Appeal number FTT/12/2009

Value Added Tax – Assessmen t in default of proper retu rns by taxpayer – Function of First-tier Tribunal – Supervisory jurisdiction wrongly applied – Matter remitted to First-tier Tribunal to determine correct amounts of tax – VAT Act 1994 s.73(1)

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

MITHRAS (WINE BARS) LIMITED **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS (Value Added Tax) **Respondents**

TRIBUNAL: SIR STEPHEN OLIVER QC

Sitting in public in London on 5 March 2010

Tim Brown, counsel, instructed by Weightmans, solicitors, for the Appellant

Sarabjit Singh, counsel, instructed by the general counsel for HMRC, for the Respondents

DECISION

1. This is an appeal against a decision of the Tax Chamber of the First-tier Tribunal ("the FTT") released on 1 May 2009. The decision appealed against concerns the Appellant's appeal against three assessments for VAT. The assessments were concerned with sales at six establishments operated by the Appellant. These were known as "Chapter Delicatessens" (referred to by the FTT as "Delis 1-6") and two further establishments operated by the Appellant named "Bar Capitale" ("Bar Capitale 1 and 2").

2. In respect of Delis 1, 2 and 3, the FTT decided that there was a binding agreement between the Appellant and the Respondents that 30% of the sales at those establishments would be treated as standard-rated for VAT purposes, and 70% would be treated as zero-rated. The Respondents do not appeal against that finding and have agreed revised assessments with the Appellant on the basis of the FTT's decision.

3. The FTT upheld the Respondents' assessments relating to Delis 4, 5 and 6 and Bar Capitale 1 and 2. The Appellant applied for permission to appeal against this part of the FTT's decision on 23 June 2009. The Appellant's grounds of appeal are that the FTT erred in law in that –

> "(a) In addressing the quantum of the assessments, the Tribunal restrict itself to having a supervisory jurisdiction instead of an appellate jurisdiction.
> (b) It decided the issue on whether the assessments were made to best judgment.
> (c) It failed to address the primary task of finding the correct amount of tax based on the material placed before it".

The Appellant also contends "that the Tribunal clearly misdirected itself that it had only supervisory jurisdiction in respect of assessments and concentrated on deciding whether the assessments were made to best judgment, i.e. were they reasonable? Instead it should have followed the guidance of the Court of Appeal in *Customs and Excise Commissioners v Pegasus Birds Ltd* [2004] EWCA Civ 1015, [2004] STC 1509, and decided what was the correct amount of tax on the material properly before it?"

4. HMRC recognised that there is substance in the Appellant's case. Both sides are at one on the legal background to the appeal. What follows is a non-controversial summary of the current state of the law. I will then apply it to the present circumstances.

The jurisdiction of the FTT

5. The Appellant's appeal to the FTT was against assessments raised by the Respondents under section 73(1) of the Value Added Tax Act 1994 ("VATA"). Section 73(1) of VATA provides that:

> "Where a person has failed to make any returns required under this Act (or under any provision repealed by 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."

6. When addressing the tax affairs of the Appellant, it appeared to the Respondents that the Appellant's VAT returns were "incomplete or incorrect". Consequently the Respondents decided to assess the amount of VAT due from the Appellant "to the best of their judgment". However, the Appellant was not restricted to appealing only against the Respondents' decision to make the assessments. The Appellant was also able to appeal against the amount of the assessments. This appears from section 83(1)(p) of VATA, which provides that an appeal lies to the Tribunal against an assessment under section 73(1) "or the amount of the assessment".

7. The FTT stated in paragraph 75 of its decision that "the function of the Tribunal is supervisory". To a limited extent that is right. The FTT has a quasi-supervisory function when considering whether an assessment was raised to the best of the Respondents' judgment, but it has more than a merely quasi-supervisory jurisdiction when considering the correct amount of the assessment. In deciding the correct amount of the assessment, the FTT has a full appellate jurisdiction. This has become more apparent as the decisions of the Courts in this field have developed.

8. The Tribunal's quasi-supervisory jurisdiction as far as a "best judgment" challenge is concerned is well established. In *Van Boeckel v Customs and Excise Commissioners* [1981] STC 290, Woolf J (as he then was) stated that in assessing the amount of tax due "to the best of their judgment", the Commissioners were required to consider fairly all material put before them by the taxpayer and on that material make a decision which was reasonable as to the amount of tax due. They were not required to make investigations so long as there was some material on which they could reasonably base an assessment, but if they did make an investigation, they had to take into account the material disclosed by that investigation.

9. Woolf J indicated that the Commissioners, when exercising their powers, made a value judgment on the material before them, and they were required to make this value judgment honestly and bona fide, and to come to a decision which was reasonable and not arbitrary as to the amount of the tax: see page 292 of the judgment.

10. In *Rahman v Customs and Excise Commissioners* [1998] STC 826 ("*Rahman 1*"), Carnwath J (as he then was) stated that a tribunal should not treat an assessment

as invalid merely because the members disagreed as to how the Commissioners' judgment should have been exercised. A much stronger finding was required, for example that the assessments had been reached dishonestly or vindictively or capriciously, or was a spurious estimate or guess in which all elements of judgment were missing or was wholly unreasonable.

11. The principles established in *Van Boeckel* and *Rahman 1* indicate that the FTT's jurisdiction when considering whether an assessment was raised to the best of the commissioners' judgment is akin to a supervisory, judicial review type jurisdiction. The FTT does not have a true appellate function in that it cannot set aside the assessment on the basis that it disagrees with the Commissioners' decision to make the assessment. The circumstances in which the FTT can decide that the assessment was not raised to the best of the Commissioners' judgment, and therefore should not have been made at all, are very limited, essentially being restricted to cases where the Commissioners have acted perversely or in bad faith. Cairnwath J in *Rahman 1* indicated that this "kind of case is likely to be extremely rare" and that in the normal case "it should be assumed that the Commissioners have made an honest and genuine attempt to reach a fair assessment": see page 835 of the judgment.

12. Turning now to the FTT's decision in the present case, paragraph 75 is relevant. This states:

> "In considering the meaning of the phrase "to the best of their judgment", the Tribunal has referred to the decisions of *Van Boeckel* … and *Rahman 1* … . The following principles emerged from those and other relevant decisions. First, there must be some material before the Commissioners on which they can base their judgment. Secondly, the Commissioners are not required to do the work of the taxpayer in order to form a conclusion as to the amount of tax due. Thirdly, 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. Fourthly, the 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 had been reached "dishonestly, capriciously or vindictively" or was a "spurious estimate or guess in which all elements of judgment were missing" or was "wholly unreasonable". Fifthly, if the assessment is shown to have been wholly unreasonable or not bona fide there would be sufficient grounds for setting it aside but that kind of case is likely to be extremely rare. Finally, it must be assumed that the Commissioners have made an honest and genuine attempt to reach a fair assessment. The Tribunal should be concentrated on seeing whether the amount of the assessment should be sustained in the light of the material then available. The function of the Tribunal is supervisory. It is not a function of the Tribunal to engage in the process of looking afresh at all the evidence before it."

13. This, I am satisfied, is an accurate summary of the *Van Boeckel/Rahman 1* principles that apply to a "best judgment" challenge. The FTT, as just noted, went on to state that: "It is not a function of the Tribunal to engage in the process of looking afresh at all the evidence before it". This is correct in that the Tribunal does not look afresh at all the evidence when deciding whether an assessment was raised to the best of the Commissioners' judgment, but considers the material (or lack of it) available to the Commissioners at the time their assessment was raised.

14. The FTT's statement in the above extract that - "The Tribunal should be concentrated on seeing whether the amount of the assessment should be sustained in the light of the material then available" - is a direct quote from the judgment of Carnwath J in *Rahman 1*, where he stated that the "debate before the Tribunal should be concentrated on seeing whether the amount of the assessment should be sustained in the light of the material then available" (at page 836). Carnwath J was not referring to the question of whether the assessment was raised to best judgment. He was addressing the question before the tribunal where the tribunal was considering the amount of the assessment in the light of the material available to the tribunal. When the tribunal considers the amount of the assessment, the *Van Boeckel/Rahman 1* principles do not apply.

15. *Koca v Customs and Excise Commissioners* [1996] STC 58 is relevant to this latter issue. In that case Latham J (as he then was) referred to the *Van Boeckel* principles and criteria and stated that on appeal "the tribunal is required to consider whether or not the assessment is one which meets those criteria". He went on to state:

> "But the tribunal has a further function. In determining the appeal, the tribunal may have evidence before it which makes it clear that although the assessment was perfectly proper on the information available to the Commissioners nonetheless it should be reduced to give effect to that further evidence, or even further argument based on the material originally before the Commissioners. This function has been clearly recognised in a number of cases, including *Van Boeckel*: see page 64 of the judgment."

16. The observations extracted from the decisions in *Koca* and *Rahman 1* emphasise the point that in an appeal against the amount of an assessment, the Tribunal is not restricted to any kind of quasi-supervisory function which involved referring to the Commissioners' judgment on quantum at the time the Commissioners made their assessment. The Tribunal's function is truly appellate, in that it can consider further information or argument at the hearing of the appeal and reduce the amount of the assessment, thereby substituting its own view on quantum for that of the Commissioners.

17. In *Georgiou and Another (trading as Marios Chippery) v Customs and Excise Commissioners* [1996] STC 463, Evans LJ referred to Latham J's judgment in *Koca* and considered the functions of the tribunal in an appeal against both an assessment and the amount of the assessment. Evans LJ noted that –

> "Mr Barlow, counsel for the Commissioners, informed us that the tribunals regularly exercised their jurisdiction by adopting a two-stage approach. First, did the Commissioners exercise their best judgment and, if so, was it a valid assessment; two, what is the tribunal's own assessment of the amount? Both counsel submitted to us that this was the correct approach. Mr Barlow said that the Commissioners were keen that tribunals should continue to function in this way because it is perceived as being advantageous to the taxpayer": see page 477.

18. In the absence of argument on other possible approaches by the Tribunal, the Court of Appeal was content to proceed on the basis of the agreed approach. The Court of Appeal did not impugn the tribunal's decision on quantum in the *Georgiou* case because the tribunal "properly took account of all the evidence and all the submissions before it". It follows that the tribunal is able to make its own assessment on quantum in the light of the material before it and it is not restricted merely to considering the reasonableness of the Commissioners' decision on quantum at the time the assessment was made.

19. Carnwath J in *Rahman 1* cautioned against the two-stage approach that had been agreed as appropriate by the parties in *Georgiou*, and indicated that in a normal case the principal concern of the tribunal should be to ensure that the amount of the assessment was fair, which involved taking into account any points raised before it by the Appellant (see page 840). This appears from a passage where Carnwath J said that: "The debate before the tribunal should be concentrated on seeing whether the amount of the assessment should be sustained in the light of the material then available", i.e. the material available to the tribunal (see page 836). The evident danger in the two-stage approach, he observed, was that it reversed the emphasis on the amount of the assessment, and it was the amount of the assessment that was likely to be the important issue in the normal case (see page 836).

20. In *Murat v Customs and Excise Commissioners* [1998] STC 923, Lawrence Collins J (as he then was) focussed on the approach of the tribunal to the amount of an assessment as compared to its approach to a "best judgment" challenge. He stated that: "an appeal against the exercise by the Commissioners of their best judgment is effectively a supervisory appeal in this sense, the tribunal cannot substitute its judgment for that of the Commissioners": (see page 926 of the judgment). He indicated that the Van Boeckel principles applied in the context of a "best judgment challenge". But he went on to state that:

> "Counsel on behalf of the Commissioners has accepted that a different approach is to be adopted by a tribunal to an appeal on quantum and an appeal on the assessment generally. The *Van Boeckel* approach is correct in dealing with the initial decision of the Commissioners to make an assessment and, indeed, to make an assessment in the amount that they made. When it comes to appeal, once it is accepted, as it was here, that the Commissioners were fully justified in making an assessment, the amount of the assessment is a matter for the tribunal to

> decision for itself, and it is a true appeal rather than a supervisory jurisdiction. The tribunal then has the responsibility of looking at all the material put before it by the Appellant and indeed by the Commissioners, considering any evidence that is given to it and deciding for itself what should be the correct amount of any assessment" (see pages 926-927).

21. This approach was applied by the Court of Appeal in *Rahman v Customs and Excise Commissioners (No.2)* [2002] EWCA Civ 1881, [2002] STC 150 ("*Rahman 2*"), at paragraph 40. Chadwick LJ stated that VATA provided "a means, by way of appeal, by which the correct amount of tax payable by the taxpayer can be ascertained" (paragraph 38). He endorsed the observations of Carnwath J in *Rahman 1* about the dangers of an over-rigid adherence to the two-stage approach and stated that: "a tribunal would be well advised to concentrate on the question what amount of tax is properly due from the taxpayer? – taking the material before it as a whole and applying its own judgment" (paragraph 44). This was because the "underlying purpose of the legislative provisions is to ensure that the taxable person accounts for the correct amount of tax" (paragraph 45).

22. In *Customs and Excise Commissioners v Pegasus Birds Ltd* [2004] EWCA Civ 1015, [2004] STC 1509, Carnwath LJ summarised the position as follows:

> "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 the 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 the time of the assessment (paragraph 38)."

23. The authorities cited above show that in considering an appeal against the amount of an assessment raised by the Commissioners, the tribunal has a full appellate jurisdiction and is able to decide for itself the correct amount of the tax due.

The approach taken by the FTT

24. By way of preliminary point I emphasise that the Appellant did not maintain a "best judgment" challenge against the Respondents' assessment before the FTT. Whilst the Appellant had claimed that the assessments were not made to best judgment in its original grounds of appeal, it withdrew this claim in an undated application to amend its notice of appeal issued on or around 22 December 2008. The FTT recorded the Appellant's core submissions at paragraph 31 of its Decision, and did not record the Appellant as making any "best judgment" challenge. Despite this, in considering the quantum of the assessments made relating to Delis 4, 5 and 6 and Bar Capitale 1 and 2, the FTT did so under the heading – "Was the assessment made to best judgment" (just above paragraph 74). The FTT stated that an "issue" in the appeal was whether the assessments were made to the best judgment of the

Commissioners (see paragraph 74), yet the Appellant was not making a "best judgment" challenge but a challenge to the amount of the assessments.

25. When the FTT came to consider the parties' arguments on quantum in detail at paragraphs 77 to 101 of its decision the decision can be read as indicating that the FTT had not been persuaded by the Appellant's arguments on quantum and preferred the Respondents' arguments. The FTT observed that the working papers showed that there had been mixed standard rated and mixed zero-rated supplies made at each of the premises but that the correct proportion of the split between the two had not been clearly identified by a proper method (see paragraph 78). At paragraph 82 they observed that, as regards the Bar Capitale restaurant, it would normally be expected that a small proportion of meals eaten would be a zero-rated takeaway food. In paragraph 95 the FTT drew attention to the fact that while the Appellant had argued that one day should not a representative period, no additional tangible reliable evidence had been submitted to substantiate the Appellant's own claim.

26. Those and other findings might have enabled the FTT to have concluded that it was not satisfied that the Appellant had discharged the burden of proving that the amounts of the assessments were incorrect, and that the FTT was satisfied that the amounts were correct on the basis of the evidence and arguments that it had had in the course of the appeal. The FTT would not, arguably, have misdirected itself if it had arrived at such conclusions, as they would have been consistent with the FTT exercising a full appellate jurisdiction and deciding for itself what the correct amount of the assessments should be. However, instead of doing this, the FTT appeared to apply, erroneously, the *Van Boeckel/Rahman 1* principles to its assessment of quantum, when those principles are reserved for "best judgment" challenges. The FTT stated the following at paragraph 100 of its decision:

> "What conclusions can we then draw? First is that a value judgment was made on the materials before Officer Walton and his team. A calculation was done which appeared to be fair. The assessment was not dishonest, capricious or vindictive and was not unreasonable. Indeed, Officer Karen Marsh after having new information submitted to her reduced the initial assessment. It is fair to say therefore there was an honest and genuine attempt to reach a fair assessment."

27. The references to the Commissioners making a "value judgment" and arriving at an assessment which was not "dishonest, capricious or vindictive" or "unreasonable" would have been relevant if the Appellant had been arguing that the assessments were not made to the best of the Commissioners' judgment. However, it was not appropriate for the FTT apparently to exercise merely a quasi-supervisory function over the Appellant's challenge to the amount of the assessments raised by the Commissioners. The FTT should have exercised a full appellate jurisdiction.

28. Before taking a view as to the correct decision that I should make, I observe that there are suggestions at paragraph 101 that the FTT, while using the language of

Van Boeckel and *Rahman 1* earlier in its decision, did in fact exercise a full appellate function. The FTT stated that:

> "There is a fair argument that an invigilation for one day must not be representative. However, the Appellant provided insufficient evidence to rebut or show that the figures and splits arrived at by the Commissioners were inaccurate. The Tribunal has not found the evidence presented by the Appellant to be convincing or persuasive in this regard. Further, the evidence which was gathered by the Commissioners to make the assessments came from a variety of different sources. There were, inter alia, meetings, exchanges of information, interviews with bookkeeper and accountant, a tour of the premises and the invigilation. It would have been preferable to carry out further invigilation exercises but in the circumstances what was done was fair. The Tribunal cannot find reasons for calling into question the assessment".

That language is consistent with the FTT considering the merits of the Appellant's argument and deciding for itself whether to change the amounts of the Commissioners' assessments. The FTT refers to the "insufficient evidence" provided by the Appellant to show that the Commissioners' calculations were "incorrect" and states that the evidence presented by the Appellant was not "convincing or persuasive". It is not impossible therefore that even though the FTT concluded at paragraph 102 that the "assessments were made to best judgment and are accordingly correct", the FTT nevertheless considered for itself whether the amounts of the assessments were correct on the basis of the evidence and arguments it heard in the course of the appeal.

29. My attention was, however, drawn to a similar position and a similar argument that arose in *Murat*. This was rejected by Lawrence Collins J. He stated that:

> "It is said that what the Tribunal is really saying is that it has not been impressed by the material put before it by the Appellant. So be it, but I cannot say that if the Tribunal has appreciated the true nature of its functions in this case it would inevitably have reached the same decision. Accordingly, the Appellant must be entitled to go back and have the matter considered afresh in the light of the correct approach." (see page 929).

The present is, I think, a case where the Appellant is entitled to "go back and have the matter considered afresh in the light of the correct approach". The FTT, as I read the present Decision as a whole and for the reasons that I have already identified, failed to address its primary task of determining the correct amount of tax based on the material placed before it. In considering the Appellant's appeal against the amount of the assessments, the FTT should have exercised a full appellate jurisdiction and decided for itself the correct amount of the tax due.

30. What then is the right course to take? Here again there is no significant difference between the parties. Both would like to see the matter remitted back to the same panel of the FTT for consideration of the correct amounts of the assessments.

31. I think that is the preferable course to take. In the course of the hearing in 2009 the Tribunal heard a great deal of evidence. Much of that had to do with the existence of the agreement issue that was, in the events, decided in the favour of the Appellant. The FTT heard evidence from numerous witnesses on behalf of both parties over the course of a six day hearing. No challenge has, as I understand the position, been made by either party to any findings of fact made by the FTT. It seems to me therefore that it would be consistent with the overriding objective of the Tribunal Procedure (Upper Tribunal) Rules 2008 that the matter should be remitted back to the same panel of the FTT for consideration of the correct amounts of the assessments. The alternative would be for the appeal to be remitted to a new panel which would then have to hear evidence and submissions all over again. I see no reason why this should be done and it would be inconsistent with the aims of the overriding objectives which include dealing with a case in a way that is proportionate to the anticipated costs and avoiding delay.

32. I therefore direct that the matter be remitted to the same panel of the FTT that heard the original appeal. That panel will be in a position to invite further submissions from the parties if and to the extent that this is considered necessary. It has the evidence and arguments on quantum before it already and now needs to apply itself to the correct test when reaching a conclusion about the quantum instead of merely asking itself whether the amounts of the Commissioners' assessments were reasonable.

Direction

33. It is directed that this matter be remitted to the same panel of the FTT that originally heard the appeal. That panel should exercise a full appellate function and decide for itself the correct amount of tax due.

SIR STEPHEN OLIVER QC
JUDGE OF THE UPPER TRIBUNAL
RELEASE DATE: