TC06405

Appeal number: TC/2016/03458
TC/2016/01237

INCOME TAX AND VAT – whether sales under-declared – presumption of continuity – quantum of closure notices and discovery assessment – whether VAT assessments to best judgment – whether behaviour 'deliberate and concealed' – whether sufficient reduction for disclosure

FIRST-TIER TRIBUNAL
TAX CHAMBER

SHAH AZIZ **Appellant**

- and -

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

TRIBUNAL: JUDGE VICTORIA NICHOLL
MICHAEL BELL ACA CTA

Sitting in public at Taylor House on 19 -20 February 2018

Mr Geoffrey Potter of Potter & Co for the Appellant

Mr Goulding, Officer of HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. The Appellant (Mr Aziz) carried on a restaurant business as a sole trader from 1 February 2007 to cessation on 31 March 2016. The Respondents (HMRC) visited the restaurant as part of its Restaurant Task Force in 2013 and, following an enquiry into under-declared income, issued closure notices and assessments under sections 28A and 29 Taxes Management Act 1970 (TMA) on 6 July 2015 and 2 September 2015, VAT assessments under section 73(1) Value Added Tax Act 1994 (VATA) on 25 September 2015 and penalty assessments under Schedule 24 Finance Act 2007 (Schedule 24) on 17 November 2015. These have since been amended to the following amounts (excluding interest) for the relevant periods as shown below:

Tax Year	Income Tax & Class 4 NICs discovery assessment section 29 TMA	Income Tax & Class 4 NICs closure notice section28A TMA	Income Tax & Class 4 NICs Penalty schedule 24		VAT Periods	VAT assessment (issued 03.02.16) section 73(1) VATA	VAT Penalty (revised 23.02.16) schedule 24
2012	£10,850.28		£7,595.19		07/11- 04/12	£4,902	£3,431.40
2013		£10,702.57	£7,491.79		05/12 - 04/13	£5,109	£3,576.30
2014		£11,214.42	£7,850.09		05/13 - 04/14	£4,546	£3,182.20
2015					05/14 - 01/15	£3,461	£2,422.70
Totals	£10,850.28	£21,916.99	£22,937.07			£18,018	£12,612.60

2. Mr Aziz appealed against the assessments within the statutory periods. At the hearing his representative, Mr Geoffrey Potter, focussed a significant proportion of his submissions on the manner in which the enquiries had been carried out and his

intention to make a complaint regarding HMRC's conduct. Mr Potter acknowledged that these issues are not within the Tribunal's jurisdiction, but he considered that HMRC's behaviour affected their ability to use 'best judgment' in making the assessments. The substantive grounds of Mr Aziz's appeal are set out in paragraphs 5 and 6 below. The evidence and findings of facts set out in paragraph 4 below include those relevant to the issues for determination in this appeal, being:

2.1 Whether there was under-declared income;

2.2 Whether HMRC's assessment of the quantum of the adjustments to be made to the self-assessment returns for the under-declared income is soundly based;

2.3 Whether the discovery assessment for 2012 is in accordance with section 29 TMA and whether the presumption of continuity applies;

2.4 Whether HMRC's assessment of the adjustments to be made to the VAT returns for the relevant periods are to HMRC's 'best judgment';

2.5 Whether the penalties have been correctly imposed and whether the under-declarations, if made, were 'deliberate and concealed'; and

2.6 Whether the correct reductions have been given for disclosure.

3. Mr Aziz appealed to the Tribunal in respect of the income tax and class 4 NICs decisions on 25 February 2016 and on 21 June 2016 in respect of the VAT decisions. We noted that the appeal in respect of the VAT decisions was some days late, but as this short delay arose because of ongoing correspondence between the parties and as HMRC do not object to the late appeal, we gave permission for the late notice of the appeal to the Tribunal.

Evidence, facts and findings

4. We were provided with two large documents bundles, including 367 pages of correspondence between the parties, and an authorities bundle. We heard oral evidence from HMRC officers Peter Le Morvan and Tracy Wellington, who are both in the Taskforces & Specialist Compliance Team. Mr Aziz signed a witness statement on 10 October 2017. As he chose not to give evidence at the hearing, the witness statement is set out in full below:

"I, Shah Baky Aziz (the Appellant) confirm that I have provided information to various representatives of HM Revenue & Customs in connection with their enquiries related to this case including interviews, provision of documents and explanations where possible both directly and through my Agent, Mr Geoffrey Potter of N W Potter & Co. All information that I have provided is included in the List of Documents prepared by Mr Potter as part of the Appeal procedure."

Mr Potter asked to give evidence, but this was limited to the matters of which he had direct knowledge. He has not been involved in the day to day operation of the trade at any stage and did not purport to be in a position to give evidence about these matters.

On the basis of the evidence we make the following findings of fact:

Background

4.1 Mr Aziz operated a restaurant business as a sole trader from 1 February 2007 to cessation on 31 March 2016, trading as the Rajasthan Restaurant. Mr Potter has acted as Mr Aziz's accountant and tax adviser since 5 February 2002. He carries out the accounting and tax work using the cash accounting paperwork, including cash books and daily reports of takings ('cash ups') prepared by Mr Aziz. The daily cash ups are carried out at the close of each day's business. Mr Aziz carries these out if he is there at close, but his brother or other members of staff will do this in his absence. The front sheet records the cash and card receipts for the day and the meal bills and card receipts are attached. These bundles are collected by Mr Aziz when he collects the laundry the following day, but they are not checked by him.

4.2 Mr Aziz was selected for a compliance check centrally as part of HMRC's Restaurants Taskforce Project. This cross-directorate taskforce was formed following the government's 2010 spending review which allocated funds to combat fraud and evasion. Mrs Caroline Lane was appointed as the lead officer for the case and she completed paperwork to carry out covert activity at the Rajasthan Restaurant. The covert checks were to carry out test purchases in accordance with the procedures set out by the taskforce. These included a direction to the officers to complete a record of their visits to note the food ordered and the cash payment made by the officer, and to record the number of staff and customers present in the restaurant at the time of the visit, any takeaways leaving the premises and any other orders overheard. The officers were instructed not to record personal information, such as the names of staff members present. The meal bill for each test purchase was to be left on the table following payment in cash. The officers involved in test purchases were briefed and de-briefed prior to each tranche of test eats.

Test Purchases

4.3 The twenty-one test purchases took place on seven days in 2013 on the dates shown in the table below. The right hand column shows whether the test purchases made were included in the cash ups for the relevant day's sales. This check was carried out by HMRC when they were given access to Mr Aziz's accounting records in 2014 and the relevant paperwork is included in the Tribunal's bundle. We find that the test purchases listed with 'no' in the right hand column were not included in Mr Aziz's sales records:

Date of test purchase	Cost / food type	Included in daily report 'cash up'
7.02.13	£17 / takeaway	yes
7.02.13	£24.65 / takeaway	yes
7.02.13	£19.35 / takeaway	no
8.02.13	£34.65 / takeaway	no

8.02.13	£16.30 / takeaway	no
8.02.13	£22.05 / takeaway	no
9.02.13	£24.50 / takeaway	no
9.02.13	£29.65 / takeaway	no
9.02.13	£22.55 / takeaway	yes
16.05.13	£55.30 / restaurant	yes
16.05.13	£34.75 / takeaway	no
16.05.13	£61.25 / restaurant	no
18.05.13	£68.40 / restaurant	no
18.05.13	£24.95 / takeaway	no
18.05.13	£70.15 / restaurant	no
23.05.13	£62.15 /restaurant	no
23.05.13	£28.70 / takeaway	yes
23.05.13	£56.35 / restaurant	yes
25.05.13	£60.90 / restaurant	yes
25.05.13	£37.50 / takeaway	yes
25.05.13	£74.45 / restaurant	yes

4.4 Following the first set of test purchases Mrs Lane authorised a visit by HMRC to Mr Aziz's restaurant on 12 February 2013 to check the cashing up exercise on that date. Mr Aziz was present and allowed the officers to carry out their checks. The purpose of the visit was to allow HMRC to record the amount of cash as compared to the amounts of card payments on that date.

Opening of the enquiries, access to records and 'additional errors'

4.5 Following the test purchases and cash up visit Mr Le Morvan opened an enquiry into Mr Aziz's VAT returns on 22 October 2013 and Mrs Lane issued a formal notice of her enquiry into Mr Aziz's self-assessment for the year ended 5 April 2013 on 6 March 2014. HMRC were given access to Mr Aziz's business records when requested. HMRC carried out a detailed check of the daily cash ups for a three month

period from 1 April 2013 to 30 June 2013 to determine if the receipts for each day tallied with the total on the daily report front sheet. The check established that the daily reports failed to include all of the sales for which meal bills were retained in the addition of total sales and that there were errors in the additions of meal bills ('additional errors'). These errors came to £ 644.95 over the three month period.

4.6 After receiving notification of the 'additional errors' at a meeting on 7 March 2014, Mr Aziz and Mr Potter went through the source records for each day of the year to 5 April 2013. Mr Potter wrote in an email on 10 April 2014 that "we maintain the accounting records from the source records supplied to us by Shah Aziz. I have stated, however, that the sales income information is taken only from the summaries supplied by Shah Aziz and it has become clear that these summaries are not an accurate record of the actual source information." It was conceded by Mr Aziz that this check had revealed that in some cases the summaries do not agree with the actual documents (meal bills) attached to them. Mr Potter's analysis showed that a number of cash sales invoices were not included, that errors were made in the daily additions and that a whole day's takings had been omitted on 31 March 2013. Mr Potter concluded that there was an accumulated error for the year to 5 April 2013 of £3,280.45 in gross sales and £95.80 in tips, and accepted that income tax and VAT would be due on these omissions.

4.7 Mr Potter said in his letter of 1 August 2015 that he did not carry out the same checking exercise for the year ended 5 April 2014 due to the amount of time involved. He therefore relied on assurance from Mr Aziz that the summaries had been re-checked and were correct for that year. Mr Potter reported that the only adjustments made to the accounts figures for 2014 were to include additional cash received of £1,000 plus VAT (April 2013) and £600 plus VAT (July 2013) to cover cash expenses and also to reconcile the sales ledger.

4.8 We find from the facts that there was a pattern of careless additions of daily takings and inadequate record keeping in the financial years ended 5 April 2013 and 5 April 2014.

Meetings and no explanation for missing meal bills

4.9 As noted above Mr Aziz met with HMRC when they carried out the cash up on 12 February 2013 and then at meetings on 29 January 2014 and 7 March 2014. The minutes of these meetings were checked, amended and signed by Mr Aziz. At the first meeting Mr Aziz was told that HMRC believed his records to be incomplete. Mr Le Morvan commented that he could see that Mr Aziz was shocked. Mr Aziz was asked questions and he said that there had been no significant changes in the business in the last few years. He told HMRC that there were rarely any discrepancies when he carried out the cashing procedure, but that any that did arise were because a cash paying customer had taken the meal bill. The procedure is that members of waiting staff write up a duplicate invoice if the customer takes the original. At the second meeting Mr Aziz asked HMRC if all the errors found were on split bills. He was then told that the test purchases had been made. Mr Aziz said that he trusts people, but if someone wants to steal they could easily pocket money as it is a busy restaurant. Mr

Potter informed HMRC that following the checks made by HMRC, he had discussed introducing sequential pre-printed invoices with Mr Aziz. HMRC advised that Mr Aziz needed to review his systems and record keeping as he is losing money.

4.10 Mr Aziz was asked about the ratio of cash to card sales at the first meeting. He answered that cash would not be more than 20% and agreed with HMRC's suggestion that it was between 15% - 20%.

4.11 In his email to HMRC on 20 June 2014 Mr Potter commented, in response to HMRC's request for disclosure or an explanation for the omissions of meal bills that were in the test purchases, that there "seems to be an implied assumption that Shah Aziz had knowledge of or was complicit in tax evasion whereas there is no evidence (I see none) to support this. There is absolutely no reason why my client could not be the victim of theft but at the moment you seem to have the only 'evidence' with which to follow this up. I am not saying that this is the case, but there are many other people working in the Restaurant who have an opportunity to defraud my client and it is unreasonable to assume that my client would have knowledge of this. All the more reason, I think, to make available to us all of your Test Purchase data." The test purchase data was made available to Mr Potter on 6 August 2014. No further explanation for the omission of meals bills was provided prior to, or indeed at, the hearing.

4.12 We concluded that Mr Aziz had not satisfied the burden of proof to displace HMRC's findings that an unknown number of meal bills were omitted from sales income over an unknown period.

Other checks carried out

4.13 Mrs Lane carried out a number of other checks for the purposes of her enquiry. First she made checks of Mr Aziz's suppliers. Second, she asked for a statement of his assets and liabilities. As Mr Potter noted, Mr Aziz's assets fell in value during the period under review, and there were no unexplained receipts.

4.14 On 10 April 2015 Mrs Lane informed Mr Potter that HMRC "as a body, has requested data from the main Merchant Acquirers. This data is held centrally and I have recently been sent data relating to the card transactions passing through Mr Aziz's business. Through a comparison of the data and the VAT returns rendered by Mr Aziz I have been able to extract a figure, expressed as a percentage, of the card takings as compared to the total takings declared….this percentage varies between 84% and 97%, which is considered to be very high." The letter noted that Mrs Lane would not expect the merchant acquirer data to match the records exactly, but she would not expect the large differences found when the data was compared to the records. She concluded that either HMRC could run invigilation or Mr Aziz could report on a period of self-invigilation. Mr Potter told us that the self-invigilation suggestion was not accepted as the correspondence moved in another direction.

Mrs Lane's suppression rate proposal

4.15 On 1 May 2015 Mrs Lane wrote to Mr Potter confirming her intention to issue notices in accordance with the schedule of additions that she had sent to him on 29 October 2014. The letter explained that in the absence of a declaration of any omission or an explanation HMRC were required to quantify the missing sales in order to make assessments. The figures that Mrs Lane produced were based on the number of covers represented by missing meal bills as a percentage of the overall covers, then averaged. This produced a schedule of additions based on a 7% suppression rate. The figures were described by Mr Potter as "in the main very crude" in his response dated 22 May 2015 and he applied for a closure notice for the year ended 5 April 2013.

Miss Wellington's merchant acquirer/cash to cash split proposal

4.16 On 6 July 2015 Miss Tracy Wellington wrote to Mr Potter to advise that she would now be dealing with the case, together with Mr Le Morvan who would continue to deal with any VAT issues. Miss Wellington advised that she had reviewed all the information and evidence and that she had reconsidered the basis on which the assessments would be calculated to settle matters. Miss Wellington issued a closure notice for the year ended 5 April 2013 and a discovery assessment for the year ended 5 April 2012 on 6 July 2015, and HMRC issued a notice of a section 9A check of Mr Aziz's income tax return for the year ended 5 April 2014. The letter also attached a schedule of the additional output tax that would be assessed for the period 1 May 2011 to 30 April 2015.

4.17 Miss Wellington told us that she had decided not to adopt Mrs Lane's 'percentage suppression' methodology for arriving at figures for the omitted sales, and had instead followed guidance issued by the restaurants taskforce to use merchant acquirer data in order to determine the gross card takings and then to use this figure to find the gross takings. This required the average cash to card split to be found and applied in order to determine the gross takings from the gross card takings figure. Miss Wellington considered that this would be the most appropriate and straightforward method to use.

4.18 In order to examine the cash to card split further to apply this guidance, and in view of the fact that Mr Aziz had not taken up the suggestion of a period of self-invigilation, two further cashing up checks were authorised by a senior officer and made at the restaurant on 21 May and 5 June 2015. Miss Wellington explained that, whereas the original cash up had produced a card to cash split of 74% to 26%, the card percentage was 77% on 21 May 2015 and 87% on 5 June 2015. Miss Wellington noted that the first two cash ups did not support Mr Aziz's statement that he would not expect cash to be more than 20% of gross takings, but she was willing to take a simple average of these three cash up results in order to propose a card to cash split of 80% to 20%. This split was then applied to the merchant acquirer data on the basis that it represented 80% of gross takings. Mr Potter has challenged the use of three cash ups to determine the cash to card split and he asked HMRC to use the data that he had produced for the split based on the business's records.

4.19 We find that the use of cash ups to determine the card to cash split is reasonable given that it had already been established that there were careless additions, systems and record keeping errors in the taxpayer's data. We consider that the cash ups on three days in 2013 and 2015 were a sufficiently representative sample and free from bias.

Gross Profit cross-check and continuity

4.20 Miss Wellington considered that, as Mr Aziz had confirmed that there had been no change in his record keeping process or business over the years, it was appropriate to give consideration to adjustments to other years. Miss Wellington cross-checked the post-adjustment gross profit rates for the years subject to her proposed assessments with the gross profit rates achieved for the four years to 5 April 2011 in the context of the presumption of continuity. This cross-checking exercise persuaded Miss Wellington not to seek additions for years prior to 2012 (as had been proposed by Mrs Lane), but to limit the additions to 2012, 2013 and 2014 as she had found that they brought the revised gross profit rate for these years in line with those for the four years ended 5 April 2011(which she found ranged from 69.69% to 71.87%) as follows:

Year	Gross profit on returned figures	Gross profit after additions
y/e 5.04.12	67.61%	69.71%
y/e 5.04.13	65.46%	68.13%
y/e 5.04.14	65.81%	68.14%

Mr Potter finds errors in merchant acquirer data and HMRC use his schedule of card sales

4.21 When Mr Potter was sent a summary of the merchant acquirer data he found that he could not reconcile it with his client's accounting records and that it was £25,000 to £30,000 per annum more than the payments banked. Miss Wellington then sent him another summary of the data available on 2 September 2015. Mr Potter identified two areas of error in HMRC's use of the merchant acquirer data in his letter dated 1 October 2015. First, the card receipts included some tips which are outside the scope of VAT and not to be included in the calculation gross profit percentages. Second there was a duplication of Amex income as it was shown for a period as both Amex income and in HSBC merchant service statements. Mr Potter noted that his client's accounting records were not affected by these errors as they reflected the card payments banked and he attached the schedules to assist HMRC.

4.22 Miss Wellington accepted that there was some double counting of Amex income, although she had had no reason to suspect that the merchant acquirer data was not correct. She said that as HMRC's concern was in relation to understated cash sales, she was able to use the schedules provided by Mr Potter as the evidence of card sales

for 2012, 2013 and 2014 in order to prepare revised proposals for additions to profits. On 3 November 2015 Miss Wellington wrote to Mr Aziz to summarise HMRC's position and to enclose computations based on the card data provided by Mr Potter. The figures were adjusted to exclude tips at a fixed rate of 10% (as they are not subject to VAT). Miss Wellington later established that Mr Aziz's tips percentage was lower than 10% but no adjustment was made in HMRC's favour. These amended computations reduced the additions proposed by HMRC's assessments to the amounts shown in the table in paragraph 1 above. The revised VAT assessments were issued on 3 February 2016, but at the hearing it was stated that HMRC accept that the VAT assessment for the period 07/11 should be cancelled because the original assessment was raised outside the four year time limit in section 77(1)(a) VATA.

Penalties

4.23 Once HMRC had issued the closure notices, discovery assessments and VAT assessments, the tax under-declared was used to calculate the potential lost revenue for the purpose of calculating the penalties payable under Schedule 24. HMRC issued the penalty assessment notices on 17 November 2015 following discussions between Miss Wellington and Mr Le Morvan, and authorisation from a senior officer. The letters advised that it had been found that Mr Aziz's behaviour was deliberate with concealment as he knew that there was an inaccuracy in a document given to HMRC and that he had taken steps to conceal the inaccuracy. It was considered that the disclosure was prompted. A reduction of 60% was allowed, made up of 10% for Telling (10%), 20% for Helping and 30% for Giving. This reduced the penalty to 70%. The maximum reduction was not allowed for Telling and Helping because Mr Aziz did not make an active disclosure, he did not accept that cash sales had been omitted and he did not provide an explanation for these shortfalls in his records.

Appeals

4.24 On 6 July 2015 Mr Aziz lodged appeals against the revised assessment for the year to 5 April 2013, other than the additional assessment of £2,773.70 and £98.50 tips (being revised calculations of the net mis-addition of sales invoices and tips for this period referred to in paragraph 4.6 above). The appeal against the revenue assessment for the period to 5 April 2012 was made on 6 July 2015 and the appeal against the assessment for the period to 5 April 2014 was made on 1 October 2015. Mr Potter requested that HMRC carry out an independent statutory review of the decisions. HMRC's decisions were upheld on review, and the conclusion of the reviews was set out in letters dated 27 January 2016 in respect of the income tax and class 4 NICs decisions and 10 May 2016 in respect of the VAT decisions.

4.25 As noted above, Mr Aziz appealed to the Tribunal in respect of the income tax and class 4 NICs decisions on 25 February 2016 and on 21 June 2016 in respect of the VAT decisions.

Submissions

5. It is submitted on behalf of Mr Aziz that HMRC has not used its 'best judgment' on a number of grounds. It is claimed that the test purchases are not evidence that Mr Aziz was responsible for inaccurate records. It is accepted that there were errors occurring in the first stages of the restaurant's accounting system at the time of the test purchases. It is claimed that the three cash ups are not statistically representative of the periods the subject of the assessments or an acceptable method to arrive at the card to cash ratio. If the information in the schedules produced by Mr Potter were to be used the figures would be more realistic.

6. Mr Potter, on behalf of Mr Aziz, has challenged HMRC to respond to his concerns about their behaviour and failure to address a number of issues as he considers that these affected their ability to use 'best judgment'. The issues include the absence of any evidence as to where the missing cash has gone and whether discrepancies were due to the acts of others; the fact that the VAT returns include some income Mr Aziz receives as an interpreter; the fact that there are timing differences between the card sale dates and the time that the money is received by Mr Aziz; the fact that there has been a change in consumer spending towards debit cards; seasonal variations; and that HMRC was given full access to all Mr Aziz's accounting and personal financial and other records.

7. HMRC submit that twenty-one test purchases were carried out and twelve were not recorded in the business's accounts. HMRC became aware of 'additional errors' made in the business sales reports. HMRC have made a discovery and used their best judgment to conclude that these omissions and errors were likely to have occurred over the 2012, 2013 and 2014 years of assessment. HMRC submit that HMRC's estimates of the additions required are more likely to be accurate than Mr Aziz's revised figures.

8. HMRC submit that the under-declarations were 'deliberate and concealed'. HMRC submit that appropriate reductions have been made for the prompted disclosure.

The relevant legislation and case-law

9. The relevant statutory provisions are as follows:

9.1 Section 9A TMA gives HMRC the power to enquire into a taxpayer's return;

9.2 Section 12B TMA requires a taxpayer to keep and preserve all such records as may be requisite for the purpose of enabling him to deliver a correct and complete return for the year or period of assessment;

9.3 Section 28A TMA provides for the completion of an enquiry by HMRC into a personal return by way of a closure notice;

9.4 Section 29 TMA provides that HMRC may make an assessment where a loss of tax is discovered and the requisite conditions have been met, including a condition

that the loss of tax has been brought about 'carelessly or deliberately' by the taxpayer or his agent. The assessment must be made within the time limits in section 36 TMA;

9.5 Section 50 TMA sets out the Tribunal's jurisdiction on an appeal against an assessment, including assessments under sections 28A and 29 TMA. It provides that if the Tribunal decides that the taxpayer has been overcharged by an assessment, the assessment shall be reduced accordingly, but otherwise the assessment shall stand good;

9.6 Section 73 (1) VATA provides that where it appears to HMRC that a taxpayer's returns are incomplete or incorrect, HMRC may assess the amount of VAT due from him to the best of their judgment and notify it to him. Section 73(9) provides that an amount assessed under section 73(1) shall be deemed to be due and may be recovered accordingly, subject to any appeal; and

9.7 The penalty regime is set out in Schedule 24 Finance Act 2007. This provides for penalties to be charged as a percentage of the potential lost revenue, being the difference between the tax payable (had the return been accurate) and the tax paid. The penalty percentage is determined according to the category of behaviour and whether the disclosure is prompted or unprompted, with reductions allowed for the disclosure.

10. HMRC referred us to the following cases that are discussed in context below:

Johnson v Scott [1978] STC 48
Langham v Veltema [2004] EWCA Civ 193
Charlton and others v HMRC [2012] UKUT 770
Jonas v Bamford [1973] STC 519
Allan v HMRC [2016] UKFTT 504 (TC)
Van Boeckel v C&E QB [1981] STC 290
Rahman (t/a Khayam Restaurant) v C&E Commissioners [1998] STC 826
C&E Commissioners v Pegasus Birds Ltd [2004] STC 1509
Phuong Duong Jimmy Lee t/a Jumbo Express [1996] Lexis Citation 816 /14127

11. The burden of proof is on HMRC to show that the conditions for a discovery assessment have been fulfilled and that the assessment has been made within the time limit. The burden of proof is on Mr Aziz to show that the assessments, including the discovery assessment, are incorrect or not to HMRC's best judgment. In *Johnson v Scott* Walton J considered why the burden of proof should be on the taxpayer to establish that an assessment is wrong and concluded that "in cases of this kind… the true facts are known, presumably, if known at all, to one person only, the taxpayer himself. If once it is clear that he has not put before the tax authorities the full amount of his income … what [HMRC] has to do in such a situation is, on the known facts, to make reasonable inferences." It is for the appellant to establish that the assessments ought to be reduced or set aside.

12. The burden of proof with regard to the penalties is that HMRC have to establish that the penalty assessments have been properly charged and that the level of penalty has been correctly determined. The burden of proof in relation to both the assessments and the penalties is the ordinary civil standard of the balance of probabilities.

Discussion

13. We considered the issues for determination in this appeal on the basis of the evidence and facts found, in particular the findings in paragraphs 4.3, 4.8, 4.12 and 4.19, the legislation and case law and the burden of proof on the parties.

Was income under-declared?

14. As noted in paragraph 4.3 and 4.8 above, we find that Mr Aziz has not satisfied the burden of proof to displace HMRC's assertion that an unknown number of meal bills were omitted from his sales income over a period of time and 'additional errors' were made. The test purchases were carried out over a range of days of the week and times and demonstrate a pattern of omissions. It is not necessary for the Tribunal to decide how or why this was going on in order to determine the fact that a proportion of his cash sales income was not declared, but it would have assisted the Tribunal if Mr Aziz had given evidence to allow us to find the underlying facts. We noted Mr Potter's reference to possibility of staff defrauding Mr Aziz, but there was no report of the action taken by Mr Aziz or of the outcome of this action on his income. This might have been relevant to the consideration of the presumption of continuity but it is not for HMRC to prove who is doing what as Walton J confirmed in *Johnson v Scott* (see paragraph 11 above).

Is HMRC's basis for determining the quantum of under-declared income soundly based?

15. Miss Wellington adopted the preferred methodology of the taskforce to determine the quantum of the under-declared income. On the basis that the test purchases had determined that a proportion of the cash sales were omitted from the records, she accepted the schedules prepared by Mr Potter as an accurate record of card sales from which she could work back to the gross sales figure, and the expected cash sales figure, using the card to cash sales percentage. HMRC determined the card to cash percentage by taking an average of the card to cash sales percentages from the three cash up checks. Our findings on the use of the cash ups to determine the expected cash sales are set out in paragraph 4.19.

16. We conclude that HMRC's method of determining the expected cash sales is reasonable for three reasons:

17. First, we found the basis of the cash ups to be fair. As the cashing up is done at the end of the day's trading, it reflects the information available at that time, both in respect of the meal bills paid in cash that are in the pile at close and in respect of the particular day's mix of cash to card sales. The test purchases established that a proportion of the meal bills for cash purchases had been omitted from some daily reports. This finding means that a proportion of the cash sales may not have been

taken into account in determining the proportion of card to cash sales in the cash ups in order to avoid double counting. HMRC did not seek to gross-up the proportion of cash sales in cash ups to reflect missing meal bills or the additional errors, but chose instead to take the proportion of card to cash sales in the cashing-up checks at face value. HMRC also allowed a fixed adjustment of 10% of tips, notwithstanding that this was later established to be higher than the average for the business. HMRC also gave Mr Aziz the opportunity to provide information based on a longer period of self-invigilation.

18. We consider that, in the absence of certainty about the proportion of cash sales that were omitted from the daily records over the relevant periods, this was a fair and reasonable basis on which to base the calculation of the proportion of card to cash sales.

19. Second, the range of the card to cash percentages from the cash ups (74% to 87%) is in line with the 15% - 20% range acknowledged by Mr Aziz in his meeting with HMRC. The lower cash percentage at the later dates is consistent with Mr Potter's report that customers are increasingly paying by debit card. We consider that taking a simple average of the percentage was reasonable.

20. Thirdly, Miss Wellington cross-checked her findings by reference to gross profit percentages, as outlined in paragraph 4.20 above, to check that her proposed figures were credible.

21. Mr Potter produced a number of schedules of figures to demonstrate that a lower or minimal assessment would be due if a lower cash to card percentage were used. We appreciate the work carried out by Mr Potter, but the schedules could not be adopted by HMRC, or indeed the Tribunal, as they were based on Mr Aziz's data that failed to account for or to make any adjustment for the omitted sales, with the result that the card percentages found were inevitably higher but not correct.

Are the assessments in accordance with sections 28A and 29 TMA?

22. It is accepted by Mr Aziz that HMRC opened the enquiries into Mr Aziz's tax returns for the years ended 5 April 2013 and 5 April 2014 in accordance with the provisions in section 9A TMA. Once HMRC had concluded that Mr Aziz had under-declared his income for those years, they were entitled to assess any additional income. As it was the information that HMRC found pursuant to the enquiry in the 2013 return, as opposed to information provided by Mr Aziz in his 2012 return, that "put the sufficiency of the [2012] assessment in question" (to adopt the language of Auld LJ in *Langham v Veltema*), HMRC had made a 'discovery' and the condition in section 29(5) TMA was satisfied. It had "newly appeared to an officer, acting honestly and reasonably, that there is an insufficiency in an assessment" as Norris J and Judge Berner said in *Charlton and others v HMRC*. If the presumption of continuity applied, and if the insufficiency of the assessment was brought about "carelessly or deliberately" (as provided in section 29(4) TMA and considered below), it was then open to HMRC to raise an assessment under section 29 TMA in July 2015 respect of the loss of tax in 2012.

When and how long does the presumption of continuity apply in this case?

23. The application of the presumption of continuity was described by Walton J in *Jonas v Bamford* in the following terms:

"… once the Inspector comes to the conclusion that, upon the facts which he has discovered, [the taxpayer] has additional income beyond that which he has so far declared to the Inspector, then the usual presumption of continuity will apply. The situation will be presumed to go on until there is some change in the situation, the onus of proof of which is clearly onus the taxpayer"

24. In *Allan v HMRC* Judge Poon and Ms Sumpter were concerned to establish the correct facts of the presumption of continuity in that case before it could be applied. This was because it had transpired that there was, at least, a second bank account that had not been taken into account in the presumption. The Tribunal concluded that if the correct presumption of continuity had been applied by HMRC, it could have been applied to the earlier years and later years.

25. We considered that it was necessary to determine when and what pattern of behaviour can be presumed to apply on the facts of this case. While we were concerned by the absence of explanation about the "how or why" the cash meal bills were omitted, the test purchases demonstrate a pattern of under-declaring income at the restaurant in February and May 2013 and Mr Aziz has admitted a series of 'additional errors' throughout 2013. The cross-check against the gross profit percentages (paragraph 4.20 above) indicated to Miss Wellington that there was a drop in the business's profits over the three years from 6 April 2011. As Mr Aziz has not provided an explanation for the missing meal bills or when or why the rate of omissions or errors might have changed or ended, he has not discharged the burden of proof to displace the presumed continuity of the under-declaration from 2012 to 2014.

Are HMRC's VAT assessments to 'best judgment'?

26. We considered the guidance provided by Woolf J in *Van Boeckel v Customs and Excise Commissioners* to determine whether HMRC's assessment of the VAT was 'to the best of their judgment' in accordance with the requirements of section 73 (1) VATA. Woolf J identified the obligations placed on HMRC in order to come to a view as to the amount of tax to the best of their judgment as follows:

26.1 HMRC 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 honesty and bona fide";

26.2 There must be some material before HMRC "on which they can base their judgment"; and

26.3 Bearing in mind the primary obligation on the taxpayer to make a return himself, HMRC "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 their best judgment, is due".

In this case HMRC had the significant information summarised in paragraph 4 above on which to exercise their judgment. The proposals were put forward by HMRC on an honest and bona fide basis for comment from Mr Aziz.

27. In *Rahman (trading as Khayam Restaurant) v Customs and Excise Commissioners* Carnwath J, commenting on Woolf J's analysis in *Van Boeckel* added that a tribunal should not treat an assessment as invalid "… merely because it disagrees as to how the judgment should have been exercised. A much stronger finding is required; for example, that the assessment has been reached 'dishonestly or vindictively or capriciously'; or is a 'spurious estimate or guess in which all elements of judgment are missing'; or is 'wholly unreasonable'. In substance those tests are indistinguishable from the familiar *Wednesbury* principles…"

28. In *Customs and Excise Commissioners v Pegasus Birds Ltd* Lord Justice Carnwath provided further guidance that although "the tribunal's powers are not spelt out, it is implicit that it has power either to set aside the assessment or to reduce it to the correct figure" It is the tribunal's primary task to find the correct amount of tax. We considered the amount of the assessments in this case and found that HMRC had taken account of all of the relevant information and had reached a reasonable conclusion. There was no justification or basis on which any other figures would be appropriate as noted in paragraph 22 above. In simple terms, Mr Potter's schedules have not explained how money was going awry between the point of sale and the cash ups and therefore have not provided a better guestimate of how much money was involved.

29. We also noted Carnwath LJ's guidance in relation to allegations to dishonesty or wrongdoing against HMRC's officers, but found that Mr Potter's allegations about HMRC's behaviour ("incompetence, tardiness, intimidation, lack of co-operation and inability to abide by the directions of the court") were matters for his formal complaint. We found that there was an honest and genuine attempt by HMRC fairly to consider all of the relevant material to make an assessment to their best judgment.

30. In paragraph 4.19 above we state our finding that the three cash ups in 2013 and 2015 were sufficiently representative and free from bias. In *Phuong Duong Jimmy Lee t/a Jumbo Express* Judge Bishopp was satisfied that an assessment based on one day of observed trading was representative. HMRC had undertaken a number of calculations and cross-checked against each other, as in this case.

31. Taking an overall view of the evidence, findings of fact and our findings on the presumption of continuity, we are satisfied that the assessments are HMRC's best judgment of the under-declaration of output tax and both reasonable and credible on the facts. Mr Aziz has not satisfied us that the assessments should be reduced from the amounts set out in the table in paragraph 1 to a better estimate.

Were the under-declarations 'deliberate and concealed'?

32. HMRC have relied on the test purchases and cash ups as evidence of the 'deliberate and concealed' behaviour by Mr Aziz and the penalties have accordingly been determined at the maximum penalty percentage of 100%. HMRC consider that Mr Aziz's disclosure to HMRC was prompted. This resulted in a penalty range under Schedule 24 of 50% to 100% to which the 60% reduction for disclosure was applied, resulting in the penalties at the rate of 70%. The penalties were notified and imposed in accordance with the provisions of Schedule 24.

33. As HMRC have the burden of proof to establish that Mr Aziz's under-declaration is 'deliberate and concealed', we considered whether the evidence proves, on the balance of probabilities, that the 'additional errors' and the removal of the cash and the missing meal bills was deliberate behaviour. It seems clear that the 'additional errors' were careless and not deliberate.

34. We then considered the removal of cash and meal bills from daily takings and find that this action was deliberate action by a member of staff, but that on the balance of probabilities, the evidence does not support the allegation that it was deliberate action by Mr Aziz. In reaching this conclusion we note that it is disappointing that Mr Aziz chose not to give evidence, but HMRC did not seek to draw an adverse inference from this and rely on the evidence of the omissions and lack of explanation. The statement of assets has not pointed to an accumulation of cash by Mr Aziz, and he seemed shocked and asked questions at the meetings with HMRC, presumably to try and understand what had happened once he had been told about the omissions and errors in his records. Mr Potter's accounting work has been found to be thorough and reliable and he has spoken to Mr Aziz's integrity, cooperation and the possibility of the omissions being due to the actions of other members of staff. The omissions were not concealed because of specific action or steps taken by Mr Aziz.

35. We find that HMRC have not discharged the burden of proof to establish that the under-declaration is due to 'deliberate and concealed' action by Mr Aziz. We find that Mr Aziz was negligent in allowing the cash and meal bills to be removed in the periods the subject of the assessments, and that he was careless in the management of his daily reporting and record keeping. As the owner of the business he has sole responsibility for the business's accounting records for tax purposes, and a duty to ensure that these were accurate and complete. However, his behaviour has been proved to be negligent and careless rather than deliberate, and on this basis the penalty should be charged within the penalty range of 15% to 30%.

36. HMRC have considered the circumstances of this case to determine if there were special circumstances, being circumstances that are exceptional, abnormal or unusual, that would merit a reduction of the penalties, but concluded that there were none. We do not find that HMRC's decision on this issue was flawed or that it should be altered.

Are the penalty reductions given correct?

37. Mr Le Morvan and Miss Wellington explained the reasons for each percentage reduction in their letters to Mr Aziz and at the hearing. We consider that the refusal to allow higher reductions because Mr Aziz would not accept that sales were missing or agree that HMRC's methods were credible is reasonable in relation to 'Telling', but not in relation to 'Helping'. There can be no doubt that Mr Potter, as Mr Aziz's representative, carried out an enormous amount of work on the figures and his card data figures were used by HMRC in determining the assessments. We consider that the reductions should be 10% for Telling as decided by HMRC, 30% for Helping and the maximum of 30% for Giving Access, making a total reduction of 70% to be applied to the range of 15% - 30% for prompted disclosure of careless behaviour. This reduces the penalty to a rate of 19.5%.

Decision

38. For the reasons set out above, the income tax and class 4 NICs amendments, and the VAT assessments, are upheld in the amounts set out in the table in paragraph 1 above, other than the VAT assessment for the period 07/11 which HMRC have agreed to cancel.

39. The penalty assessments are varied. Mr Aziz is liable to penalties at the rate of 19.5%.

40. 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.

VICTORIA NICHOLL

TRIBUNAL JUDGE
RELEASE DATE: 21st MARCH 2018