TC02469

Appeal number: TC/2011/01588

TYPE OF TAX – VAT – assessment – VATA 1994 section 73 - best judgement - appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

PETER WHITEHOUSE trading as FREEMASONS ARMS **Appellant**

- and -

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

TRIBUNAL: JUDGE ALISON MCKENNA
TERENCE BAYLISS FFA FAIA

Sitting in public at Priory Courts, Birmingham on 11 December 2012

The Appellant appeared in person

Mrs P Checkley of HMRC appeared for the Respondents

DECISION

1. This appeal concerns best judgement VAT assessments issued to the Appellant in respect of the Freemasons Arms, a public house of which the Appellant was the sole proprietor from August 2004 until October 2006.

2. The assessments in dispute in this appeal are: for the 07/05 period, £7103; for the period 10/05 to 07/06, £4290 and for the final period £8382. At the Appellant's request, the assessments were reviewed by HMRC and upheld by the reviewing officer on 4 November 2010. The Appellant's Notice of Appeal was dated 17 January 2011 but the Tribunal gives permission for the appeal to proceed out of time. HMRC accepted the Appellant's hardship application, so allowing the appeal to proceed without prior payment of the tax due.

The Evidence

3. The background facts were largely agreed by the parties. The Appellant failed to file a number of VAT returns at the proper time in respect of the Freemasons Arms. An officer from HMRC met with the Appellant and his accountant and later inspected the pub premises. The Appellant explained that he had employed a manager for the pub who had proved to be unreliable. He accepted that the business had, in those circumstances, maintained inadequate records. He was notified by HMRC that assessments would be raised.

4. HMRC inspected the business records available and found that there were no till rolls or "Z" readings held. The sales declared for the missing periods were not verifiable in view of the absence of these records. The business expenditure had been reconstructed by the accountants to the best of their ability. The Appellant's accountant accepted that he had completed the year end accounts with estimated figures. By the time of HMRC's visit in 2008, the Appellant had ceased to be the proprietor of the Freemasons Arm, having sold the lease, and so it was not possible to observe current trade.

5. The Tribunal heard sworn evidence from Mr Bourne of HMRC, who had made the best judgement assessment. He had filed a witness statement dated 28 September 2011, detailing the history of his involvement with this case. He described his meeting with the Appellant and his accountant and his concern about the poor business records. He explained that he had raised his assessment with reference to the records available, including the VAT return for the VAT period 04/06 and the accountants' record of expenditure. He had used these records as a basis for assessing the mark up applied to drink and food sales for the periods under assessment, taking into account the cost of goods for re-sale and the declared input and output tax on the VAT return. He had estimated the mark up rate as 97.5% and invited the Appellant to produce evidence as to why the business would not have achieved that level of mark up in the periods for which records were missing. He explained that as the mark up figure was based on actual sales rather than anticipated sales it already took wastage

into account. In the absence of any evidence to the contrary, he had considered it reasonable to replicate this level of mark up for the best judgement assessments.

6. Mr Bourne had engaged in quite a lengthy correspondence with the Appellant's accountants in 2009 and 2010, with regard to the level of mark up applied and the consequent assessment figures. This correspondence was before the Tribunal in its bundle of evidence. Mr Bourne had issued a detailed letter in August 2008 explaining the methodology behind his best judgement assessments. He had answered the accountants' detailed questions about the calculations based on this methodology. The Appellant's accountants had suggested that a more reasonable approach to best judgement would be for HMRC to apply the level of mark up for the four best selling drinks sold in the pub over the periods under assessment, as such figures were verifiable with regard to industry standards and would produce a mark up figure of 76% for the business as a whole. Mr Bourne explained that, as the pub had operated a restaurant, he did not consider this to be a reasonable approach and that it would in any event produce a lower level of mark up than the actual figures in bench mark period. Mr Bourne told the Tribunal that in his experience, any business selling food would achieve a mark up of at least 100% and often between 200 and 500%. He accepted that the Freemasons Arms had not been a "gastro-pub", but his experience was that even a take away food business would have a mark up in the region of 150 to 200%. He said that in the absence of reliable records he had not been able to form a firm view about the ratio of food to drink sales achieved by the business and had not received any satisfactory evidence from the accountants on this point. In the circumstances he maintained that the best judgement assessments he had issued were reasonable, based upon an analysis of actual trade in a period for which there had been a VAT return and applying the same mark up across the business as a whole to the periods under assessment. The Appellant did not wish to ask Mr Bourne any questions in cross examination.

7. The Appellant gave oral evidence to the Tribunal but did not produce any fresh documentary evidence. He explained that the business records had been left in a mess by his former employee and that he was unhappy about it because in his other business (as an electrician) he had never had any difficulty with HMRC. He had taken over the pub for a short period while the employee was on leave and had only then realised the extent of the problem. He had signed VAT returns prepared by others but not checked the figures. He had then taken over the running of the pub himself, with the help of his family, from May or June 2006 until he sold it in October 2006. He said he had found himself to be liable for considerable debts after the sale, as he had discovered that the business owed rent and payment for beer in addition to VAT.

8. He told the Tribunal that the Freemasons Arms was a working man's pub, located a mile from the town centre. He said that its trade had suffered from the smoking ban, to the point where there was one day when he remembered that the entire takings were £65. The pub had sold hot food such as cheese pie, fish and chips, or liver and onions at lunch time. It did not sell cold food. It had sold two main meals for £5 at lunch time. He said he had had to insist that the customers also purchased a drink at lunchtime, as they had not always done so. He said that he faced

fierce competition and under-cutting from another local pub, so that the food sales had to be priced accordingly. He had sold more expensive main meals such as steaks in the evening. He had employed one member of staff in the kitchen only and the restaurant could seat 30 people.

9. In answer to questions from Mrs Checkley, Mr Whitehouse told the Tribunal that he had invested in the kitchen when he took over the pub simply because its equipment needed replacing. He had installed fridges, fryers, hot plates and extractors. He had also re-furbished the seating in the pub. He said it just needed doing and it was not his intention to increase the food sales. He denied having told Mr Bourne that he had spent £90,000 on kitchen refurbishments.

10. In answer to questions from the Tribunal, Mr Whitehouse stated that if the pub had takings of £2500 including VAT over a week, he estimated that only £500 would be derived from food sales. He described how food stock was purchased and delivered twice a week and that all the drinks had to be purchased from the brewery. His manager had handled the ordering of food and drink. He said he had not received discounts from the brewery depending on the level of beer sales and that he was not required to sell food by the terms of his lease. He said he had expected to make a profit of 25 or 30 pence for every pound taken. Mr Whitehouse told the Tribunal that the mark up figure relied upon by HMRC in making the best judgement assessment was "ridiculous".

11. In view of the fact that the evidence given by Mr Whitehouse at the Tribunal hearing was new to HMRC, the Tribunal asked Mr Bourne to comment on whether anything he had heard would cause him to change his view as to best judgement. He said it had not. He was familiar with this type of pub and said that many of them are run profitably. He repeated that the business had achieved a 97.5% mark up in the period he had used as a bench mark and that Mr Whitehouse had not explained why the business would not have achieved the same mark up in later periods. His view remained that the mark up figure used for assessment must be higher than that for beer only in view of the catering aspect of the business and his opinion, based on his experience, was that 97.5% was a low mark up figure for the catering industry.

The Law

12. 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.

13. 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 somewhat unclear on which aspect was challenged, but the Tribunal treated this appeal as one concerning both the reasonableness of the best judgement approach 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.

14. Mrs Checkley referred the Tribunal to a number of first instance decisions regarding appeals against best judgement assessments. Decisions made at first instance do not have precedent value and we are not bound to follow them.

15. 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 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.

16. The Tribunal also had regard to the comments of Woolf J (as he then was) in *Van Boeckel v Customs and Excise* [1981] STC 290 to the effect that it is perfectly proper for HMRC to take the results thrown up by a test period into account in making a best judgement assessment.

Conclusion

17. The Tribunal found Mr Whitehouse to be an honest witness, although unfortunately he was vague in his recollection of key details and had no additional documentation available to assist him in his appeal. It was clear that he had not paid close attention to the running of the business as when essential record-keeping had been neglected by staff he had not discovered this promptly. The Tribunal also formed the view that Mr Whitehouse had not had good knowledge of business expenditure and we suspect that the cost of goods for re-sale might well have been higher than the figure the accountants had supplied, especially given the absence of stock records. However, this is a case in which, unfortunately, there was an absence of evidence to support our suspicion and accordingly we have no basis upon which to reduce the assessments under appeal.

18. Mr Whitehouse bears the burden of proof of satisfying the Tribunal that HMRC's best judgement assessment was not reasonable. We conclude that the statutory conditions for making the assessment were satisfied in view of the Appellant's failure to keep proper records. We also conclude that, on the material available to HMRC, the assessments represented a reasonable exercise of its best judgement, based on a test period for which figures were available. We do not regard the Appellant's accountants' suggested approach as a reasonable one, given that it bases its assessment only on beer sales and does not take into account the food sales, which we find to have been an important element of the pub's trade. We were not satisfied by Mr Whitehouse's evidence that food accounted for as little as one third of the pub's sales. Our own impression, based upon the bench mark period figures which HMRC had used and which were made available to the Tribunal, was that

drink and food sales accounted for roughly equal halves of the pub's sales. We cannot make a finding of fact to that effect as the Appellant disputed it and Mr Bourne said he had not considered the records to be sufficiently reliable to make that assessment. However, we conclude that the food sales were not an insignificant part of the business and in those circumstances we are satisfied that it would not have been reasonable for HMRC to exclude the generally higher mark up on food sales from its assessment altogether.

19. Mr Whitehouse also bears the burden of satisfying the Tribunal that the amounts of the assessments were wrong and should be varied on the basis of the facts as found by the Tribunal. However, he produced no evidence upon which the Tribunal could rely and Tribunal was unable to make a finding of fact on the basis of Mr Whitehouse's unsupported assertion that there was generally a much lower mark up figure applied than that evidenced in the earlier benchmark period. Accordingly, we find that the Appellant did not discharge his burden of proof and we must conclude that the assessments are for the correct amounts.

20. In all the circumstances, we now dismiss this appeal and confirm the assessments.

21. 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: 8 January 2013