stay competitive, and the turnover declared in the pub's annual accounts had stayed fairly static over the years.

THE TRIBUNAL'S FINDINGS

43. The Appellant has accepted that there was an under-declaration of VAT and that HMRC was entitled to make an assessment under s 73 VATA.

44. On the material before it, the Tribunal is abundantly satisfied that HMRC when making the assessment acted in good faith, and applied a fair and reasonable methodology to determine quantum, even if there might have been other methodologies that HMRC might have decided to apply. This is not one of those rare cases in which the Tribunal, in the exercise of a quasi-supervisory jurisdiction, would find that the assessment was not raised to the best of HMRC's judgment and should never have been made at all, for instance on the ground that it was reached dishonestly or vindictively or capriciously, or was a spurious estimate or guess in which all elements of judgment were missing, or was wholly unreasonable (see *Mithras (Wine Bars) v HMRC* [2010] UKUT 115 (TCC) ("*Mithras*") at [9]-[11]). In particular, the decision of HMRC not to apply a reduction to the earlier VAT periods was not dishonest, vindictive, capricious, spurious, or lacking in judgment or unreasonable. Indeed, in the Tribunal's view that decision was not open to criticism at all. It might have been open to HMRC to decide to apply some such reduction, but HMRC decided not to do so and gave valid reasons for not doing so.

45. As has been indicated above, the sole substantive issue in this appeal is the challenge to the quantum of the assessment. In an appeal against quantum, the Tribunal has a full appellate jurisdiction. It can consider any further evidence or arguments presented by the parties in the appeal and reduce the amount of the assessment, thereby substituting its own view on quantum for that of HMRC. (See *Mithras* at [7], [16]-[21]).

46. In an appeal against quantum, generally the burden lies on the taxpayer to establish the correct amount of tax due. The HMRC assessment is *prima facie* right, and remains right until the taxpayer shows not only that it is wrong, but also shows positively what corrections should be made in order to make the assessments right or more nearly right. There is an element of guess-work and an almost unavoidable inaccuracy in a properly made best of judgment assessment. It is therefore not enough for an appellant to show shortcomings in the HMRC methodology. The Appellant must by evidence and argument positively show a methodology and/or figures that are more reliable than those used by HMRC in making the assessment, even if the Appellant's methodology and figures may also have their own inevitable shortcomings. (See *Khan v Revenue and Customs* [2006] EWCA Civ 89 at [69].)

47. The Appellant argues that a more reliable methodology than that adopted by HMRC would be to rely on reports from a professional stocktaker that he has produced in evidence. However, Officer Carroll gave evidence as to why he considered such stocktaker reports to be unreliable, and the Appellant has not produced any evidence to show why such stocktaker reports should be considered to be reliable evidence of the matters for which he relies on them. Pages of the stocktaker reports produced by the Appellant contain the annotation "These results are subject to the validity of the information supplied". The stocktaker reports are for periods between November 2017 and July 2018, which fall outside the period of the HMRC assessment in any event. They also cover only a very limited period (one of the criticisms made by the Appellant of the HMRC methodology) and say nothing about periods going back as far in time as 03/04. The Tribunal is not persuaded that there stocktaker reports are more reliable than the evidence relied on by HMRC.

48. The Appellant argues that the kind of turnover suggested by the HMRC methodology was simply not achievable by a two-room pub on a council estate, one room of which was used for functions only and was closed at the time for renovations. However, this was a bare statement by the Appellant. No evidence has been produced by the Appellant to show what

kind of turnover would normally be achieved by a pub with the relevant characteristics of the Appellant's pub. It has not been established that any such evidence, had it been produced, would have given figures significantly lower than those used by HMRC in the assessment.

49. The Appellant's grounds of appeal in his notice of appeal state that he believes that he was robbed by certain former members of staff, which led to a higher level of takings after those members of staff left his employment. Further evidence was not provided of this. On the evidence before it, the Tribunal is not satisfied on a balance of probability that the Appellant was robbed by former members of staff. However, even if he was, there is no evidence upon the basis of which the Tribunal could make any kind of findings at all as to the amounts involved.

50. The Appellant contends that allowances should be made for discrepancies such as over-rings. However, the Tribunal notes that any such discrepancies, if they occurred, might just as easily have been discrepancies that led to takings being under-recorded (under-rings), as well as discrepancies that led to takings being over-recorded. Again, the Appellant has not produced any evidence to suggest that a business having the characteristics of his pub, or even businesses generally, tend to over-record sales by a certain amount due to such discrepancies. The Tribunal is not persuaded on the evidence that an allowance made for such discrepancies in any particular amount would lead to a more reliable figure than that used in the HMRC assessment.

51. The Appellant's main contention is that HMRC were wrong to conclude that the level of turnover that he was found to have had in 2017 had been consistently at the same level for all periods going back as far as VAT period 03/04. However, HMRC have provided reasons for applying a consistent amount to all VAT periods. The Appellant gives reasons why he says that turnover in previous periods would have been lower. However, he has not shown why those reasons are more likely to be correct than the reasons given by HMRC for concluding that the level of sales was more or less consistent for all periods. The Appellant has certainly not shown by what amount the figures for past VAT periods would have to be adjusted to give a more reliable figure than that used by HMRC.

52. The Appellant says that he achieved increased sales in recent years due to the Farringdon Club first closing in the afternoons, and then closing altogether. However, apart from his own vague and general evidence to this effect, there simply is no evidence at all that sales in the pub rose at any point above the level that they had been in VAT period 03/04, either at all, or by any given amount. At the hearing, the Appellant confirmed that the Farringdon Club closed only in February 2018, which was after the end of the period to which the assessment under appeal relates. Its closure therefore would not have affected the Appellant's turnover in the period relevant to this appeal. The Appellant said that the Farringdon Club began closing in the afternoons in February 2014. However, there is no evidence of how much of the afternoon trade of the Farringdon Club was picked up by the Appellant's pub thereafter or of how much the Appellant's turnover increased as a result. Furthermore, even if it were to be accepted the Appellant's trade was boosted to some degree or other by the partial closure of the Farringdon Club, it would be necessary to determine whether or not this was offset by other factors. The gain in former customers from the Farringdon Club would have been only a part of the Appellant's trade. Swings and roundabouts are an inevitable part of any business. The gain of one group of customers does not inevitably lead to an overall increase in turnover for the business as a whole.

53. The only evidence that does exist providing actual figures over extended periods (the Appellant's annual accounts and the evidence of the takings of the fruit machine) show that

turnover was consistent over a long period. The Appellant has not provided evidence capable of establishing a more reliable figure than that in the HMRC assessment.

54. The Appellant argues that customers have had more money to spend in recent years than they did at the time of the 2008 financial crisis, and that he has built up the trade since taking over the pub many years ago. He also suggests that the HMRC assessment does not take into account changes in prices due to inflation or changes in duty, or due to his use of "happy hours".

55. In respect of these arguments, the Tribunal's findings are the same as in paragraphs 52-53 above. In any business, the turnover figure is affected by a number of different factors, changes in one of which may be offset by changes in another. For instance, a drop in the volume of drinks sold by a pub from one year to the next may be offset by an increase in prices of drinks due to inflation over the same period, leaving the turnover figure in pounds approximately the same as what it was before. There is no reason why the turnover of a business will for instance necessarily increase by the amount of inflation. In this case, there was evidence that turnover had been relatively constant over a long period. The Appellant has not produced better or more reliable evidence to show that this was not the case, and to establish a more reliable figure than the amount of the HMRC assessment.

56. The Tribunal accordingly finds that the Appellant has not shown a methodology and/or figures that are more reliable than those used in making the assessment.

CONCLUSION

57. The appeal is dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

58. 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.

DR CHRISTOPHER STAKER

TRIBUNAL JUDGE

RELEASE DATE: 4 MAY 2020