TC03610

Appeal number: LON/2008/00164

VAT –best judgment assessment – was it reasonable – yes - was there a taxable supply by the taxpayer to self-employed minicab drivers in respect of the provision of two-way radios and bookings in exchange for "circuit fees" – yes – had output tax been charged on this supply – no - amount of assessment upheld - appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

LONDON CARS HOLDINGS LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE ALISON MCKENNA
MRS SHAMEEM AKHTAR

Sitting in public at Bedford Square on 7 May 2014

Mr Evans of MTL McHardy Trenfield Accountants and Tax Consultants for the Appellant

Ms Sinclair, Officer of HM Revenue and Customs, for the Respondents

DECISION

1. The Appellant company is a mini-cab firm operating in east London. This appeal concerns HMRC's decision to make a best judgment assessment and to issue a Notice of Assessment, both dated 22 February 2007, in respect of the VAT quarterly periods 02/04 to 11/06 for the amount of £39, 637.

2. HMRC's case, in summary, is that whilst the Appellant had properly accounted for VAT in respect of its trade with its customers, it had not so accounted for the separate taxable supply it had made to self-employed mini-cab drivers, to whom it had provided two-way radios and bookings in exchange for a payment (known in the mini-cab trade as a "circuit fee"). In respect of the decision to raise a best judgment assessment, HMRC's case was that the Appellant had originally submitted the answer to a questionnaire confirming that a circuit fee was charged but thereafter had not answered its questions or agreed to be interviewed or produced documentation requested, so that it was reasonable in all the circumstances for it to make a best judgment assessment.

3. The Appellant's case, in summary, was that there was no second supply. It was submitted that the provision of the radios and of bookings to the drivers was for no fee, but that the Appellant had deducted a management charge/commission from the payment made to it by its account customers before passing that payment on to the drivers. Mr Evans also submitted at the hearing of this appeal (but not previously) that the questionnaire referred to at paragraph [7] below had been incorrectly completed by the company director Mr Dell and that the information it contained could not therefore be relied upon.

The Tribunal's Jurisdiction

4. Section 73(1) of VATA 1994 provides that

> Where a person has failed to make any returns required under this Act …or to keep any documents and afford the facilities necessary to verify such returns or where it appears to the Commissioners that such returns are incomplete or incorrect, they may assess the amount of VAT due from him to the best of their judgment and notify it to him.

5. Section 83(p) of the 1994 Act provides for an appeal with respect to the assessment itself and also with respect to the amount of the assessment. The Appellant's grounds of appeal are that "the assessments raised are incorrect" but the Tribunal treated this appeal as one concerning both the reasonableness of the best judgment approach taken by HMRC and also the amount of the assessments. The Appellant bears the burden of proof of satisfying the Tribunal that HMRC's approach was unreasonable and that the assessment figures were wrong on the facts.

6. The Tribunal had regard to the Court of Appeal's decision in *Rahman (trading as Khayam Restaurant) v Customs and Excise Comissioners (No 2)* [2003] STC 150 and to Chadwick LJ's description in that case of the two-stage role for the Tribunal in

considering a best judgment appeal. The Tribunal noted the requirement for it to decide, firstly, whether HMRC's methodology was so flawed that it amounted to an unreasonable exercise of discretion and if the best judgement assessment was found to be reasonable, to consider whether the amount of the assessment was correct, in relation to which the Tribunal was able to make its own findings of fact and take fresh evidence into account.

The Facts

7. The Appellant registered for VAT with effect from 1 September 2003. HMRC sent it a generic questionnaire in November 2005, asking questions about the company's method of doing business. The questionnaire was returned dated 28 March 2006, having been completed and signed by one of the company's directors, Mr Dell. The answers to the questionnaire included information that account work fees were paid to the drivers "less rent payable" and that there were 20 drivers who paid a weekly "circuit fee", said to be £85 for full time drivers and £60 for part time drivers. The questionnaire also stated that the business acts as principal for account work and charges VAT on the full invoiced value, but does not charge or account for VAT on any separate administration charge.

8. HMRC sought clarification of a number of points in correspondence, but further information was not provided by the Appellant. HMRC arranged a visit to the Appellant's premises in February 2007 where they met Mr Evans, who in addition to representing the Appellant at the hearing of this appeal, also serves as the company secretary. Although the visit had been made by appointment, Mr Evans was not then willing to discuss the business at all and asked for all questions to be put in writing. On inspection of the business records, HMRC's officer noted that the VAT returns related to income from account customers only, which was at variance with the information about the business given in the questionnaire to the effect that it also conducted non-account work. He also noted that the company was operating a cash accounting system but again this was at variance with the information given in the questionnaire. On undertaking a bank account reconciliation exercise, the officer noted some significant discrepancies. The difference in funds banked compared with outputs declared in the period 05/04 was just under £28,000 and in the 08/04 period, just over £13,000.

9. The Tribunal heard evidence from the HMRC officer who had conducted the visit to the Appellant's premises. Officer Pradeep Vaghela had, in accordance with the Tribunal's directions, prepared a witness statement which had been served on the Appellant's representative prior to the hearing. He explained to the Tribunal that he had in 2007 been involved in a special project concerning mini-cab firms but had since moved to other duties. He had, at the time of the visit to the Appellant, conducted four previous visits to companies in the same line of business and reviewed returned questionnaires. His understanding of the usual business model in this industry was that the driver pays the firm a "circuit fee" in respect of all work (cash and account fares) and he explained that there would be no incentive for a mini-cab firm to give work to a driver who was not paying it a fee for the work.

10. Officer Vaghela explained to the Tribunal that his decision to make a best judgement assessment in the Appellant's case was based upon, firstly, the answers given in the questionnaire and the absence of any information to contradict the picture of the company's mode of business that had been presented in those answers; secondly, his knowledge of the business model of similar firms and the standard practice of payment of circuit fees by drivers; and thirdly, the significant difference between the funds banked and those declared as income when he had conducted the bank account reconciliation.

11. Officer Vaghela explained to the Tribunal that he had not seen any records of circuit fees being charged and had not been able to ask about this as he was not permitted to speak to the Dells or to any of the drivers. He said he had not looked at the company's accounts and he had not been provided with any other information by Mr Evans in response to the questions asked in correspondence. Mr Evans put only one point to Officer Vaghela in cross-examination, which was that the questionnaire had been completed wrongly by Mr Dell. Understandably, Officer Vaghela was unable to comment on this proposition.

12. Officer Vaghela explained that his letter of 22 February 2007 set out the basis of his assessment. He had concluded that the Appellant was making a second taxable supply in charging the drivers a circuit fee and that it had adopted a method of accounting which sought to off-set one supply with the other. As he had not been told how many full-time and how many part-time drivers were working, he had assumed fifteen full-time and five part-time drivers. He had then multiplied the number of drivers by the figures given for full and part-time circuit fees in the questionnaire, producing a weekly income figure from this source. He had then multiplied that figure by the number of weeks in each VAT period. The total figure reached by that method was deemed to be VAT-inclusive, so the applicable VAT fraction was applied to arrive at the VAT due (then 17.5%) for each period. His methodology was not challenged by Mr Evans in cross-examination.

13. Mr Evans opened the Appellant's case to the Tribunal on the basis that he would be calling no witness evidence but during the hearing Mrs Dell, who was present, indicated to the Tribunal that she would like to give evidence. Ms Sinclair did not object and the Tribunal considered that it would be helpful to hear from her. As she had not previously made a witness statement, the Tribunal adjourned for a short period to give Mr Evans an opportunity to discuss this development with his client, and offered HMRC the same facility if it wished to consider its position after Mrs Dell's evidence in chief.

14. Mrs Dell elected to give her evidence on oath and was duly sworn. She explained that she is a director of the company with her husband, and that after they had been in business for some time another mini-cab firm had approached them for help with account work for the Primary Care Trust and Mental Health Trust. She explained that they had simply adopted the business practices of the other firm in relation to this work. The Tribunal had been provided with an "Office Price List" and a "Drivers Price List" and Mrs Dell explained that the difference between the two prices (26%) was the firm's profit. She said that they had "inherited" this price list

from the other firm. All jobs were priced according to this list, which was calculated on the basis of the post codes of the collection and delivery addresses. Mrs Dell told the Tribunal that at the relevant time only 1% of the company's business was from non-account work, in respect of which the drivers were paid directly in cash and no management fee was charged to the driver. She described this arrangement as a "treat" for her drivers. The vast majority of the company's work was from the account customers, and this worked in the following way. A job would be faxed by the customer to the company, this would be allocated to the driver and a job docket created. On Thursdays, the drivers brought in their own dockets and these were matched with the job dockets. On Fridays Mr Dell would go to the bank and take out sufficient cash to pay the drivers what they were owed for the jobs that week, minus the management fee charged by the company. The account holder would then be invoiced and an amount transferred to the company's bank account by BACS. Mrs Dell said that there was often a delay before the BACS payment was received, but then you might get several at once. In cross-examination Mrs Dell accepted that there was a risk to the company inherent in this business model, because there was no financial risk to the drivers if the account holder did not pay. When questioned about the two-way radios, Mrs Dell said that the drivers did not pay the company a rent for them, although the company had bought them (with the benefit of a loan) and paid the yearly licence fee to OfCom. The drivers kept the radios in their own cars when not at work but they were owned by the company.

15. Mrs Dell told the Tribunal that she runs the office but that she relies on Mr Evans to handle the accounting and VAT matters. She also explained that the company was, at the time of these assessments, involved in some very sensitive work, for example transporting blood between hospitals, or transporting children who had been taken into care to safe accommodation. She explained that all of the drivers were Criminal Records Bureau checked, and that they had to be extremely reliable and discrete in view of the nature of this work. She said that the company had to abide by a confidentiality agreement and that she had herself accompanied children on their journeys at times. The drivers and company had to be very close-knit in these circumstances and she described them as being like a family. Mrs Dell explained that she and her husband lived above the office and took it in turns to work twelve hour shifts at the controls. They took home about £180 a week between them and paid a minimum wage to a person who sometimes filled in as controller to give them a break.

Submissions

16. Ms Sinclair on behalf of HMRC asked the Tribunal to find that for the relevant periods the Appellant had two streams of income. The first was fares from customers (principally account holders) and the second was the circuit fees paid by the drivers. This was, she submitted, accurately described in the questionnaire as "rent payable". She submitted (and it was accepted by Mr Evans) that the company was the principal in its contractual relationship with the account customers, and not acting as an agent for the drivers. Mr Evans had at times referred to the imposition of a management charge/commission fee on the drivers, but this arrangement would only be applicable if the driver were the principal and the company his agent. Whilst this appeared to be

the arrangement for cash customers, Mrs Dell's evidence was that this accounted for only 1% of the company's work at this time. Ms Sinclair pointed out that the Tribunal had received no evidence to contradict the picture of the business given in the questionnaire, apart from Mrs Dell's impromptu evidence which she asked us to reject. In particular, she submitted that the Tribunal had seen no sales records, witness evidence from drivers, or copies of contracts between the company and its drivers to support the Appellant's case.

17. Ms Sinclair referred us to a number of First-tier Tribunal decisions, which had been included in the Tribunal's bundle and so served on Mr Evans in advance of the hearing. These included *Crayford and Bexleyheath (Motors) Limited* which was decision 13620 in 1995 and in which the Tribunal had concluded that the company had "been correctly accounting for output tax on the full amount of the circuit fees". She also referred us to *RJ and CA Blanks* which was decision 14099 of 1996 and in which the Tribunal had found that, despite the absence of a specific contractual term, there was an "unescapable inference" that the drivers contracted with the Blanks' mini-cab firm in exchange for the two way radios and access to customers that they afforded. There was a different remuneration system for drivers in that case however.

18. Mr Evans submitted that the questionnaire had not indicated that the drivers were all self-employed and there was no consistency to their work pattern, so that the basis of the assessment calculation was wrong. He further submitted that no circuit fees were paid by the drivers to the company and that the questionnaire was wrong to have reported this arrangement. In response to a question from the Tribunal, he accepted that he "probably could" have produced evidence from the drivers to underpin these submissions, but accepted that the Tribunal had no evidence before it to support his case other than the oral evidence given by Mrs Dell, on which he asked us to rely.

Conclusion

19. As noted above, the burden of proof in satisfying the Tribunal that HMRC's decision to issue a best judgment assessment was not reasonable rests with the Appellant. Having considered all the evidence carefully, we conclude that the Appellant has not satisfied us that HMRC's decision was unreasonable in all the circumstances. We note here in particular that the answers to the questionnaire presented a picture of the company's mode of business which raised legitimate questions, but that Mr Evans chose not to assist HMRC with its further enquiries. We also note that HMRC's visit to the company's premises again raised questions about the accuracy of the VAT returns, especially in view of the significant amount of cash banked which did not tally with the reported output tax. It was, in our view, reasonable for HMRC to have concluded that a second taxable supply was being made by the company to the drivers in view of the answers to the questionnaire. We are satisfied that the test for making a best judgment assessment under section 73(1) of VATA 1994 (set out at paragraph [4] above) was met because, as Mr Evans had refused to discuss the matter at the visit and did not supply the answers to questions subsequently raised in correspondence, the company had not assisted HMRC to verify its returns and it was reasonable in those circumstances for HMRC to conclude that

the returns were incomplete or inaccurate in view of the discrepancies between the answers to the questionnaire and the situation it had found at the visit to the premises.

20. We also find that the amount of the assessment should be upheld. We are satisfied on the balance of probabilities that the provision by the company of the two-way radios and of jobs from its account holders is a supply of services by the company to the drivers and that this was for consideration because, as the questionnaire states, a "rent" is paid by the drivers to the company for these services. It is difficult to conceive how the company could have survived if this were not the case, as on Mrs Dell's evidence all the costs were front-loaded and the company alone took the risks associated with non-payment or late payment by the account holders. We agree with the conclusion in the *Crayford and Bexleyheath* case that output tax is due on the circuit fee income.

21. Officer Vaghela's methodology in making his assessment calculation seemed to us to be correct on the basis of the information he had available to him. His calculation was in fact based largely upon information provided by the company itself in its response to the questionnaire. The basis on which the assessment was made was set out fully and fairly in his letter dated 22 February 2007, yet despite the passage of seven years since that letter, the Appellant failed to provide any documentary evidence to the Tribunal to show that the officer's assumptions were wrong. Mr Evans' submissions to the Tribunal were unsupported by evidence and we note that he could have produced to the Tribunal witness statements from drivers and/or letters of agreement between the drivers and the company to contradict the information about circuit fees given in the questionnaire; he also could have served a witness statement from Mr Dell stating that the information he had given in the questionnaire was wrong, but he did not take any of these steps. The Tribunal found it helpful to hear from Mrs Dell and we found her to be an honest and conscientious person but, as she freely admitted, she was unaware of the finer details of the business and had left those matters to Mr Evans. We find that she had adopted the other firm's business practices without understanding them and was consequently unaware of the precise financial arrangements between the company and the drivers. In the circumstances we found ourselves unable to rely on her evidence that no circuit fees were paid and, as Mr Evans did not produce any other evidence to support his client's case, he was unable to satisfy the evidential burden resting upon the Appellant in this appeal.

22. In all the circumstances we conclude that the decision to make a best judgment assessment was reasonable and that the amount of the assessment should stand. Accordingly, we now dismiss this appeal.

23. 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.

ALISON MCKENNA
TRIBUNAL JUDGE

RELEASE DATE: 20 May 2014