



TC02091

Appeal number: TC/2011/04725

*VALUE ADDED TAX – Assessment in respect of underdeclared tax –
Whether proper records kept – No – Whether assessment to the best of the
officer’s judgment – Yes – Appeal dismissed*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

MAHIR LONDON LIMITED

Appellant

- and -

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

**TRIBUNAL: JUDGE TIMOTHY HERRINGTON
SHEILA CHEESMAN**

Sitting in public at 45 Bedford Square, London WC1 on 16 April 2012

Mr Zaki Husein, Kaiser & Associates, for the Appellant

**Mrs Silvia Knibbs, Appeals and Reviews, HM Revenue and Customs, for the
Respondents**

DECISION

Introduction

1. This is an appeal by Mahir London Limited (“Mahir”) against an assessment in respect of underdeclared VAT of £26,655.
2. We heard evidence from Mr Michael Mallia, one of the Respondents’ officers (“Mr Mallia”). Mahir did not appear to give evidence but its case was presented by its representative, Mr Zaki Husein.

The Facts

3. Based on the evidence that we heard and the documents put before us, we find the following facts.

4. Mahir was first registered for VAT on 2 March 2005. The nature of its business was the retail sale of clothing for adults and children. Mahir ceased trading on 31 October 2010 and transferred its business to another company. Consequently it submitted an application to deregister for VAT which was approved with effect from 1 November 2011.

5. During February 2011 the Respondents (“HMRC”) visited Mahir’s business premises to inspect its records following the deregistration. This inspection was carried out by Mr Mallia and he undertook an exercise in relation to Mahir’s zero-rated purchases and sales. Mahir’s sales comprised a mixture of sales of adult clothing, which was subject to VAT at the standard rate and children’s clothing, which was zero-rated. Subsequent to the visit, Mr Mallia wrote to Mr Kamal, a director of Mahir, on 9 February 2011 to inform of his findings. This letter stated:

“I examined the zero-rated sales. Up to period 11/08 less than 10% on average were zero-rated. I did an exercise as below where I compared the zero-rated purchases to the zero sales.

<u>Period</u>	<u>zero-rated purchases</u>	<u>percentage</u>	<u>sales</u>	<u>percentage</u>
10/10	2,457	6%	16,005	49%
09/10	14,597	12%	66,689	49%
06/10	9,050	26%	41,567	49%
03/10	15,110	28%	42,723	45%

This shows that your zero-rated sales records are incorrect with the result that not enough output VAT is being declared. The average zero-rated purchases from the above calculation shows 18%. However I have taken out the 10/10 period out of the equation as this was for only one month so as not to distort the figures. This resulted in a 22% average zero-rated purchases.

To be fair to you I am treating 25% of purchases as zero-rated and therefore 25% of the sales were zero-rated as well which leaves 75% standard rated. I have applied this

percentage to the sales and you will therefore be receiving a £26,655 assessment calculated as follows: ...”

5 The letter then went on to set out the detailed calculations by which the assessment figure of £26,655 was arrived at.

6. Mahir disputed the calculations. In response to Mr Mallia’s letter of 9 February 2011 Kaiser & Associates, Mahir’s representatives, wrote to HMRC in a letter dated 6 March 2011 which stated that the calculations did not take into account various
10 factors such as the differences in stock in hand and sales margin (their contention was that on average children’s clothes tend to have a higher margin). The letter appended a schedule, showing figures derived from Mahir’s VAT returns for the entire period of its trading (that is for all the periods from 05/05 to 09/10) which showed that taken over the whole of this period the average zero-rated sales claimed was 23.6%, which
15 was in line with the average zero-rated purchases over the same period of 18.02% (allowing for a 5% margin of error). This schedule showed a marked increase in zero-rated sales from the 02/09 period onwards. In presenting the case before us, Mr Husein asserted that the reason for this marked increase was a change of strategy on the part of Mahir, whereby it concentrated on selling children’s clothes during this
20 period, whereas despite purchasing a considerable amount of children’s clothes in earlier periods these had not been selling very well.

7. On 11 March 2011 Mr Mallia wrote to Mr Kamal in response to Kaiser & Associates’ letter of 6 March 2011 explaining why the assessment was only based on
25 the periods from 02/09 onwards rather than the whole period of trading. Mr Mallia stated that in the earlier periods the returns showed between 78% and 98% standard rated sales and in the periods from 02/09 onwards purchases averaged 22% zero-rated purchases but 49% zero-rated sales. He stated that whilst Mahir might have a higher mark-up on children’s clothes this was allowed for in the calculation as he
30 allowed 25% instead of 22% zero-rated sales. These points were amplified in Mr Mallia’s oral evidence; he stated that of the 23 VAT returns made by Mahir 13 showed repayments of VAT due, which was inconsistent with 75% of the sales throughout the whole period being standard rated sales.

35 8. On 24 March 2011 HMRC issued a Notice of Assessment to Mahir for £26,655 plus interest of £461.47.

9. Following further correspondence, Kaiser & Associates asked for a review of
40 Mr Mallia’s decision on Mahir’s behalf. This was conducted by Mrs Fiona Hill a higher officer of HMRC who concluded in her letter of 23 May 2011 that Mr Mallia had acted entirely fairly and reasonably. In particular, Mrs Hill noted that input tax claimed throughout the whole period of Mahir’s trading was shown as 86% standard rated leaving 14% as zero-rated and the assessment raised had used a generous figure of 25% zero-rated purchases. Mrs Hill also considered that Mr Mallia had taken into

account factors such as stock in hand and sales margin, which resulted in the average figure of 22% applicable to zero-rated purchases being increased to 25%.

10. Mr Mallia's oral evidence covered what he found as regards the extent of Mahir's record keeping in respect of the underlying material that supported Mahir's VAT returns. Mr Mallia explained that he had seen records of purchases, which mainly came through importations but the sales records were limited. Although till rolls were used, Mahir did not retain them. All sales were recorded, usually by Mahir's director, manually on a piece of paper and it was from these documents that the VAT returns were prepared. Mr Mallia had sight of these documents. There was no other material produced to verify what was actually sold or the split between standard rated and zero-rated sales, although Mr Husein pointed out that a considerable number of sales would have been paid for by credit card so that it might have been possible to obtain the detail about the nature of particular sales by examining the credit card receipts. Mr Mallia confirmed that he did not ask for or examine any credit card receipts. Mr Mallia confirmed that no stock records were available. Mr Mallia's evidence on the extent of Mahir's records was not disputed and indeed Mr Husein in his opening remarks admitted that Mahir was not highly skilled on the administrative side of the business, and was disorganised in the way it maintained records.

The Law

11. Section 73(1) of the Value Added Tax Act 1994 ("the Act") provides as follows:-
"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."

The question as to what constitutes "to the best of their judgment" was considered in the case of *Van Boeckel v Customs and Excise Commissioners* [1981] STC 290 and in the decision at page 292 Woolf J in referring to section 31 of the Finance Act 1972, the predecessor legislation to section 73(1) of the Act, laid down the following principles:-

"The contentions on behalf of the taxpayer in this case can be summarised by saying that on the facts before the tribunal it is clear, so it is contended, that the assessment in question was not valid because the commissioners had taken insufficient steps to ascertain the amount of tax due before making the assessment. Therefore it is important to come to a conclusion as to what are the obligations placed on the commissioners in order properly to come to a view as to the amount of tax due, to the best of their judgment. As to this, 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

5 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.

10 Secondly, clearly there must be some material before the commissioners on which they can base their judgment. If there is no material at all it would be impossible to form a judgment as to what tax is due.

15 Thirdly, it should be recognised, particularly bearing in mind the primary obligation, to which I have made reference, of the taxpayer to make a return himself, that the commissioners should not be required to do the work of the taxpayer in order to form a conclusion as to the amount of tax which, to the best of their judgment, is due. In the very nature of things frequently the relevant information will be readily available to the taxpayer, but it will be very difficult for the commissioners to obtain that information without carrying out exhaustive investigations. In my view, the use of the words 'best of their judgment' does not envisage the burden being placed on the commissioners of carrying out exhaustive investigations. What the words 'best of their judgment' envisage, in my view, is that the commissioners will fairly consider all material placed before them and, on that material, come to a decision which is one which is reasonable and not arbitrary as to the amount of tax which is due. As long as there is some material on which the commissioners can reasonably act then they are not required to carry out investigations which may or may not result in further material being placed before them."

Later in the decision, at page 296, Woolf J stated:

30 "As I have indicated, unless the situation is one where no material is before the commissioners on which they can reasonably base an assessment, the commissioners are not required to make investigations. If they do make investigations then they have got to take into account the material disclosed by those investigations. Obviously, as a matter of good administrative practice, it is desirable that the commissioners should make all reasonable investigations before making an assessment. If they do that it will avoid, in many cases, the necessity of appeals to the tribunal. However to try and say that in a particular case a particular form of investigation should have been carried out, is a contention which, in my view, as a matter of law, bearing in mind the wording of s.31(1), is difficult to establish."

45 12. The legal question to be determined is therefore whether the assessment made by Mr Mallia on 11 March 2011 and the subsequent review decision of Mrs Hill made on 23 May 2011 can be said to have been made to the best of their judgment and in that respect we will apply the principles laid down in *Van Boeckel* as set out above.

Submissions

13. Mr Husein submitted that the assessment made was not reasonable as to the amount of tax due and that Mr Mallia had failed to consider fairly all the material put before him. In particular, by failing to consider all the periods during which Mahir was trading and basing his assessment on the percentage of zero-rated sales during that whole period, rather than, as he did, ignoring the earlier periods and only selecting those periods most favourable to HMRC, Mr Mallia did not act fairly or to his best judgment. By concentrating only on the later periods and not considering further material that he could have done, such as the credit card receipts and the fact that Mahir had altered his sales strategy to concentrate on the sale of children's clothing in the later periods, Mr Mallia did not consider all the material that was available to him.

14. Mrs Knibbs submitted that on the absence of any sales records the assessment was raised to best judgment and was reasonable. The burden of proof was on Mahir to verify its sales which it was unable to do having destroyed its till rolls and having kept no stock records. Looking at the VAT returns from the entire trading period, only 14% of all purchases were zero-rated and therefore Mr Mallia's approach of using a figure of 25% was reasonable to allow for non-saleable purchases and the higher mark-up for children's clothing which had not in any event been evidenced.

Conclusions

15. Based on the papers before us and the evidence that we heard, it is clear that Mahir has failed to keep the necessary documents and records to enable HMRC to verify its returns. Based on the value of the zero-rated purchases made throughout its trading period, in our view it was reasonable for Mr Mallia to conclude that a history of 13 returns showing repayments due out of a total of 23 is inconsistent with 75% of the sales throughout the whole period being standard rated sales. Mahir, with whom the burden of proof lies, was unable to produce any evidence supporting its assertion that the reason why there was an increase in zero-rated sales was because of the change of strategy to concentrate on the sale of children's clothing and in the absence of till rolls or other evidence of particular sales, or any stock records to support its assertion that there had been a strong reduction in the stock of children's clothes in the later periods it cannot do so.

16. The only material available to Mr Mallia were the VAT returns themselves and the handwritten sales sheets produced by Mahir, with which the returns were understandably consistent. In our view Mr Mallia is not to be criticised for failing to ask for the credit and receipts in case they could shed any further light on the sales. As was made clear in the second passages from *Van Boeckel* quoted in paragraph 11 above, it is not the duty of HMRC to do the taxpayer's work for him and if Mahir felt that the credit card receipts would help in establishing the correct position as to the

proportion of zero-rated sales in the latter period then it was incumbent upon them to produce the relevant material to Mr Mallia. They had ample opportunity to do so following Mr Mallia's initial letter of 9 February 2011 setting out his findings following his visit.

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17. We therefore find that Mr Mallia's calculations were based on all the relevant material that was available to him. He made a value judgment on that material, in the context of the profile of Mahir's business, and in particular the fact that throughout the period that Mahir traded its purchases of zero-rated stock amounted to only 14% of its total purchases. In the light of that, the application of a 25% figure to zero-rated sales for the periods covered by the assessment resulted in a decision which was generous to Mahir and which was honest, bona fide and reasonable as to the amount of tax due.

15 18. We therefore dismiss the appeal.

19. 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.

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**TIMOTHY HERRINGTON
TRIBUNAL JUDGE**

RELEASE DATE: 19 June 2012

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