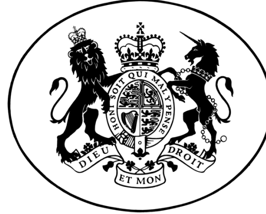

TC03160

Appeal number: TC/2013/01197

Flat Rate Scheme – choice of category – catering or retail – definition of 'catering' – VAT Regulations 1995 regs. 55B & 55K – whether choice by taxpayer reasonable – guidance by HMRC – fairness of backduty assessment – appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

THE VINTAGE TEA HOUSE LIMITED

Appellant

- and –

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS

Respondents

TRIBUNAL: JUDGE MALACHY CORNWELL-KELLY
MR HARVEY ADAMS FCA

Sitting in public at Bedford Square, London, on 2 December 2013

Ms Christine Braidwood FCA for the taxpayer

Mr John Nicholson of the Solicitor's Office of Her Majesty's Revenue & Customs for the respondents

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DECISION

Introduction

5 1 This appeal concerns assessments issued on 14 December 2012 to underdeclared value added tax for periods 08/08 to 05/12 due to the allegedly wrong Flat Rate Scheme percentage being used by the taxpayer, choosing the rate for 'retailing that is not listed elsewhere' instead of 'catering services including restaurants and takeaways'. By the hearing, the assessments for periods 08/08 and 11/08 had been 10 withdrawn and it was accepted that period 05/12, having been withdrawn on review and not reissued, also fell out. There is no dispute as to the figures and the issue is one of categorisation alone. We received oral evidence from Ms Nina Cooper, the proprietor of The Vintage Tea Shop Limited, and from Ms Joanne Shuttleworth, the case officer.

15 *Facts*

2 The Vintage Tea Shop began trading in 2006 selling gift items such as teapots, mugs, novelty signs, gifts, books, teabags and the like, and even some items of furniture; it had about ten seats for customers to enjoy tea and coffee and light refreshments.

20 3 The tea shop aspect of the business grew. By May 2008, there were some 20 seats for eating or drinking customers, and when the local council visited in September 2009 they found 28 such seats; by May 2010, the number was down to 22 but when Ms Shuttleworth visited in July 2012, there were 24 seats inside and 4 outside. Food being served included breakfast, Panini, lunches, drinks and ice cream, and Pimms, 25 wine and bottled beer were available. Ms Cooper was not permitted to operate an oven in the premises since there was no adequate ventilation, so sandwich machines, griddles and a microwave were used to prepare hot food. Because she was not able to cook as such, Ms Cooper was obliged to buy in cakes from supermarkets and cut them up, thus reducing her potential profit margin.

30 4 The analysis carried out by Ms Shuttleworth after her visit in July 2012 showed that over the periods of assessment the tea shop sales were always greater than 66% of turnover and in some periods it was up 87%. Mr Shuttleworth then produced a schedule showing, for each quarter, the actual percentage of total sales represented by the tea shop.

35 5 The lease of the premises prescribed that their permitted use was for "the sale of home and garden accessories, with ancillary sale of cakes sandwiches pastries and other cold foods of a similar nature together with coffees teas and other non-alcoholic drinks for consumption on or off the premises or such other uses within Class A1 of the Use Classes Order 2005 as the landlord may approve".

40 6 A planning permission dated 19 May 2010 showed that there had been an application to for change of use from A1 (retail) to mixed use of A1 (retail) and A3 (cafe). The permission granted was for "café serving coffee, other hot and cold drinks, sandwiches, similar light refreshments and meals for consumption on or off the premises, and for associated retail sales" with only reheated food and cold food

prepared elsewhere being served. The available seating was to be limited to 22 covers (i.e. seats).

7 Ms Cooper had elected to join the Flat Rate Scheme in May 2008 and had chosen the category 'retailing that is not listed elsewhere' at 7.5% rather than 'catering services including restaurants and takeaways' at 12.5%[1]. Ms Cooper's evidence was that she had come from a retailing background and had not sought or received advice when making this choice, but had acted on the basis of an HMRC leaflet about the Scheme given to her by a friend (this was not Public Notice 733, and nobody could provide a copy of it or could remember what advice it contained).

8 Ms Cooper said that she had been influenced in making the choice by the terms of her lease which made the catering side of things ancillary to the retail sales, so that it seemed right to elect for the category most in line with her obligations.

Submissions

9 For the taxpayer, it was argued that it was likely that the retail element of the business had originally been higher than it had become and that the choice of the retail rate had been reasonable in the circumstances. Moreover, the Revenue should have spotted the possibility that it might be the wrong choice much earlier - especially since the name of the business was not associated with retailing in the ordinary sense and suggested that there might be a mismatch. The principal reason the taxpayer had had for choosing the retail category, however, was that it corresponded most closely to the user restrictions in her lease. The terms of the extant planning permission reinforced the understanding that the retail character of the premises was regarded as critical.

10 The definition of 'catering' in Public Notice 733 was very wide and was not in the Flat Rate Scheme regulations; 'catering' to most people meant cooking hot food from raw ingredients, not simply heating up prepared meals. The definition was not contained in the 1995 regulations in terms and was contrary to the understood policy behind the Scheme of taking into account the different rates of profit resulting from the gross margins associated with the type of business in question. In this case, the margin on food supplies was reduced below that associated with catering because of the prohibition on cooking on the premises, and the need to buy in much of the food at prices which reflected that. There was reasonable doubt possible in the selection of the two categories which were contended for, and the taxpayer had acted reasonably.

11 In the alternative, it was submitted, taxpayers should not be able to elect for a particular category in the Scheme without some attempt being made by the Revenue to ensure that they had had their attention drawn to the criteria in the regulations before making a choice which, many years later, could lead to a crippling bill for arrears of tax. In the circumstances, backdating the assessments so far, as in this case, resulted in harsh and unfair treatment of a small business.

[1] This was the rate from the start of 2011; before that, the rates varied between 12%, 10.5% and 11% over the assessed periods. The assessments take account of these variations.

12 For the Revenue, it was pointed out the definition of 'catering' in Public Notice 733, corresponded to that in Schedule 8, Group 1, Note (3) to the Value Added Tax Act 1994, which was the framework of the Flat Rate Scheme regulations, and it was the definition replicated in Public Notice 733. The business clearly fell within its ambit and, equally clearly, the turnover was preponderantly attributable to catering supplies as so defined. The only reasonable choice of category at any stage in the periods under assessment was therefore the catering category, a conclusion which could only have been reinforced if the taxpayer had reviewed the position at the end of each year.

13 Moreover, when the taxpayer had made her election for the retail category, the business had already been in operation for two years and the pattern of turnover had become established. Against that, the requirements of the lease or the planning permission were irrelevant, though it was not conceded in any event that even if they were relevant the terms of them altered the position: both allowed for the catering activity which actually took place. A person acting reasonably, as required by the regulations, would have read the Public Notice, which was quite unambiguous, and have chosen the catering category in view of the actual turnover of the business.

Legislation

14 Value Added Tax Regulations 1995

> 55B
>
> (1) The Commissioners may, subject to the requirements of this Part, authorise a taxable person to account for and pay VAT in respect of his relevant supplies in accordance with the scheme with effect from—
>
> (a) the beginning of his next prescribed accounting period after the date on which the Commissioners are notified . . . of his desire to be so authorised, or
>
> (b) such earlier or later date as may be agreed between him and the Commissioners.
>
> (2) The date with effect from which a person is so authorised shall be known as his start date.
>
> (3) The Commissioners may refuse to so authorise a person if they consider it is necessary for the protection of the revenue that he is not so authorised.
>
> (4) A flat-rate trader shall continue to account for VAT in accordance with the scheme until his end date.
>
> 55K
>
> (1) Where, at a relevant date, a flat-rate trader is expected, on reasonable grounds, to carry on business in more than one category in the period concerned, paragraph (3) below shall apply.
>
> (2) . . .

(3) He shall be regarded as being expected, on reasonable grounds, to carry on that category of business which is expected, on reasonable grounds, to be his main business activity in that period.

(4) In paragraph (3) above, his main business activity in a period is to be determined by reference to the respective proportions of his relevant turnover expected, on reasonable grounds, to be generated by each business activity expected, on reasonable grounds, to be carried on in the period.

5

Category of business	*Appropriate percentage*
Accountancy or book-keeping	14.5
Advertising	11
Agricultural services	11
Any other activity not listed elsewhere	12
Architect, civil and structural engineer or surveyor	14.5
Boarding or care of animals	12
Business services that are not listed elsewhere	12
Catering services including restaurants and takeaways	12.5
Computer and IT consultancy or data processing	14.5
Computer repair services	10.5
Dealing in waste or scrap	10.5
Entertainment or journalism	12.5
Estate agency or property management services	12
Farming or agriculture that is not listed elsewhere	6.5
Film, radio, television or video production	13
Financial services	13.5
Forestry or fishing	10.5
General building or construction services*	9.5
Hairdressing or other beauty treatment services	13
Hiring or renting goods	9.5
Hotel or accommodation	10.5
Investigation or security	12
Labour-only building or construction services*	14.5
Laundry or dry-cleaning services	12

Lawyer or legal services	14.5
Library, archive, museum or other cultural activity	9.5
Management consultancy	14
Manufacturing fabricated metal products	10.5
Manufacturing food	9
Manufacturing that is not listed elsewhere	9.5
Manufacturing yarn, textiles or clothing	9
Membership organisation	8
Mining or quarrying	10
Packaging	9
Photography	11
Post offices	5
Printing	8.5
Publishing	11
Pubs	6.5
Real estate activity not listed elsewhere	14
Repairing personal or household goods	10
Repairing vehicles	8.5
Retailing food, confectionary, tobacco, newspapers or children's clothing	4
Retailing pharmaceuticals, medical goods, cosmetics or toiletries	8
Retailing that is not listed elsewhere	7.5
Retailing vehicles or fuel	6.5
Secretarial services	13
Social work	11
Sport or recreation	8.5
Transport or storage, including couriers, freight, removals and taxis	10
Travel agency	10.5
Veterinary medicine	11

Wholesaling agricultural products	8
Wholesaling food	7.5
Wholesaling that is not listed elsewhere	8.5

(2) * "Labour-only building or construction services" means building or construction services where the value of materials supplied is less than 10 per cent of relevant turnover from such services; any other building or construction services are "general building or construction services".

15 Value Added Tax Act 1994 Schedule 8 zero-rating

Group 1 - Food

The supply of anything comprised in the general items set out below, except—

(*a*) a supply in the course of catering; and

(b) . . .

General items

Item No

1 Food of a kind used for human consumption.

. . .

NOTES:

(1) "Food" includes drink.

. . .

(3) A supply of anything in the course of catering includes—

(*a*) any supply of it for consumption on the premises on which it is supplied; and

(*b*) any supply of hot food for consumption off those premises;

(3A) For the purposes of Note (3), in the case of any supplier, the premises on which food is supplied include any area set aside for the consumption of food by that supplier's customers, whether or not the area may also be used by the customers of other suppliers.

(3B) "Hot food" means food which (or any part of which) is hot at the time it is provided to the customer and—

(*a*) has been heated for the purposes of enabling it to be consumed hot,

(*b*) has been heated to order,

(*c*) has been kept hot after being heated,

(*d*) is provided to a customer in packaging that retains heat (whether or not the packaging was primarily designed for that purpose) or in any other packaging that is specifically designed for hot food, or

(*e*) is advertised or marketed in a way that indicates that it is supplied hot.

5 (3C) For the purposes of Note (3B)—

(*a*) something is "hot" if it is at a temperature above the ambient air temperature, and

(*b*) something is "kept hot" after being heated if the supplier stores it in an environment which provides, applies or retains heat, or takes other steps to 10 ensure it remains hot or to slow down the natural cooling process.

(3D) In Notes (3B) and (3C), references to food being heated include references to it being cooked or reheated.

Conclusions

15 16 It was not argued, and our researches have not established, that the definition of catering in Schedule 8 to the 1994 Act has been incorporated into the 1995 regulations at any point. It is, however, reproduced in Public Notice 733 and although Ms Braidwood contended for a narrower understanding of the term she did not advance authority for any alternative definition, for example from trade usage or the food 20 industry. For the want of any other appropriate definition, therefore, we accept that the definition in Schedule 8 is sufficient for the interpretation of regulation 55K.

17 Regulation 55K refers in terms to the taxpayer selecting one of its categories expecting on "reasonable grounds" to carry on his or her "main business activity" in 25 the selected category; regulation 55K(4) again makes it explicit that main business activity is determined by reference to turnover. As we have indicated, there is no issue that the taxpayer's turnover in the relevant periods was preponderantly in relation to catering rather than to retail sales.

18 Mr Nicholson submitted that the proportions of the turnover of the business were 30 already established in May 2008 when the taxpayer elected to join the Flat Rate Scheme and that the criteria on which the choice should be made at that time were therefore clear. There is however no evidence before us as to the turnover proportions of the business prior to May 2008 and, while it may be reasonable to guess at its being similar to that in the period afterwards, that is not a sufficient basis on which to 35 criticise a choice by the taxpayer that otherwise had some factors to commend it.

19 That the lease restrictions inclined the business to a retail orientation was a factor which Ms Cooper was entitled to weigh in the balance, since it must be assumed that she would be required to comply with its terms; the same was true of the then planning requirements, which we accept would also have been in Ms Cooper's mind 40 as likely to influence the conduct of her business. After the first year, however, the case becomes irresistible that the turnover proportions were clearly in favour of catering, and at that point that category should have selected for use thenceforth.

20 As to the policy of the Flat Rate Scheme categorisations for which Ms Braidwood contended, we make no finding. There is no evidence as to the matter and unless 45 considerations germane to statutory construction are put in issue it is not for the

tribunal to depart from the clear words used. Nor is it for us to comment upon the practice of the Revenue in making backduty assessments within their legal powers, or in not reviewing proactively choices made by a taxpayer in the selection of one or other of the categories available. It is also outside our jurisdiction to consider whether the Revenue should ensure that taxpayers making an election under the Scheme are fully informed of the issues before doing so.

21 In the circumstances, we find that for the year from May 2008 the choice of category made by Ms Cooper was reasonable, so that the appeal succeeds in relation to periods 02/09 and 05/09. For the reasons already stated, the assessment for 05/12 was withdrawn by the review officer and not reinstated, so that period and the assessments for quarters 08/08 and 11/08 which have been withdrawn, fall out of account. In relation to periods 08/09 to 02/12 inclusive the appeal does not succeed.

Appeal rights

22 This document contains the full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply in writing 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 the tribunal no 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.

MALACHY CORNWELL-KELLY
TRIBUNAL JUDGE

RELEASE DATE: 16 December 2013