[2016] UKFTT 0517 (TC)

TC05266

Appeal number: TC/2014/01500

VAT – standard rate/zero rate split – possible suppression of takings – invigilation-assessment to best of judgement

FIRST-TIER TRIBUNAL
TAX CHAMBER

SEYED ANAYET TORKIZADEH AND HOMEIRA TORKIZADEH T/A THE GRANARY **Appellant**

- and -

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

TRIBUNAL: JUDGE MARILYN MCKEEVER
MR NIGEL COLLARD

Sitting in public at Brighton on 4 February 2016

Mr Arthur, accountant, for the Appellant

Mr Haley, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. *Preliminary*

2. As noted below, Directions were issued after the hearing to allow the Appellant to provide additional calculations and information and to make further submissions with a view to enabling the parties to agree a settlement of the matters under appeal. Owing to an administrative oversight, the Tribunal was not provided with copies of all the post-hearing correspondence between the parties. A decision was originally made on the basis that the Appellant had not submitted any further information. The Appellant's representative drew the Tribunal's attention to the fact that the Appellant had provided additional information which had not been taken into account in making the decision.

3. The Tribunal has now considered all the post-hearing correspondence between the parties and considers that the original omission to consider such information was an "accidental slip or omission" within Rule 37 of The Tribunal Procedure (First-tier Tribunal)(Tax Chamber) Rules 2009. Accordingly, this may be corrected by sending notification of the amended decision to all parties and making any necessary amendment to any information published in relation to the decision.

4. This document contains the amended decision.

5. *Introduction*

6. This case concerns whether Mr and Mrs Torkizadeh, T/A The Granary, who ran a cafeteria/takeaway in Crawley, Sussex, had underpaid VAT as a result of the suppression of takings and/or an incorrect split between standard and zero rated supplies.

7. The appeal relates to the VAT periods ending February 2010 to February 2013 inclusive. A notice of assessment was issued on 4 September 2013 in the sum of £28,436.00 under section 73(1) Value Added Tax Act 1994 (VATA).

8. We had before us a bundle of documents including correspondence between the parties and copies of accounts and other evidence and we heard witness evidence from Mr Pitcher of HMRC (who had reviewed the decision of the officer who had carried out the investigation as that officer had left HMRC) and from Mr Torkizadeh.

9. *The Facts*

10. The Appellant acquired the business in 2008. It was in a run-down condition and was only open from 8am to 2pm. It did not make money. The Appellant made a number of improvements to the premises. In particular, he moved the counter back and created space for several additional tables, so more people could eat inside. It is unclear when this was done, but a letter from the Appellant's then accountant states

this happened in 2011 and included a letter from the local authority, dated 23 November 2010, relating to a change in planning use class as evidence.

11. The cafeteria served food and drinks to be eaten on the premises and to be taken away. The menu included a variety of sandwiches baps and similar items which could be served hot or cold including toasted sandwiches. They also served cooked breakfasts, hot pies and sausage rolls and hot and cold drinks.

12. A letter from the Appellant's then accountant indicated that the Appellant had extended the opening hours in 2011. At some stage, the Appellant began to sell takeaway pizzas. Mr Torkizadeh could not remember when but thought it was after 2011. The notes of the officers who visited the premises in November 2012, referred to below, recorded that Mr Torkizadeh stated that he had started selling pizzas about six to twelve months previously.

13. On 8th November 2012, two officers of HMRC made an unannounced visit to The Granary. During that visit, they made observations about the business, its menu, the food and drink displayed and sold and they also inspected the till rolls which showed the recorded split between zero rated and standard rated supplies. Most of the items had been zero rated, including two takeaway pizzas which the officers had observed being purchased, which should have been standard rated. The recent VAT returns had showed that about 75% of the sales were zero rated, which was inconsistent with the officers' observations. HMRC's report of the visit recorded that Mr Torkizadeh was treating all outside catering services and all takeaway food and drink (regardless of whether it was hot or cold) as zero rated. Mr Torkizadeh was given information about the correct VAT treatment of the various supplies.

14. HMRC followed this up with a pre-arranged visit to the Appellant on 22 April 2013. The Appellant was handed various VAT information sheets and notices concerning the correct treatment of sales and the correct VAT treatment of the various types of food and drink sold by the Appellant were discussed at length.

15. It was agreed that the best way of establishing the correct split between zero and standard rated supplies was for the Respondents to conduct invigilation at the Appellant's premises.

16. Two invigilation days were arranged, with the knowledge and agreement of the Appellant on 6 June 2013 and 12 June 2013.This involved officers being present throughout the whole of the trading day on each occasion and recording observations of sales made. The observed sales were then compared with the till records and the results analysed. The analysis showed that the level of zero rated sales averaged 26%, although the subsequent assessment was adjusted in the Appellant's favour, using a figure of 30% zero rated supplies.

17. Of more concern to HMRC was that the observed takings were approximately double the declared takings in the VAT returns, which together with the other business figures suggested that the Appellant was suppressing its takings by 50%. The VAT returns showed average daily gross takings of £200. On 6 June 2013, the takings

were £514.18, excluding purchases made by the officers. It was explained that the figures were distorted by a local school sports day which had increased sales. A reduction of 20% was made to allow for this, though there was no evidence as to why that percentage had been chosen. The takings on 12 June, were £407.75. The contemporaneous notes stated that the Appellant had confirmed on that day trading was as normal, but at the hearing, Mr Torkizadeh said that there had been a sports day at another school on 12 June which had also distorted the takings.

18. HMRC's letter of 26 June 2013 stated they had analysed the VAT returns, the information collected on the two invigilation days and the schedule of VAT assessments. The observed split between zero and standard rated items was 30%/70% (rounded in the Appellant's favour). The letter stated "I have taken on board your comments that the level of standard-rated sales has increased since registration i.e. take-away pizza, jacket potatoes being introduced, and therefore I have staggered the zero-rated allowance to show a higher percentage in the earlier periods."

19. The zero-rated percentage used between periods 08/08 (when the Appellant registered for VAT) and 02/10 inclusive was 50%, between periods 05/10 to 02/12 inclusive 40% and for 05/12 to 02/13 inclusive 30%.

20. At the hearing, HMRC decided not to proceed with the allegations that the takings had been supressed, so that the only area in dispute related to the split between zero rated and standard rated supplies.

21. Following the various checks, The Appellant accepted that the zero/standard rate split had been incorrect and HMRC accepted that the errors in applying the correct split had arisen as a result of the Appellant's lack of experience and knowledge. The correspondence indicates that HMRC had been at some pains to explain the correct VAT treatment of the various items which the Appellant sold. There was, however, no evidence from the Appellant as to what the correct split should have been, either before the hearing or provided at it.

22. At the hearing, Mr Torkizadeh stated that he had made errors in relation to what items should be standard rated; for example, he was unaware that VAT should be added to sales of bottles of water, even if taken away. He agreed that if given the opportunity, he would be able to provide more information to enable a reasoned estimate as to the correct split to be made.

23. With the agreement of HMRC, the hearing was adjourned and Directions were made to give the Appellant 60 days to provide additional information on the split and HMRC a further 30 days after the expiry of that period to review the information and attempt to reach an agreement on the figures. It was agreed that no further oral hearing would be required.

24. *The law*

25. Section 73(1) VATA provides that "*where it appears to the Commissioners that [a VAT return is] incomplete or incorrect, they may assess the amount of VAT due from [the taxpayer] to the best of their judgement and notify it to him*". This is the

provision under which the assessment for £28,436 was issued. The Appellant appealed the assessment under section 83(1)(p) VATA. Under section 84 VATA, the Tribunal can increase the amount of the assessment if it thinks it is too low. Otherwise it can either allow or dismiss the appeal.

26. The Appellant has accepted that the zero/standard rated split was wrong in the periods in question, so that HMRC is entitled to issue an assessment under section 73(1) VATA. The question is whether the amount of that assessment was made to "the best of their judgement".

27. The requirements for a decision to be to the best of HMRC's judgement were set out in the High Court case of *Van Boeckel v C & E Commissioners [1981] STC 290*, where Woolf J, as he then was, said:

"…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…

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."

28. Three further criteria were added in the case of *C A McCourtie LON/92/191* where the Tribunal said "*In addition to the conclusions drawn by Woolf J in Van Boeckel earlier tribunal decisions identified three further propositions of relevance in determining whether an assessment is reasonable. These are, first that the facts should be objectively gathered and intelligently interpreted; secondly, that the calculations should be arithmetically sound; and, finally, that any sampling technique should be representative and free from bias."*

29. *The Appellant's submissions*

30. The Appellant contended (in relation to the allegation of cash suppression though it is also relevant to the zero/standard rate split) that the HMRC officer did not use his best judgement as he extrapolated two day's takings in June 2013 as being representative of the previous four years' takings.

31. Specifically on the rate split, is was submitted that "sufficient consideration not given to different sales mix, …prior to additional tables and chairs being supplied for customers to eat in."

32. *The Respondent's submissions*

33. The decision maker had met the principles of best judgement by basing the assessment on the findings of the two invigilation exercises, taking into account the mitigating factor of the sports day at the local school and discounting purchases made by HMRC personnel and taking account of the differing tax rates over the period.

34. *The post-hearing correspondence*

35. The Appellant's representative provided additional details on 25 April 2016. The information consisted of a schedule headed "Summary of standard rated and zero rated sales". The Schedule had columns headed "cold", "hot", "total" and "output VAT" and there was a further column showing the applicable VAT rate. Figures were provided for each VAT quarter, except that overall totals were shown for VAT quarters ending June 2008 to February 2010 inclusive.

36. We assume that "cold" referred to sales of zero rated food and "hot" referred to the sale of standard rated food, although it had been repeatedly pointed out that many cold items were standard rated. On this basis, the percentage of sales which were claimed to be zero rated differed little from the figures in the original VAT returns and the amount of output tax shown in the schedule as due was also the same as had been declared in the returns. In other words, although the Appellant had recognised that he had zero rated many sales which should have been standard rated and had undertaken to provide revised figures, the figures were not significantly different from those originally submitted.

37. These submissions were made after the time allotted in the Tribunal's Directions and HMRC, in the hope of reaching a settlement, applied to extend the timetable for considering the matter. An extension of time was granted.

38. HMRC then sent its own computation to Mr Arthur with a view to settling the matter. The computation set out the total VAT under-declared as £15,149.92. In arriving at its figure:

- HMRC had used Mr and Mr Turkizadeh's recorded takings and had applied a percentage to determine the zero rated/standard rated split.
- The percentage used was calculated from the observations/invigilations they had carried out
- They had taken account of changes to the rate of VAT
- They had applied different percentages to different periods to take account of the fact that standard rated sales had increased over the period with the introduction of pizzas to the menu and (we infer) that the café had provided additional seating for customers.

39. On 16 June 2016 HMRC submitted an Application to the Tribunal stating that the parties had been unable to reach agreement on the zero rated/standard rated split and requesting the Tribunal to determine the matter. This was copied to the Appellant's representative.

40. By email of 29 June 2016, Mr Arthur raised some queries on HMRC's calculation to which HMRC responded on 1 July 2016.

41. So far as the Tribunal is aware, there were no further negotiations or correspondence between the parties.

42. *Discussion*

43. We find that the zero/standard rate split was wrong throughout the period under consideration. By his own evidence, the Appellant was zero rating many items which should have been standard rated. HMRC's notes of the unannounced visit on 8 November 2012, which we accept, indicate that the Appellant was treating all take-away food, hot or cold, as zero rated as well as all outside catering services (although it seems there were not many occasions when such services were provided).

44. The onus is on the Appellant to show the assessment in incorrect.

45. The question is whether the assessed split was made according to HMRC's best judgement. As set out in the *Van Boeckel* case, he primary obligation is on the taxpayer to produce accurate returns and HMRC is not expected to do the taxpayer's work. HMRC must have some material before them on which they can base their judgement and must fairly consider that material and come to a conclusion which is reasonable and not arbitrary. However, the Court recognised that the person who has access to the relevant information is the taxpayer and the requirement for best judgement does not place a burden on HMRC to carry out exhaustive investigations. The *McCourtie* case added requirements, among others that the facts should be objectively gathered and any sampling technique should be representative and free from bias.

46. HMRC based their calculations of the rate split primarily on the invigilation days, although observations were also made on the 8 November 2012 visit that "a large proportion of supplies were standard rated" which did not reflect the recent VAT declarations which showed zero-rated supplies of approximately 75%.

47. HMRC's letter of 26 June 2013 noted that the level of standard rated sales had increased since registration and accordingly, the split used in the assessment varied, with the proportion of zero-rated sales starting at 50% and falling to 40%, then 30%.

48. The timing of the fall to 30% correlates with the latest time mentioned by Mr Torkizadeh at the November 2012 visit, of when he began to sell pizza, although he might have been selling pizzas for some time before that.

49. The correspondence does not specifically say that the increase in the amount of seating was taken into account in determining the split but nor was there any evidence as to how the additional seating affected the type of sales, given that take away hot food and drinks are standard rated in any event.

50. It might be argued that two days of invigilation, one week apart and the short visit in November 2012 did not represent a "sampling technique which was representative and free of bias" as the trade might have varied in different seasons or depending on whether the local school was on holiday or not. However, we consider that the invigilation exercise, as a technique, is an objective and reasonable one. Whilst is might have been appropriate to make further observations, it is important to remember that the primary obligation to provide the relevant information is on the taxpayer, who has access to that information, and HMRC does not have to conduct "exhaustive investigations". The investigations must be reasonable and proportionate and in a case such as the present one, it would be unreasonable to expect HMRC to conduct numerous invigilations over a long period.

51. Mr Torkizadah had not provided any evidence as to the zero/standard rate split before or at the hearing. Following the hearing he was given the opportunity to produce revised figures taking account of his acknowledged errors. The Appellant's calculations submitted after the hearing did not in fact take account of those errors. Nor were any reasons given as to why those calculations should be regarded as correct.

52. HMRC has made reasoned calculations on the basis of the materials and information available to them and has taken the changing pattern of sales into account, so far as possible, on the basis of that information.

53. We accordingly consider that HMRC made the assessments to the best of their judgement.

54. It is for the Appellant to show, on the balance of probabilities, that the assessment was incorrect and this he has failed to do.

55. *Decision*

56. For the reasons set out above we allow the appeal so far as it assesses an additional amount of VAT by reason of the suppression of takings, but we dismiss the appeal so far as is relates to HMRC's assessment of the split between zero and standard rated supplies.

57. We direct HMRC to issue a revised assessment on the above basis.

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.

MARILYN MCKEEVER
TRIBUNAL JUDGE

RELEASE DATE: 1 AUGUST 2016