[2017] UKFTT 653 (TC)

TC06080

Appeal number:TC/2015/06578

VAT –under declared sales– business use of car - best judgment – appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

BEST BUY COMMUNICATIONS LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE IAN HYDE
PHILIP JOLLY

Sitting in public at Birmingham on 4 April 2017

Mr M Sarwar for the Appellant

Mr D Ridley, presenting officer, for the Respondents

DECISION

1. This appeal concerns assessments raised by HMRC for under declared output tax in respect of misdescribed sales, road fuel scale charges and related penalties.

2. The appellant is a VAT registered business selling second hand mobile phones and accessories.

3. Evidence was given by Mrs Kirsty Williams, an Assurance Officer employed by HMRC with particular expertise in examining tills and by Mr Liaqat Ali Khan, the appellant's accountant. Mr Khan also produced a witness statement. There was also produced to the Tribunal an unsigned witness statement from Mr Imran Butt, a director and owner of the appellant but Mr Butt did not attend because he was unwell. The two witness statements were very similar and, where necessary we have adopted the evidence of Mr Khan, being an accountant familiar with his client's business.

The facts

4. On hearing the evidence we find the facts to be as follows.

5. In May 2012 during a corporation tax enquiry into the appellant HMRC decided in the absence of prime records it needed to investigate the appellant's till rolls and Mrs Williams was asked to carry out the investigation.

6. On 16 October 2012 HMRC made an unannounced visit to the appellant's premises but were refused entry.

7. On 3 December and 13 December 2012 by agreement Mrs Williams and other colleagues from HMRC made visits to the appellant's premises. During the first visit Mrs Williams investigated the till, produced till reports and ensured the till was set to produce information on the till reports that HMRC wanted to see. On the second visit Mrs Williams obtained till reports detailing transactions that took place between the first and second visit.

8. On 4 January 2013 HMRC wrote to Armstrongs, the appellant's then accountants, raising concerns over the till printouts. Armstrongs advised that the discrepancies were due to incorrect use of the till and because the till readings covered the period including the run-up to Christmas, Black Friday and introduction of a new iPhone.

9. In February 2014 the appellant's new accountants, AKA, advised that the till was used as a cash box with daily gross takings recorded upon cashing up at the end of the day. Daily gross takings would consist of money in the till (cash plus chip and pin receipts) less £100 float. The till readings could not be relied upon due to mistakes by the director and staff. For example HMRC's reports showed two cancelled sales of £350,045 which were clearly errors. The appellant could provide records from VAT period 03/13 onwards.

10. AKA notified HMRC in May 2014 that the appellant was operating the VAT margin scheme for second-hand goods.

11. Following a further visit to the appellant's premises on 15 December 2014 HMRC notified the appellants accountants by letter dated 19 December 2014 of discrepancies including input tax reclaims on fuel costs relating to a Mercedes car where no road fuel scale charges had been declared.

12. On 5 January 2015 the appellant accountants accepted a number of errors but claimed that the Mercedes was used for 100% business use. HRMC asked to see the Mercedes insurance policy but the accountants refused on the grounds that it would not prove anything about business use.

13. On 14 May 2015 HMRC issued a notice of assessment under section 73 Value Added Tax Act 2004 ("VATA") for £93,305.61 but, following an internal review, it was amended by a review decision letter of 27 October 2015 whereby;

(1) the assessment in relation to under declared sales was removed in full;

(2) the assessment for £405.36 for road fuel scale charges in the VAT periods 06/11 to 12/14 remained in place; and

(3) the assessment for under declared output tax in relation to sales misrecorded as returned goods for VAT periods 06/11 to 12/12 was reduced to £3,388

14. In assessing for the under declared output tax relating to returns, HMRC used the information obtained from interrogating the till during the December 2012 visits. 18 transactions described as returns were noted over the eight week period from 19 October 2012 to 2 December 2012, being;

(1) 19 October – 2 December 2012 - 12 totalling £3,671 with an average value of £305.91

(2) 3 December – 12 December 2012 – 6 totalling £688 with an average value of £114.66

giving a total value of £4,339 and an average return value of £242. Due to the nature of the business HMRC discounted two returns per month over the three month period, leaving 12 returns at an average of £242, being £2,904 of suppressed gross sales per quarter. Applying that amount to the periods under assessment at the relevant VAT rate produced under declared output tax of £3,388.

15. On 30 October 2015 the appellant appealed this assessment.

16. On 23 February 2016 penalty assessments were issued being £56.31 in respect of the road fuel scale charges and £660.66 in respect of output tax for returned goods.

17. The appellants appealed the penalty assessments, the penalty appeals being consolidated with the substantive appeals. However the penalties have been

suspended and are not now being disputed by the appellant except to the extent they depend on the outcome of the substantive VAT appeal.

Legislation and case law

18. Regulation 31(1) of the Value Added Tax Regulations 1995 provides;

> (1) every taxable person shall, for the purposes of accounting for VAT , keep the following records-
>
> (a) his business records
>
> (b) his VAT account
>
> ….
>
> (i) all credit notes, debit notes, or other documents which evidence an increase or decrease in consideration that are received, and copies of all such documents that are issued by him…."
>
> (2) the Commissioners may [for the purposes of any scheme]….supplement the list of records required in paragraph (1)"

19. VAT notice 4.4, which applies to traders such as the appellant within the retail point of sale scheme provides

> "…you must keep a record of your [Daily Gross Takings]. You must include in your DGT record;
>
> - all payments as they are received by you….from cash customers for your retail supplies;
> - the full value , including VAT, of all your credit or other non-cash retail sales at the time you make the supply; and
> - details of any adjustments made to this record"

20. Section 73(1) VATA provides;

> "(1) 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 that due from him to the best of their judgement and notify it to him"

21. Section 83 VATA provides :

> " subject to section 84, an appeal shall lie to a tribunal with respect to any of the following matters….
>
> (p) an assessment-
>
> (i) under section 73(1) or (2) in respect of a period for which the appellant has made a return under the Act…

…or the amount of such an assessment"

22. Section 73 and its predecessor provisions have been considered on a number of occasions by this Tribunal and the higher courts.

23. In *Van Boekel v Customs and Excise Commissioners* [1981] STC 290 Woolf J 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. 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 judgement as to what tax is due.
>
> Thirdly, it should be recognised, particularly bearing in mind the primary obligation … 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 judgement" 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 materials being placed before them."

24. The distinction between the supervisory jurisdiction of the tribunal to determine whether HMRC has properly exercised best judgment within section 73 and the Tribunal's fact finding jurisdiction to consider whether the assessment was correct was addressed by Chadwick LJ in *Rahman v Customs and Excise Commissioners (No2)* [2002] EWCA Civ 1881 who at [42] agreed with the following observations of Carnwath J in Rahman (No1) [1998] STC 826 at page 840, commenting on Woolf J's guidance in *Van Boekel*;

> "I do not wish to diminish in anyway the importance of guidance given by Woolf J [in the *Van Boekel* case] to customs officers as to how to exercise their best judgment when making assessments. However, when the matter comes to the tribunal it will be rare that the assessment can justifiably be rejected altogether on the ground of a failure to follow that guidance. The principal

concern of the tribunal should be to ensure that the amount of the assessment is fair, taking account not only the commissioners' judgment but any points raised before them by the appellant"

25. In *Customs and Excise Commissioners v Pegasus Birds* [2004] EWCA Civ 1015 Carnwath LJ in the Court of Appeal at [29] stressed the importance of finding the right amount of tax;

"in my view the tribunal faced with "a best of their judgment" challenge, should not automatically treat it as an appeal against the assessment as such, rather than against the amount. Even if the process of the assessment is found defective in some respect applying the *Rahman (2)* test, the question remains whether the defect is so serious or fundamental that justice requires the whole assessment to be set aside, or whether justice can be done simply by correcting the amount to what the tribunal finds to be a fair figure on the evidence before it. In the latter case the tribunal is not required to treat the assessment as a nullity, but should amend it accordingly"

26. Carnwath LJ commented further at [38] by way of guidance to the tribunal;

"(1) 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 that time of the assessment"

HMRC's assessment and the parties' arguments: road fuel scale charges

27. In reviewing the VAT records HMRC noticed that the appellant had recovered input tax on diesel purchased for a Mercedes E-class car but there was no evidence of road fuel scale charges, detailed mileage records or any apportionment calculation between business and non-business use.

28. HMRC took the view that the journey from home to business and vice versa was a private journey for VAT purposes and, as the business premises were located away from where Mr Butt lived and the Mercedes was available to him to get to and from home to the shop the vehicle could not have been used 100% for business purposes. There was no evidence that the car was garaged at the business premises and, the appellant having refused to supply any insurance documentation, there was no evidence of any business only insurance provision. HMRC therefore concluded the car was not used the business only purposes and have assessed for road fuel scale charges.

29. The road fuel scale charges were calculated using the CO2 emissions from the current Mercedes-Benz E class brochure. The emission range in the brochure for the various diesel engines in E-classes was found to be from 114 to 136. HMRC based the assessment on the lowest of the values being 114.

30. The appellant did not challenge the calculation of the road fuel scale charge but whether it should be imposed. The appellant's position was that Mr Butt used the Mercedes entirely for business use and a separate vehicle was available for private use. The Mercedes was kept near the premises and the other car used for driving to and from home. Further, the mileage was consistent with business only use.

HMRC's assessment methodology and parties' arguments: returned sales

31. HMRC argue that, as the appellant was not at the time of these transactions operating the second hand margin scheme, the appellant was within the retail point of sale scheme and so should have kept, in accordance with VAT Notice 727 section 4.4, "details of any adjustments made to this record", that is to say where goods have been returned. There were no such records.

32. In the absence of any evidence to the contrary HMRC concluded that sales have been under declared because they have been misdescribed as returned goods and, the appellant not having kept sufficient records, were entitled to assess the appellant under section 73 in respect of these errors.

33. In determining the tax due to their best judgment, HMRC had limited information available and so used the information obtained from interrogating the till during the December 2012 visits.

34. As to the number of returns, HMRC in its submissions to this Tribunal applied a credibility check grossing up the 18 returns over 8 weeks of the sample period to 29 over a full VAT period of 13 weeks. In HMRC's view assessing on the reduced number of 12 returns must therefore represent best judgment.

35. HMRC are content with the methodology and accuracy of their assessment and point out that the burden of proof is on the appellant to prove the assessment wrong.

36. The appellants argued that the till records were inherently unreliable. The till was used as a cashbox and the readings could not be relied upon due to mistakes by the directors and staff, for example HMRC's reports showed two cancelled sales of £350,045 which were clearly errors and accepted by HMRC as such.

37. The appellants made a number of criticisms of HMRC's approach and methodology, focusing on the details of how the till investigation was carried out. The criticisms included;

(1) the officers running the corporate tax investigation, which ran for some three years, had access to all relevant records including purchase and sales invoices, bank statements for their business and the family did not raise an assessment.

(2) The sample period was unrepresentative because the till readings covered the period including the run-up to Christmas, Black Friday and introduction of a new iPhone.

(3) Mrs Williams' failure to find the red book in which was recorded daily sales and which was being held by her corporate tax colleagues

(4) There were discrepancies in the dating and timing of the printouts and other aspects of the investigation

(5) Mrs Williams interviewing Mr Butt's son on her visits to the premises

(6) The facts that some 95% of the original assessment has been withdrawn because of errors

38. HMRC argue that these matters do not affect the assessment. In particular, the fact that the officers running the corporate tax investigation did not raise an assessment was not relevant.

39. Mrs Williams asked several times for records of daily gross takings and returns and was never supplied with anything or told about the red book. In any event that related to earlier periods and if it was being kept by her corporate tax colleagues, the business should be recording the same information for recent periods in a different format.

Decision on road fuel scale charges

40. There is no argument between the parties as to the amount of the assessment but whether the Mercedes car is used solely for business purposes or partly business and partly private purposes.

41. Whilst it is to an extent an all or nothing decision, we consider that nevertheless the two stages of the Tribunal's jurisdiction are nevertheless engaged. Did HMRC exercise best judgment and, is the amount of tax assessed the correct amount (being in effect a choice between the amount assessed or nil).

42. In our view, HMRC exercised best judgment and the appellant has not produced any evidence to discharge its burn of proof in this appeal. The appellant argued that it could not produce the insurance because at the time Mr Butt was in hospital. However, neither HMRC not this tribunal has been presented with the certificate or any other evidence since then that the car was not used for private use, and in particular the drive between home and the business.

43. We therefore consider that the appellant has failed to discharge the burden of proof and its appeal in respect of the road fuel scale charges is dismissed.

Decision on returned sales

44. HMRC is only entitled to raise an assessment if one of the conditions within section 73 are satisfied. The appellant has failed to show any records for returns for the relevant periods and so we find that HMRC is entitled in principle to issue a Section 73 assessment.

45. We are conscious of the guidance in the case law, and in particular that of Carnwath LJ in *Pegasus Birds* that our primary task is to find the correct amount of tax.

46. We accept the appellant's evidence that the staff did not operate the tills properly and that they the data produced by them was inherently unreliable.

47. The appellant also made a number of detailed criticisms of HMRC's approach and methodology in carrying out the investigation and raising the assessment. However, having considered them, save as set out below, we do not find them to be material to the assessment or the appeal. Specifically, whilst we find fault in the assessment as described below, we do not accept the appellant's argument that HMRC and Mrs Williams specifically were unprofessional. We found Mrs Williams to be an honest and credible witness.

48. It is unfortunate that the VAT investigation and the corporation tax investigation did not communicate, as it appears the corporation tax team had more information which may potentially have been useful, for example the red book. This would not have been the "exhaustive investigations" which Woolf J said HMRC should not have to carry out. On the other hand the appellant did not volunteer the information.

49. HMRC's methodology appears to have two defects. First, HMRC's calculations appear to understate the number of returns and, second, the value of each return does not appear to be credible.

50. As to the number of returns, HMRC's sample period identified 18 returns over an 8 week period. HMRC, in order to calculate the number of returns, then discounted this number by 2 per month to reach 12 and applied 12 returns to each quarter.

51. HMRC's initial calculation ignores the fact that a quarter is three months not the 8 weeks of the sample period and so the 18 returns should have been uplifted. However, in its submissions to this Tribunal HMRC applied a credibility check grossing up the 18 returns over 8 weeks of the sample period to 29 over a full VAT period of 13 weeks. In HMRC's view assessing on the reduced number of 12 returns must therefore represent best judgment. It is therefore part of HMRC's case that 12 returns over a quarter is accurate and we see no reason to disturb it.

52. As to the average value of a return, a value of £242 in a shop that sells second hand phones and accessories is extremely high. The appellant could not identify to the Tribunal any items that were sold by the shop of that value, let alone sufficient to compensate for the other small value items such as phone covers. This was supported by Mr Khan's witness statement in which he said that the appellant sold phone accessories between £5 and £20, second hand phones between £20 and £100 subject to the rare sale of expensive phones like iPhones. Nevertheless, the appellant did not produce any evidence to positively assert any value. However, on the other hand HMRC did not provide any supporting evidence to justify that value other than the mathematics of the data from the sample period. Indeed at the hearing HMRC could

not justify the value of £242 or even comment on whether an average of £50 was too high or too low.

53. We accept that HMRC do not need to carry out an exhaustive investigation but checking for price lists or asking for average sales values as a check would not have been onerous in the context of an average value that ought to have been clear to HMRC as being excessive. In our view HMRC have not considered the nature of the trader in making the assessment and that the decision to assess at an average return value of £242 was not reasonable. It may well have been that the returns calculation was relatively minor part of a wider assessment but that does not justify sensible checks on the amounts being assessed.

54. However, conscious of the guidance from the courts, we do not think the errors justify setting aside the assessment but instead amend the assessment to reflect a return value of £50 being a figure closer to the likely true average value of returned goods.

55. The appellant's appeal in respect of the assessment of returns is accordingly allowed in part and the appeal in respect of fuel scale charges dismissed.

56. The penalty assessment in respect of output tax for returned goods shall be amended commensurate with the decision and amended assessment in paragraph 54 above.

57. 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.

IAN HYDE
TRIBUNAL JUDGE

RELEASE DATE: 29 August 2017