TC01593

Appeal number: TC/2011/02666

Income Tax; Closure Notice; Discovery Assessments; whether Appellant overcharged by assessments; whether Appellant negligently delivered incorrect returns; omission of sales; adequacy of business records; method of calculation of turnover and profit; takings build-up; relevance and calculation of funds obtained through gambling; applicability of Retail Price Index to takings build-up for year of enquiry to other years of assessment; presumption of continuity; onus of proof; Taxes Management Act 1970 ss. 8, 12B, 19A, 29, 36(1), 50(6), & 95; whether assessments should stand good - No; whether assessments should be reduced - Yes; appeal allowed in principle.

FIRST-TIER TRIBUNAL

TAX

WILLIAM CHAPMAN **Appellant**

- and -

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

TRIBUNAL JUDGE: **J. GORDON REID Q.C., F.C.I.Arb.**
Member: **PETER R. SHEPPARD, F.C.I.S., F.C.I.B., ATII,**

Sitting in public at George House, 126 George Street, Edinburgh on Monday 10 & Tuesday 11 October 2011

Alison Safadi for the Appellant

Colin Vallance, HM Revenue & Customs Appeals & Review Unit for the Respondents

DECISION

Introduction

1. The Appellant carries on the business of servicing and repairing motor vehicles. The appeal relates to assessments for the tax years 2004/2005 to 2007/2008 (and related penalty determinations) and raises *inter alia* questions about the onus of proof, the adequacy of the Appellant's business records, the methods of calculation of turnover and profit by the Respondents, and the identification and treatment of funds derived from the Appellant's significant gambling activities over the tax years in question.

2. For reasons we explain below, the Hearing, which took place at Edinburgh on Monday 10 and Tuesday 11 October 2011, focussed principally on the Appellant's activities during the tax year 2006/2007 (the "Enquiry Year"). At the Hearing, the Appellant was represented by his sister, Mrs Alison Safadi, who also gave evidence on oath. The Appellant attended throughout but did not give evidence. The Respondents (the "Revenue") were represented by Colin Vallance of their Appeals & Review Unit, Glasgow. He led the evidence of Maureen Hendry, an inspector of taxes. She was responsible for the enquiries into the Appellant's tax affairs. The Revenue produced a file of productions and a file of authorities. Mrs Safadi prepared and lodged two files of documents. There was considerable duplication. For convenience, we shall refer, where necessary, principally to the Revenue's file of documents.

3. Mrs Safadi has no legal or accountancy qualifications. She carries on business on her own account, in event management. In spite of her lack of experience and qualifications, she presented the Appellant's case, in the main, with commendable vigour and skill. Although she made a number of bad points, overstepped the mark in her cross examination of Mrs Hendry and had to be checked from time to time, these were more than outnumbered by the many pertinent questions she asked and points she made; she had a good command of the facts and the documents, and put forward some good arguments in her closing submissions. The Appellant, who is an alcoholic (but currently tee-total), was fortunate to have her assistance.

Assessments under appeal

4. The following assessments are under appeal:-

Year	Amount	Appealable Decision	Date Issued
2004/5	£16,676.58	Discovery Assessment	10 February 2011
2004/5	£6,670.00	Penalty Determination	11 February 2011
2005/6	£16,841.03	Discovery Assessment	10 February 2011

2005/6	£6,736.00	Penalty Determination	11 February 2011
2006/7	£17,663.44	Closure Notice	10 February 2011
2006/7	£7,065.00	Penalty Determination	11 February 2011
2007/8	£10,101.28	Discovery Assessment	10 February 2011
2007/8	£4,041.00	Penalty Determination	11 February 2011

5. The 2006/7 assessment is made under s28A (1)&(2) of the Taxes Management Act 1970, as amended (the "TMA"). The 2007/8 assessment is made under s29. The other assessments are made under s29 and s36. All the penalty determinations are made under s95(1)(a). The sums in the Table include National Insurance Contributions. The Tax and NIC amount in total to £61,282.33. Penalties have been charged at 40%. They amount in total to £24,512. That percentage was not attacked at the Hearing. Accordingly, if any tax is due a penalty charge at 40% will fall to be added. Interest also falls to be added.

Grounds of appeal

6. The broad ground of appeal is that all returns were correct; there had been no omission of sales; various funds passing through the Appellant's bank accounts and those of his wife, were attributable to the Appellant's gambling activities which were not taxable. In her closing submissions, Mrs Safadi argued that the assessments for the years prior to 2006/7 and the subsequent year could not possibly be correct. It was also asserted that, although the Appellant's business records were not in the format desired by the Revenue, they were nevertheless adequate and sufficient.

Legal Framework

7. There was no dispute about the legal framework within which this type of appeal (sometimes referred to as a back duty appeal) fitted. S9A TMA gave the Revenue power to enquire into the Appellant's return. They duly gave notice in relation to the Appellant's 2006/2007 return. They requested documents informally, then formally under s19A TMA as they were entitled to do. Once enquiries are completed, the Revenue issues a closure notice under S28A(1)&(2).

8. In relation to the timing of the discovery assessments issued under s29 TMA in this case for the years 2004/2005 and 2005/2006, the Revenue acknowledged that they had to bring themselves within s36 TMA and (as their Statement of Case puts it) *demonstrate at least negligence in relation to the extended time limit assessments for the years 2004/5 and 2005/6 and the penalty determinations.* S36(1), as amended, refers to a loss of income tax brought about *carelessly,* and enables an assessment to be made at any time not more than six years after the year of assessment to which it relates. We were not addressed on the timing of the amendment to s36(1) substituting in effect *brought about carelessly or deliberately* for *attributable to fraudulent or negligent conduct,* or any transitional arrangements. S29 of TMA contains a similar

amendment. Both have effect from 1 April 2010 (Finance Act 2008 s118 and Schedule 39 paragraphs 1, 3, & 9).

9. S50(6) TMA provides that if, on appeal, the tribunal decides that the appellant is overcharged by an assessment or a self-assessment, the assessment is to be *reduced accordingly, but otherwise the assessment …. shall stand good.* There is also power, in s50(7) TMA to increase the assessment if the tribunal decides that the appellant has been undercharged.

10. S95 TMA deals with penalties. No issue arose about the penalties claimed and we need say nothing further about the law on this topic.

11. S12B TMA requires a taxpayer such as the Appellant 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 a year of assessment or other period. These include records of all amounts received and expended in the course of trade.

Factual Background

The Appellant's Business

12. The Appellant is a motor mechanic by trade and carries on business as a sole trader servicing and repairing motor vehicles from garage premises at 25 Auchinairn Road, Glasgow, under the names Bishopbriggs Auto Services and Bishopbriggs Mechanical Services. He has been trading there from at least 2001. An apprentice mechanic assists him more or less full-time. Another individual worked part-time although what he did was not clear. The Appellant also had a receptionist but she seems to have left at some point after the Enquiry Year. The Appellant's wife was not involved in the business. She appeared to work elsewhere as a shop assistant.

13. The nature of the Appellant's business is best described as a backstreet garage. The principal type of work the Appellant carries out is brake pad replacement and servicing of older motor vehicles. Sometimes he provides spare parts for his work. On some occasions, customers bring spare parts to him and ask him to fit them. His typical charges over the Enquiry Year were about £60 for changing brake pads which normally takes about three quarters of an hour to an hour. For a service, he charged about £80 to £90. The total charge might be more depending on the spare parts supplied and the time taken to carry out the service. Normally, it would take about one and a half to two hours.

14. The information about his charges for his time was vague but appeared to be only about £25 for a couple of hours work, which seemed to us to be very low. There was no information about what charges were made for the time expended by the apprentice. He was paid about £75 per week during the Enquiry Year, which is barely £2 an hour for a 40 hour week and £2.50 per hour for a 30 hour week.

15. A constant throughput of vehicles having their brake pads changed which appears to be as profitable an activity as any other would yield at most about seven vehicles a day, five days a week, say fifty weeks a year and would produce a turnover of about £105,000 (7x£60x5x50).

16. In 2006, the Appellant bought additional equipment and expanded the premises of which he was the tenant. The equipment was purchased between January 2006 and June 2006 and included six ramps. This was said to be for convenience and to improve his working environment. He entered into a lease of four additional workshop units at a rent of £7,875 per annum plus VAT. The date of entry was 24 January 2006. He continued to trade while the expansion and improvements were being undertaken. In May 2006, he obtained a loan of £20,000 from the Bank of Scotland repayable over just over five years.

17. It seems to be accepted by the Appellant that he took on more staff in the tax year 2007/2008. How many, and what their hours were not the subject of evidence.

Bank Accounts and Statements

18. The Appellant had an account with RBS number ******49. Statements covering the period between 12/7/06 and 23/5/07 were produced. He also had a Bank of Scotland account No*****17. Statements covering the period between 26/3/06 and 8/5/07 were produced. No statements for earlier or later years were produced.

19. Mrs Chapman had a Royalties Gold Account with RBS number *****01. Statements covering the period 6/4/06 to 5/4/07 were produced. Her credit card statements over the Enquiry Year were also produced. She also had an Instant Access Savings Account with RBS, account number ******82. Statements covering the period from 6/4/06 to 5/4/07 were produced. These show among other items that between about October 2006 and April 2007 sums of £25 were regularly paid into that account by the Chapmans' daughters. This related to a loan of £1,000 made to each of them by the Appellant. The names Speirs and King which appear on the statements are the surnames of the daughters.

20. The loan obtained in May 2006 referred to above is shown as a credit entry in his Bank of Scotland account ***17 on 11 May 2006. However, the documents produced indicate that the equipment was purchased before the Bank loan was made; that the funds came from gambling winnings; and that £9,500 of the loan obtained was paid into Mrs Chapman's account. This is borne out by the credit entry of £9,500 on 16 May 2006 shown on her RBS account ****82, and the withdrawal of £10,000 from the Appellant's Bank of Scotland account ****17 on the same day.

21. We have mentioned various bank transactions to show that many of the entries are specific to the Appellant's circumstances at the time and are not indicative of any regular source of income or pattern of spending which might be applied with confidence to other years when drawing conclusions about his income.

The Revenue's Investigations

22. The Appellant submitted his Tax Return for the year ended 5 April 2007 (the Enquiry Year) on 9 January 2008. It disclosed sales of £42,777, a net profit of £11,175 and a profit for tax purposes (after deduction of capital allowances) of £7,720. It also disclosed that his business accounting period was from 6 April 2006 to 5 April 2007.

23. By letter[1] dated 5 January 2009 to the Appellant, the Revenue intimated that they intended to enquire into the return. A schedule of documents and information required was attached and was also intimated to the Appellant's accountants, D McFadyen Accountancy & Taxation Services (the "Accountant"). The information sought related to the accounts period 6/4/06 to 5/4/07 and included all prime records of sales including cashbook, sales invoices, remittance advices and other records used to record sales. Also required were *inter alia* work diaries, worksheets, appointment books, receipts for expenditure, bank statements, chequebook stubs, cash and bank reconciliation, financial accounts, wages records, details of creditors, drawings, capital allowances calculations, and an explanation of various items in the Appellant's submitted accounts.

24. When nothing was produced in response, a statutory notice requiring production of *inter alia* the above mentioned documents were sent to the Appellant on about 20 February 2009. The Accountant responded by letter dated 26 March 2009 stating:

> "Our client has mislaid his records for the 2007 Return
>
> The Sales figure was the amount provided by our client. The Wages only relate to an apprentice working during the year…".

The Revenue, in turn, responded by letter dated 30 March 2009 requiring *inter alia* bank statements, details of capital introduced, accounts with suppliers, the leasing of the Appellant's premises, employees, and capital allowances. A meeting was also suggested.

25. By letter dated 17 June 2009, to the Revenue, the Accountant produced the business bank statements. He provided further brief responses to some of the points raised in the correspondence.

26. A meeting took place at the Accountant's offices on 10 September 2009. The meeting lasted about one and a half hours. Also present were the Appellant, the Accountant, Mrs Hendry and one of her colleagues. The Revenue produced detailed typewritten minutes extending to eleven pages which were sent to the Accountant later that month. There is no record of the Accountant or anyone else disputing their accuracy at the time. They were not discussed in detail in evidence.

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[1] All letters from the Revenue should be assumed to have been written by Mrs Hendry unless otherwise stated.

27. The Revenue's purpose at the meeting was to consider the 2007 return in more detail and to find out more about how the Appellant's business operated. The Minutes recorded that the Appellant kept no cash hoards at home and that he was mostly paid by cheque. It appears from the Minutes that the Appellant's daughter, Tammy King, acted as a receptionist/book-keeper throughout the period 6/4/06 to 5/4/07 but left at some point thereafter. Mention was made of a ledger and records being removed by the police investigating a murder as a motor car in which the police were interested had passed through the Appellant's premises at some point. Reference was also made to a book for jobs and a ledger being kept and to the Appellant generally giving customers a receipt especially if there was a warranty with any spare parts provided. We are unable to reach any firm view as to what documents and records were removed by the police.

28. The Minutes also record that the premises were expanded in early 2006 when the lease was re-negotiated. Five or six ramps were installed to use instead of jacks for repairs. This led to an unspecified improvement in the business. The expanded premises and equipment were in place by around the beginning of the tax year 2006/2007. The Appellant obtained the loan mentioned above.

29. The Minutes note a discussion about the heritable property owned by the Appellant. Apart from the matrimonial home where he lived with his wife and his two surviving adult sons, the Appellant said that he did not own any. He was asked to reflect on this. He and the Accountant left the room; when they returned the Accountant explained that the Appellant had two buy to let properties from which he derived no profit and therefore thought he need not declare any interest in them.

30. The Minutes do not record any discussion about the Appellant's alcoholism or gambling activities.

31. Further correspondence ensued in relation to the Revenue's attempts to obtain comprehensive books and records relating the Appellant's activities over the Enquiry Year. In December 2009, the Appellant wrote to the Revenue apologising for his lack of commitment at the meeting in September 2009. He acknowledged that book keeping and paper work were not his strong points. The letter disclosed that the Appellant had assembled further paperwork. This was delivered to the Revenue in January 2010 by Mrs Safadi. Thereafter, the Revenue raised further queries and suggested another meeting which took place on 25 March 2010. By this stage, the Appellant had still not lodged his return for the tax year 2007/2008, apparently on the advice of the Accountant.

32. The Appellant, Mrs Safadi, the Accountant, Mrs Hendry and her colleague attended the meeting on 25 March 2010 which took place at the Accountant's premises at Bishopbriggs. The meeting lasted about one and a half hours. Minutes were prepared by the Revenue and extended to over six pages. Although the correspondence does not record it, by this stage the Appellant must have intimated that one source of his funds was his gambling activities. At the meeting in 2010, Mrs Hendry proposed a visit to the Appellant's home to examine a box, where gambling winnings and betting slips were said to be stored (see paragraph 44 below),

but the Appellant refused. There was, however, a short visit to the Appellant's premises after the meeting. There are no minutes of what transpired there. This was discussed in evidence at the Hearing. However, we were unclear as to what books and records were exhibited. They seem to have related to current business operations i.e. 2010.

33. After the meeting, the Appellant wrote to various bookmakers (about fifteen) with whom he had telephone accounts requesting statements of his accounts with them. At this stage, the Revenue were still seeking bank account details, details of his employees, a statement of assets and liabilities, capital allowance computations and a certificate of financial accounts. Copies of the Minutes were sent to the Accountant at the end of March 2010. There is no record of him challenging their general accuracy.

34. In May 2010, the Appellant provided some further information about his and his wife's bank accounts. He also provided information received from various bookmakers. By July 2010, Mrs Hendry had reached a number of conclusions. She concluded that (i) the Appellant had submitted an incorrect tax return for the Enquiry Year, (ii) he had omitted sales for that year, (iii) he failed to keep records of his sales and purchases, (iv) he was unable to substantiate the figures on his tax return for that year, (v) the additional funds in his and his wife's bank accounts could not be explained solely by the Appellant's gambling activities, (vi) the declared turnover of £42,777 for the Enquiry Year was low for the type of business in question and having regard to the recent expansion of his premises, (vii) in the absence, in her view, of business records, a takings build-up module (discussed below) should be used; this identified a shortfall in turnover of £52,114 (viii) the retail price index should be used to calculate shortfall in declared income in the earlier tax years 2004/2005 and 2005/2006, and the later year of 2007/2008, and (ix) the Appellant had failed to disclose rental from the buy-to-let properties which he had purchased. There was no dispute about point (ix).

The Takings Build-Up

35. The purpose of the Takings Build-Up is to identify the level of turnover required to account for funds deposited in the bank accounts of the Appellant and his wife, drawings, purchases, certain identified expenditure, and certain expenditure which is estimated, such as purchases for food and general living expenses. Some of the estimates may have been based on information provided by the Appellant's wife by letter dated 20 November 2009.

36. This produces a gross figure. Here it was £152,916. From that figure, deductions are made for identified cash withdrawals during the Enquiry Year, and non-business receipts. One example of non-business receipts was *dig money* received by the Appellant from his two sons, who lived at home throughout the Enquiry Year. Another example is the entry for the sale of a personal car registration number plate for £15,000. Mrs Hendry accepted that, as explained in Mr Chapman's letter dated 15/1/10, this was unrelated to his business. He received two cheques totalling £15,000 (£14,750 and £250) which were credited to one of his bank accounts. The total sum which fell to be deducted from the sum of £152,916 was £58,025. This left

a net figure of £94,891 representing (according to the Revenue) the turnover required to account for the flow of funds. The declared turnover for the Enquiry Year was £42,777, producing a shortfall or omitted sales of £52,114 (£94,891-£42,777).

37. Mrs Hendry applied the Retail Price Index to the shortfall derived from the Takings Build-Up to the tax years 2004/2005, and 2005/2006. This increased the declared turnover for these years of £45,227 and £42,239 by £48,612 and £49,855 respectively. She did not attempt a Takings Build-Up for the years 2004/2005, 2005/2006, or 2007/2008 or call for details of bank transactions during those tax years which could have been used to create a Takings Build-Up for each tax year under scrutiny.

38. She applied the same approach for the tax year 2007/2008. The declared turnover for that year was £61,234. The calculated increase was £54,295 using RPI (to identify a percentage increase on the calculated turnover of £94,891 for the Enquiry Year). However, this produced a total turnover of £115,529 which she regarded as too high. She therefore reduced the increase to £33,766. This produces a calculated turnover of £95,000 for the year to 5 April 2008. In her letter dated 23 December 2010, she explained the position this way:-

> "In this instance I have considered the fact that you actually recorded a higher turnover for that year and therefore intend to make the additions in line with the revised turnover figure for 2006/2007 rather than RPI, this means that the additions will be £33,766 and not £54,295 (if RPI was used)."

39. The correspondence discloses that in November 2010 Mrs Hendry indicated that an offer of settlement in the order of just under £60,000 which included interest and penalties might well have been accepted. However, the Appellant did not take up the suggestion.

The Appellant's Health

40. The Appellant has been an alcoholic from some point in the nineties if not before. While there were no medical records to vouch this, the Revenue accepted that the Appellant was an alcoholic. The evidence of his sister, which we accept, was that the Appellant was extremely distressed by the death of his brother in 1994. This affected the Appellant's drinking habits. His condition was compounded by the death of his son in 2001 at the age of twenty one years. It is plain that such a family tragedy can have a devastating effect. According to Mrs Safadi's evidence, which we accept, the Appellant was drinking heavily between 2001 and 2008 although by some point in 2007 his health was improving. Happily, he has been able to curtail his drinking habits and has been tee-total since some point in 2008.

The Appellant's Gambling Activities

41. The Appellant has been a heavy and regular gambler for many years. He bet mainly, if not exclusively on football results, principally the English Premier League. He had accounts with at least fifteen betting establishments.

42. He placed bets with these bookmakers over the telephone on a regular basis. The amount which he bet on any one result varied considerably from about £50 to several thousand pounds. He sometimes placed four or more substantial bets in the course of a single day.

43. He also bet in cash locally at nearby betting shops. He frequently spent much of his day drinking in the local public houses, and betting at the local bookmakers. There are no records from which it can be determined how much cash he spent at local bookmakers or what its source was or indeed what profit, if any he made from this aspect of his gambling activities. We were informed that about 70% of the Appellant's customers paid by cheque.

44. Although at the meeting of 10 September 2009, the Minutes record the Appellant as stating that he kept no cash hoards, the Minutes of the meeting of 25 March 2010, record that the Appellant kept winnings and winning betting slips in a box at his home. According to the minutes, the Appellant was vague about this box its size, type and contents and at one stage said there were several boxes. The Appellant is recorded as saying that there was £71,000 in the box before he purchased a property for his parents. He subsequently exhibited to the Revenue winning betting slips amounting to about £71,000; these slips covered a period of about 14 months between February 2005 and May 2006. That sum included the stake money laid out to make the bets. It does not mean that he made £71,000 *profit.*

45. Betting slips which the Appellant had produced also showed total stake money of £37,313. Arrangements were made to enable the Revenue to contact the bookmakers with whom the Appellant had accounts so that details of his gambling activities could be obtained.

46. The productions included a very large quantity of betting slips (almost all winning slips). The Appellant did not generally keep betting slips when he did not win. Statements of account for various periods were produced by eight bookmakers. However the earliest period covered was 4 February 2007 (Boyle Sports). One other account (Stan James) begins on 4 April 2007. All the rest begin after the end of the Enquiry Year.

47. Both parties carried out various calculations to show the amount bet by the Appellant, the amount won and the amount lost over various periods.

48. One exercise carried out by the Revenue showed a win rate of about 27%, which of course is impressive. This was based on the winnings of £71,000 and the stakes of £37,313. This appeared to cover the period between February 2005 and May 2006. Another carried out by Mrs Safadi showed a win rate of 53% based on an analysis of the Boyles Sports statements between 4 February 2007 and 18 March 2007. In the Coral account covering the period between 18 March 2007 and 5 April 2007 the win rate was 29%. Yet another showed a win rate of about 43%. None could present a true overall picture as cash betting could not be included in the calculations. Although some bank deposit entries were examined and might well be attributable to cash winnings, an examination of these did not enable a reliable conclusion to be

made, even although the Bank of Scotland account ***17 showed that between 6 February 2007 and 5 April 2007 the Appellant bet a total of £56,210 and received £68,813.60 i.e. net winnings of £12,603.60 in just under two months. Winning bookmaker receipts for 2010 amounted in total to £39,619.32.

49. All this shows that profitability in gambling is normally the subject of substantial variance and analysis of short periods are not indicative of an overall success or failure rate in the long run. The same is true of other games which mix skill and chance such as poker, where the variance is notorious.

50. On balance, while the records showed that over some periods the Appellant made an overall profit, the general impression from all the information was that the Appellant was probably not as successful a gambler as he thought and that overall his gambling activities from the records produced did not yield as great a profit as the Appellant believed. At one of the meetings it is recorded that he claimed to win nine times out often. Whether his cash betting made him a profitable or more profitable gambler is impossible to say because the evidence does not enable any conclusion to be drawn.

51. The evidence of the Appellant's gambling and drinking activities does enable us to conclude that the Appellant was not and could not have been constantly attending to his garage business throughout normal business hours particularly in the earlier tax years. There was no evidence that the garage was open outwith normal business hours during the week. Mrs Safadi told us and we accept that the garage opened on an occasional basis on a Saturday to accommodate customers. This is also noted in the Minutes of the meeting on 10 September 2009.

52. The Appellant's business could not have had a constant throughput of vehicles being serviced, repaired or having their brake pads renewed throughout each hour of each day of the week. This is relevant to the question of turnover which we discuss below.

The Appellant's Business Records

53. Throughout the periods of the assessments in question, the Appellant's business records appeared to be shambolic, incomplete and unreliable. In a document produced on behalf of the Appellant (which the Appellant appears to have signed) in relation to equipment purchased between January and June 2006, it is stated *I did not ….have a book keeping system in place.* At some point in 2008, Mrs Safadi became involved in the administration of the Appellant's business. This led to an improvement and is probably the principal reason for the Appellant's accounts for 2007/08 showing a substantial increase in turnover (in the order of 50%). Mrs Safadi was, no doubt, able to collect and collate more efficiently information about the Appellant's business activities during that tax year.

54. Although the Minutes of the meeting dated 10 September, mention a ledger and book relating to customers, these did not feature in the evidence at all. Mrs Safadi's evidence, which we accept, was that customer and work details were generally written

down on pieces of paper. While she tried to emphasise the accuracy of this system our overall impression was that it was somewhat haphazard and unlikely to be wholly comprehensive or accurate. The Minutes also record that prior to July 2006 when a RBS account was opened the Appellant only accepted cash from his customers.

55. The Minutes of the meeting dated 25 March 2010, record that by that stage the Revenue had still not received what they regarded as adequate records of the Appellant's business over the Enquiry Year.

56. The Appellant was and so far as we are aware is not registered for VAT. He did not prepare or issue invoices to his customers for work carried out.

57. The Accountant prepared the accounts for the Enquiry Year. It is not clear when he first started to act for the Appellant. He did not calculate PAYE or national insurance details for the Appellant's employees in the Enquiry Year but did so in later years.

58. Mrs Safadi prepared and produced various spread sheets which show that, while the declared turnover for each of the tax years 2004/2005, 2005/2006 and the Enquiry Year, was similar, there was a dramatic increase in declared turnover of almost 50% for the tax year 2007/2008, yet purchases remained relatively constant over these four tax years. On the other hand, while wages costs remained broadly similar for the first three tax years, in the tax year 2007/2008 they soared from £3,882 to £20,285. There were no telephone and office costs for the first three tax years but £4,727 for the tax year 2007/2008. These figures are also reflected in the very brief trading and profit and loss accounts prepared by the Accountant.

59. The Appellant's Trading and Profit and Loss Accounts for the year to 5 April 2005 disclosed sales of £45,227, wages of £4,484 and a net profit of £12,910. For the tax year to 5 April 2006 the accounts disclosed sales of £42,239 wages of £3,998 and net profit of £11,294. For the Enquiry Year the Accounts disclosed sales of £42,777 wages of £3,882 and a net profit of £11,175. For the year to 5 April 2008 the Accounts disclosed sales of £61,234, wages of £20,285, and a net profit of £11,564. However, in a spread sheet prepared by Mrs Safadi staff wages for the tax year 2007/2008 are shown at £8,531.00. There is also a nil entry for *Wages Billy* which may be a reference to the Appellant.

Purchase of Properties

60. The Appellant originally denied at the meeting held on 10 September 2009 that he owned any properties apart from his own home. He subsequently recanted at the same meeting and confirmed that he bought a property at Forresthall Drive, Glasgow in 2008. The transaction settled in July 2008 and the property was let the following month. There is a mortgage over that property.

61. He also stated at the meeting that between about September 2007 and March 2008 he bought a property at Sinclair Gardens, Glasgow. There is a mortgage over the property. Documents produced show that 7 Sinclair Gardens, Bishopbriggs,

Glasgow was purchased by the Appellant in 2007. The transaction settled in June 2007 and the property was let the following month.

62. The Appellant also stated at the meeting that he had bought a house at 17 Broadleys Avenue, Bishopbriggs, Glasgow for his parents. Documents produced show that the transaction settled in October 2006. The Appellant appears to be liable for the mortgage but his parents actually pay it as is disclosed by bank statements in their name covering the period of the Enquiry Year. The financial arrangements between the Appellant and his parents led to two payments totalling £12,000 being transferred from their bank account to his Bank of Scotland account ****17 in September 2006.

63. The Revenue accept that the outgoings for the first two properties equal or exceed the rent generated from them. Rental income has not been used in any of the Revenue's calculations.

64. Finally, we record for completeness that documents produced show that the Appellant purchased his present home at 6 Miller Close, Bishopbriggs, Glasgow in 2005. There is a mortgage over that property.

Closure and Assessments

65. Mrs Hendry sent a closure notice to the Appellant in relation to the Enquiry Year on 10 February 2010. It was issued under s28A (1)&(2) of TMA. It recorded that the Appellant's Self-Assessment return was being amended to reflect omitted sales of £52,114, and additional tax of £17,663.44. Details of the calculation were enclosed.

66. On the same date, a Notice of further assessment for the year ended 5 April 2005 was issued to the Appellant. The amount of additional tax assessed was £16,676.58. This reflected the additional tax due as a result of omitted sales of £48,612 calculated by reference to the Takings Build-Up for the Enquiry Year and the application of the Retail Price Index. Details of the calculation were enclosed.

67. On the same date, a Notice of further assessment for the year ended 5 April 2006 was issued to the Appellant. The amount of additional tax assessed was £16,841.03. This reflected the additional tax due as a result of omitted sales of £49,885 calculated by reference to the Takings Build-Up for the Enquiry Year and the application of the Retail Price Index. Some details of the calculation were enclosed.

68. On the same date, a Notice of further assessment for the year ended 5 April 2008 was issued to the Appellant. The amount of additional tax assessed was £10,101.28. This reflected the additional tax due as a result of omitted sales of £33,766.00 calculated initially by reference to the Takings Build-Up for the Enquiry Year and the application of the Retail Price Index, and subsequently modified as described by Mrs Hendry in her letter dated 23 December 2010. Some details of the calculation were enclosed. On 11 February 2010, Penalty Notices were issued as specified in the Table set out above at paragraph 4.

Submissions

69. Mrs Safadi submitted that the sum of £52,114 which is the shortfall of funds in the Takings Build-Up which the Revenue claim are omitted sales could be accounted for by the Appellant's gambling activities. She referred to her exercise of calculating gambling activities between the period 6 February 2007 and 5 April 2007. She noted that the cases cited by Mr Vallance contained no such evidence or evidence of bank accounts. The Accountant had examined the records for the Enquiry Year. The Appellant's records while not in the format required by the Revenue were nevertheless adequate and complete. There was no hard evidence of omitted sales. Better book-keeping was in place for the year 2007/2008 so those figures were more likely to be accurate. The turnover for the Enquiry Year contemplated by the Revenue in the Takings Build-Up was simply not feasible for a small backstreet garage. The Revenue correspondence contains many errors and should be considered carefully. She submitted in effect that the Takings Build Up was an artificial exercise with no hard evidence to back it up.

70. She also submitted that the omission of the rental from properties was a mistake which made no difference as no profit was derived from them. In fact, there were losses which the Appellant could have claimed in relation to them so it was he who had suffered not the Revenue.

71. She submitted that if the assessment relating to the Enquiry Year was bad then the assessments for the other years fall away.

72. Mr Vallance acknowledged that the onus was on the Revenue to prove neglect in relation to the tax years 2004/2005 and 2005/2006. But, he submitted, once there was a finding of neglect, the onus in relation to quantum falls on the Appellant. He referred to sections 36 and 95 of the TMA. Here there was evidence of careless breach of duty. The Appellant failed to keep a record of sales and purchases; he failed to keep a record of drawings; he failed to disclose rental income. Essentially, the only evidence of the Appellant's activities over the Enquiry Year was the bank statements; there were no ledgers. Mr Vallance referred to s12B (1)(a) of the TMA. On the question of onus he referred to s50(6) of TMA and to *Norman v Golder 1944 TC 293 at 297, T Haythornthwaite & Sons Ltd v Kelly 1927 11 TC 657 at 672 and Nicholson v Morris 1977 51 TC 95 at 110.* There was no evidence to substantiate that deposits from property bought by the Appellant came from gambling winnings. The Appellant did not keep complete records of his gambling activities; reference was made to *Brimelow v Price 1965 49 TC 41 at 48.*

73. RPI was an appropriate way of calculating the amount due for the earlier and later tax years. Reference was made to *Jonas v Bamford 1973 51 TC 1 at 25* and to *Franks v Dick 1955 36 TC 100 at 108.* The presumption of continuity applied both to the earlier years and the later year. Mr Vallance acknowledged that there were no bank statements for the earlier or later years, but that the Revenue had power to require their production.

74. With regard to the tax year 2007/2008 he accepted that RPI produced a result which was wrong hence the reduction which Mrs Hendry made. He was unable to provide any answer to the question posed by the Tribunal, namely if RPI is wrong for 2007/2008 how does it produce a correct result for 2004/2005 or 2005/2006? He did however, make a passing reference to *Coy v Kime* which we have identified as being reported at *1987 STC 114.*

Discussion

Assessment of the Evidence

75. We found both Mrs Hendry and Mrs Safadi to be generally reliable and credible. In particular, we do not accept the allegation made by Mrs Safadi in cross-examination that Mrs Hendry was telling lies. Mrs Hendry gave her evidence with considerable restraint having regard to the extreme nature of Mrs Safadi's questions. There were differences of recollection between them as to what transpired at the meetings and the visit to the Appellant's premises. These differences were largely on matters which were ultimately unimportant for the decision-making process although we can understand that a lay representative might regard them as important. For example, Mrs Safadi repeatedly accused Mrs Hendry of telling her to shut up at one of the meetings. Mrs Hendry denied this. Whether she did or did not tell Mrs Safadi to shut up does not matter at the end of the day. The Appellant's position was adequately protected. The Accountant was present throughout.

76. The Appellant did not give evidence although he sat in the Tribunal room throughout and watched the whole proceedings. He passed information to Mrs Safadi from time to time. However, the evidence as a whole was somewhat unsatisfactory and full of gaps. The documentary evidence was very difficult to follow and impenetrable in places. Although Mrs Safadi did her best, this was largely due to the Appellant's failure to keep adequate business records; this was compounded by the fact that he did not keep a complete record of his gambling activities even although he was not obliged to do so.

77. It was accepted by the Revenue that the Appellant was an alcoholic. His health, happily, seems to have gradually improved in 2007 and 2008; he has been tee-total since some point in 2008. It was said that he was too nervous and stressed to give evidence. There was, however, no medical evidence whatsoever. Mrs Safadi indicated that the Appellant's GP would not provide a letter or report unless ordered to do so by the Tribunal. We therefore cannot hold that the Appellant was unfit to give evidence. It may be that he simply chose not to give evidence to avoid awkward questions about his business and his record keeping. We do not propose to draw adverse inferences from his failure to give evidence but we cannot draw inferences favourable to him where the evidence appears confused or the true position doubtful.

78. Finally, as to the state of the evidence (particularly the documents), it is not the function of this Tribunal to act as forensic accountants and examine in detail all the documents produced (many of which were never considered in detail at the hearing) and come up with the answer (see *Hurley* referred to below at page 312). The Revenue spent a great deal of time and effort attempting to unravel the Appellant's

business affairs. We have a considerable degree of sympathy for the approach which they took. They made strenuous efforts to resolve the dispute without the necessity of a tribunal hearing.

The Appellant's Business Records and Turnover during the Enquiry Year.

79. Both parties focussed on the Enquiry Year. Virtually, all the evidence related to that period. It was assumed that the other years stood or fell with the Enquiry Year. That is how matters have turned out; no attempt was made to examine the Appellant's business activities and bank and cash transactions in the earlier years or in the later year. Accordingly, if these earlier and later assessments overcharge the Appellant, there is no mechanism we can adopt or evidence we can apply to identify how the assessments should be *reduced accordingly* (TMA s50(6)). If that is so, the assessments must be discharged or set aside, or to use the statutory language, be *reduced* to nil. This arises not because of the inadequacy of the Appellant's records but because of the approach and methodology adopted by the Revenue and the evidence which we heard. Allowing an assessment to fall because of the inadequacy of a taxpayer's business records would be a rogue's charter. The Appellant here has at least produced professionally prepared accounts for the years in dispute, albeit based to some extent on questionable record keeping.

80. Mrs Safadi was not involved in the Appellant's business or the preparing, maintaining or keeping such records during the Enquiry Period. Accordingly, the picture of what the Appellant actually did by way of record keeping and what his actual turnover was indirect and somewhat vague. We heard evidence from Mrs Safadi that the Appellant wrote down on a piece of paper, details of the business with each customer. When this was done, and whether the price was written down at the outset, and what was given to the customer was simply unclear; how these pieces of paper were stored or whether they were left lying around the Appellant's premises is also not clear. It was said that a *receipt* was given for warranty purposes where spare parts had been bought by the Appellant and installed in the course of the work. That is not the normal type of warranty document. A customer would normally rely on his rights under a contract for the supply of goods and services. What was not given to the customer was an invoice setting out the work done and the price charged. The basic record of turnover was therefore absent.

81. The Minutes of the meeting held on 10 September refer to a receptionist being employed during the Enquiry Year. She is said to have had a computer; but what she did with it is a mystery as there do not appear to be any computer generated contemporary records. What was sent to the Accountant at the end of each year and in particular at the end of the Enquiry Year is also not certain.

82. Overall, the Revenue were justifiably dissatisfied with and suspicious of the Appellant's business records for the Enquiry Year. In our view, they were entirely justified in resorting to the preparation of a Takings Build-Up for the Enquiry Year. As described above, this involves an analysis of the funds available to the Appellant, his outgoings, actual and assumed, with a view to establishing the level of turnover needed to support his financial transactions during the year in question.

83. On the findings we have made, we conclude that the Appellant's business records were inadequate for the tax year 2006/2007. The Appellant failed for one reason or another properly to collect and collate records of all transactions with his customers. The system (if it was a system at all) which he operated was bound to lead to incomplete and incorrect recording of his turnover. He had no system of invoicing customers. He did not seem to keep any regular ledgers. He relied on writing down brief details of transactions on pieces of paper which may have been left lying around his premises. Some were bound to be lost. It was not disputed that at least 30% of his transactions were in cash. Given his lifestyle of uncontrolled drinking until about 2007/2008 and his cash gambling locally, it is not surprising that funds from his gambling and funds from his business appear to have become inextricably mixed. The result is that the Appellant's business and gambling transactions are largely impenetrable. We have considerable sympathy for the Revenue and their attempts to identify what is truly taxable.

84. While we have some reservations about the logic of some aspects of the Takings Build-Up it was not challenged as an appropriate approach for the Enquiry Year. However, it is an analysis based on the particular transactions of that year and seems to us to be difficult to justify applying the results to other years. It is an examination of specific transactions which happened to occur in that year. No inference can be drawn from that examination that the same transactions or similar ones occurred in the ensuing or past years. For example, £15,000 was taken out of the equation because it related to a non-business transaction (sale of a registration plate). It cannot be assumed that a similar transaction will occur in another tax year even if the result of that particular transaction being excluded was to the taxpayer's benefit.

85. There were really only two points of dispute in relation the Takings Build-Up. The first related to part of a loan taken out by the Appellant in early 2006. This was taken out of the calculation as it formed part of a sum of £24,250 which was used to calculate the Required Sales figure. Had it not formed part of the sum of £24,250 that figure would have been lower and the Required Sales figure and the consequent omitted sales figure would have been higher.

86. The second point relates to the resulting *Required Sales* figure of £94,891. This represents the Revenue's assessment of the Appellant's turnover for the Enquiry Year. At the end of the day, the Takings Build-Up is only an estimate and it is necessary to stand back and consider whether the resulting figures are realistic. We consider that a turnover of 2006/2007 of almost £95,000 for the Enquiry Year is wholly unrealistic. We have described the type of work carried out, the sums charged and the hourly rates which seem to have been applied during the Enquiry Year. These were not challenged. In those circumstances, there would have to have been a constant stream of motor vehicles passing through the Appellant's premises fifty weeks a year and a production rate of six or seven vehicles every day. Given the evidence of the Appellant's health, his drinking and his gambling habits it is plain that he was not present working on the premises throughout the day. He appears to have been the only qualified mechanic on his premises although he had assistance from an

apprentice and possibly one other part-time worker. An apprentice and the other part time worker are unlikely to have worked on their own or, if they did, they are unlikely to have worked as efficiently as an experienced and fully trained mechanic. There was no evidence that the other part time worker was a trained mechanic.

87. This leads us to find on the balance of probabilities that the closure notice, which is based on a turnover of £94,891 must be wrong. To put it another way we are satisfied on a balance of probabilities that the Appellant has been overcharged by the assessment. The assessment must be reduced accordingly.

88. Using our best judgment, we consider that a throughput of vehicles of a little more than half that required to justify a turnover of £94,891 is reasonable and justified on the evidence. We have already made findings about the Appellant's work and charges. Given the Appellant's apparent erratic work pattern during the Enquiry Year and the relatively modest assistance he had, we consider that a realistic throughput would be about an average of four vehicles a day at about £60. This produces a turnover for the Enquiry Year of £60,000 (4x£60x5x50). That is equivalent to £30 per hour for a 40 hour week and a 50 week year. That exceeds the hourly rate referred to above. We have reservations about the accuracy of that rate. The more likely rate is at least £25 per hour rather than for two hours. £25 per hour is more in line with our assessment.

89. A turnover of £60,000 is also in line with the turnover for the ensuing year (2007/2008), which was £61,234. The Appellant's return for 2007/2008 had still not been submitted when the parties met in March 2010. The Appellant's premises expanded in the first half of 2006, so it would not be surprising that the turnover increased significantly from the two previous years (2004/2005-£45,227; 2005/2006-£42,239). In addition, by 2007, the Appellant's health was improving so it is reasonable to conclude that he was probably working more regularly and efficiently. It is true that the entry for wages for the 2007/2008 was substantially greater than the previous year. There was no evidence of a significant increase in the number of employees for 2007/2008 although the wages bill increased. Finally, by the time the 2007/2008 accounts came to be prepared, Mrs Safadi had become involved. It is reasonable to conclude that she was more diligent than the Appellant had been in identifying the true extent of the turnover and collecting and collating the relevant information in a more accurate manner. She was not involved in such an exercise in relation to the Enquiry Year.

90. The evidence, such as it is, discloses that the Appellant was a reasonably successful gambler. One calculation showed that in a fourteen month period he made a return of 27% on his telephone betting. Another calculation indicated a profit of up to £5,000 per month. At the very least this suggests that the Revenue may have underestimated the extent of the Appellant's funds derived from his gambling activities.

91. We acknowledge that if a man makes substantial sums of money in betting it is not unreasonable to expect him to keep records of his betting transactions so that if he is subsequently challenged by the Revenue to explain an increased wealth he can

satisfy them that it is not due to any undisclosed taxable profits but to his betting winnings. If he chooses not to do that he runs the risk of having attributed to taxable profits what, if he had kept records of his betting transactions, he might have been able to convince the Revenue were in fact untaxable betting winnings. (See *Brimelow v Price 1965 49 TC 41 at 48*).

92. In our view, the closure notice therefore overcharges the Appellant. The figure for omitted sales in the Takings Build-Up falls to be reduced to **£17,223 (£60,000-£42,777** [the declared turnover - see paragraph 36 above]**).** This proceeds upon what we regard as a realistic turnover, namely £60,000 rather than the turnover of £94,981. We have been asked to issue a decision in principle on this issue. We therefore leave it to parties to agree the amount of tax due. No argument was presented on the question of penalty or interest. Accordingly, the basis on which these were charged remains the same; but they will be applied to a reduced figure.

The Revenue's Calculations for the Tax Years 2004/05 and 2005/06

93. The assessments are based on an application of RPI to the Required Sales figure in the Takings Build-Up for the Enquiry Year. For the reason already given the Takings Build-Up cannot be applied across the board.

94. It is, we understand, common for the Revenue where they have to show fraudulent or negligent or careless conduct and a loss of tax attributable to it to produce what are sometimes referred to as capital statements for the tax year in question to demonstrate under-declarations and a loss of tax. The burden under s36 TMA may be discharged depending on whether the taxpayer offers any explanation and the adequacy of that explanation. A good explanation of the composition of capital statements is to be found in Park J's judgment in *Hurley v Taylor 1998 71 TC 268 at 282-3; see also page 286-7; 289*; these passages and the passage referred to below are not affected by the Court of Appeal's decision in the same case). No capital statement or Takings Build-Up has been produced for either of the earlier years of assessment in the present appeal. All the evidence or at least the bulk of it related to the Enquiry Year. The Appellant's books and records may well have been poorly kept for the earlier years, that is to say incomplete and therefore unreliable. That is probably negligent or careless conduct, but we cannot, on the material before us, infer what the result of that was (see *Hurley at 292*). The Revenue have failed to discharge the s36 burden of showing that there was a loss of tax attributable to that negligent conduct.

95. The application of RPI does not, in any event, seem to us to be a legitimate way of proceeding. On the evidence, we cannot identify any other way. We do not know what the Appellant's charges were in the earlier years. We therefore cannot make any reasonable assessment of what the turnover would have been. We cannot apply a percentage to the declared turnover based on the declared turnover for the Enquiry Year and what we have found it to be. The Appellant says it is as he declared it to be. It is substantially less than the turnover for the Enquiry Year as we have found it to be. That makes some sense insofar as sense can be made of the Appellant's business

and non-business activities and record keeping. The Appellant was probably less fit for work in those years, and thus less productive; his premises were smaller.

96. When asked why a Takings Build-Up was not produced for the earlier years the answer given by Mr Vallance, after consulting Mrs Hendry, was *time constraints.* That was a commendably honest answer. Having spent so much time and effort on the Enquiry Year, we do not find this surprising but we cannot endorse such an approach in this case where the Takings Build-Up relies on a number of specific transactions peculiar to the Enquiry Year.

97. Business economic models have their place in HMRC's enquiry work but they have also been the subject of criticism (see e.g. *Scott v McDonald 1996 STC (SCD) 381 at 387*). They do not give a precise result but may produce a more realistic estimate of the profits than the accounts based on unreliable and incomplete records. Where a capital statement is prepared for one year and sought to be applied to other years, they have to be adjusted to take account of exceptional items peculiar to the particular year. That was not done here.

98. These assessments therefore cannot stand. As there is no basis upon which we can substitute another figure, the assessment must be reduced to nil. The penalties and interest will also be reduced to nil.

The Revenue's Calculations for the Tax Year 2007/08

99. The Revenue must have considered that the application of RPI to the Takings Build-Up to be wrong for the tax year 2007/2008 as they reduced their omitted sales figure considerably, as discussed above.

100. The calculation seems to us to be arbitrary and cannot stand. The Takings Build-Up is peculiar to one specific tax year and cannot be applied across the board. It is based on an analysis of a number of specific banking transactions which have no particular pattern, and which have to be adjusted in the light of specific information about them (e.g. the transaction relating to the car registration plate). For that reason alone the assessment cannot stand. Moreover, for the reasons already discussed a turnover of £95,000 is simply unrealistic and must, on the evidence, be wrong.

101. As there is no basis upon which we can substitute another figure, the assessment must be reduced to nil. The penalties and interest will also be reduced to nil. Moreover, the declared turnover for the year 2007/2008 was £61,234. This is in line with our own assessment for the Enquiry Year. As we have already noted (paragraph 53) Mrs Safadi's involvement in the administration of the Appellant's business and her collection and collation of information led to an improvement in the Appellant's record keeping. We can identify no basis for concluding that a declared turnover of £61,234 is an under-declaration; and if so by how much.

Presumption of Continuity

102. In *Franks* there was detailed evidence of the taxpayer company's book-keeping, and more importantly, evidence of a suspicious transaction which led the Revenue

accountant to give evidence that the directors were occasionally receiving payments from customers which were not recorded in the company's cash book (paragraph 10 page 103). Although there appeared to have been a thorough examination of the company's books only one discrepancy was found. Nevertheless, the Commissioners held that the Company's accounts could not be relied upon, and the assessments were, in large measure, confirmed. The commissioners did not indicate what evidence they accepted or rejected; nor did they give reasons for their conclusion that the company's accounts could not be relied upon to show its whole trading profits. On appeal, Danckwerts J simply asked himself whether there was evidence on which the Commissioners could have come to the conclusion they reached. On the basis of the one incident he held that there was; and that it was open to the Commissioners to conclude that there must have been other similar incidents even although there was considerable evidence that the company's records had been properly kept and fully examined, but only one discrepancy had been found. *Franks* seems to us to be a somewhat surprising decision which might have been dealt with differently today. We do not read it as supporting the Revenue's approach to the earlier years and the later year in this appeal.

103.In *Jonas,* the taxpayer was a company director with a controlling interest; he was also a gambler. A wide range of issues were canvassed. There was evidence of company irregularities procured by the taxpayer. The Appellants produced no accounts and led no evidence of the company's turnover. The Revenue in that case deployed a similar approach to the Takings Build-Up as their computations showed a *Cash Deficiency* for the first six of the tax years under consideration. The taxpayer sought to explain part of that deficiency by reference to successful betting on horses. The evidence was inconclusive and the Commissioners assumed he broke even for some of the years in question but not others. The onus was on the taxpayer to displace the assessments; all assessments were confirmed except one (1957/58)which was discharged because the Revenue failed to prove wilful default. On appeal, Walton J held that the taxpayer had failed to discharge the onus of showing that the assessments in question were wrong (page 24). In particular, he rejected the taxpayer's attack on the Commissioners' findings of fact that various items should be taken as credits and taken out of account in making the assessments. In relation to the last three years of assessment (1962-65) the taxpayer had declined to provide any information. Accordingly, the inspector issued assessments in the round sum of £5,000 for each year. The Commissioners dealt with these years briefly, noting that the Appellant had not discharged the onus on him (page 18). On appeal it was argued that the inspector had not sought discovery, and there was no evidence of any unexplained intake of moneys by the taxpayer. Walton J dealt with these arguments thus (at page 24):-

> "But, so far as the discovery point is concerned, once the inspector comes to the conclusion that, on 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 on the taxpayer."

104.The presumption *goes on until there is some change.* The presumption as expressed in that case looks to the future and not the past. It is difficult to see how one can apply such a presumption based on the Enquiry Year to the earlier years. Moreover, there was some change in the tax year 2007/2008. There was a dramatic rise in declared sales which is in line with what we have found the turnover for the Enquiry Year to be. Mrs Safadi became involved in the maintenance and collation of the taxpayer's business records and the records of his gambling activities. We consider these matters to be sufficient to negate any presumption of continuity which might otherwise have been justified. Even then, there would have to be some adjustments to take account of transactions peculiar to the Enquiry Year. That was not done.

105.Overall, *Jonas* reaffirms that the onus lies on the taxpayer to show that the assessments are wrong and ought to be reduced or set aside (see also *Norman at 295* and *297*; *T Haythornthwaite at page 667, 670, 672, 673* and especially *Nicholson at page 110;* and in the Court of appeal at 119). Here, we, as the fact finding body are indeed satisfied, on the balance of probabilities, that all the assessments are wrong and cannot stand.

106.We should add that in our view *Coy v Kime* does not assist the Revenue in this appeal. *Coy* was a back duty case in relation to a taxi-driver. The inspector calculated the taxpayer's gross income for the fourth of five consecutive tax years, by reference to fuel expenditure, an assumed rate of consumption (mpg), an average length of trip, 15% tips and an allowance for a night rate. He also relied on a government survey relating to average family expenditure and argued that declared profits for earlier years should be increased pro rata using the retail price index (see page 116). There was, in addition, specific evidence of sundry bank deposits over the first four tax years in issue although these do not seem to have been used in the calculations. (see pages 115, 117 and 119). The court, on appeal, held that the commissioners' determination was justified on the evidence (at 120). There was no discussion of the presumption of continuity or the application of the retail price index. It is certainly an example of the application of the retail price index but how it was applied is not clear.

107.*Coy* was referred to recently but not discussed in *Khawaja v Etty 2004 STC 669*. That was a back duty case relating to a restaurant. The Appellant's records were inadequate. The Revenue derived their figures from calculations based on the amount of meat purchased by the restaurant, the wastage involved in preparation of the meat, the average amount of meant used per meal and the average value of each meal (see paragraph 26 page 680). The Revenue described this as the *business economics test* (paragraph 20 page 679). Detailed evidence and calculations centred around a base year (1995-1996). Omitted remuneration (including another concealed source of emoluments) of £41,000 was established (see paragraphs 9.2. and 9.7 page 674). Omitted remuneration from earlier and later years was *marked down* or *marked up.* (see paragraph 9.2 page 674). How this was done is not disclosed in the report; the resulting figures were all round sums.

108.It is easy to see how a pattern of concealment can be identified from this type of detailed examination of the operations of the restaurant, and applied realistically to earlier and later years. This occurs in VAT *mark up* cases, where patterns of suppression are identified from observation and examination of the trader's (often a restaurant business) records. The capital statements approach normally involves an examination of several individual years before the presumption of continuity can be contemplated, as in *Jonas.* Even in *Khawaja* the application of the base year figure was held to be erroneous, and on appeal, Lawrence Collins J made a broad axe deduction (paragraphs 27 and 28 page 680), the basis of which is again not disclosed in the report. While an estimate is permissible, and often is the only way of proceeding, even an estimate has to be based on some evidence. Here, for the earlier and later years, that evidence is lacking.

109.As we have already noted, the assessments for the tax years 2004/2005 and 2005/2006 are based upon turnover of £93,839 (£45,227+£48,612) and £92,094 (£42,239+£49,855) respectively. Given, the nature of the Appellant's business, his health and *modus vivendi* during those tax years, and the smaller size of the premises (compared with later years), we consider on a balance of probabilities that these assessments must be wholly unrealistic. However, we have no evidence either as to what transpired during these tax years in terms of turnover, other than the declared sales, or from which what actually transpired may be inferred, to make an appropriate deduction or even a broad estimate. For the earlier years there is no evidence of unaccounted for bankings, expenditure or capital accretions.

110.We recognise that it is our duty to make the best estimate we can in the face of an unsatisfactory evidential position (see *Rouf v HMRC 2009 STC 1307 Extra Division (paragraph 29).* Any attempt on our part to do so here would simply be arbitrary. Normally, a taxpayer shows that he has been overcharged by an assessment by demonstrating, the onus being on him, that a specific lesser figure is appropriate. In this case, we do not consider that the fact that the Appellant did not give evidence makes any difference (cf *Roufat paragraph 31*). The oddity here is that we are satisfied that these assessments must be wrong but we have no material to enable us to substitute another figure. If the application of RPI does not yield the appropriate result for 2007/2008, as the Revenue concede, it cannot be applied in any meaningful way to the earlier years either. We simply cannot form any view as to the extent to which, if at all, the Appellant has under-declared his turnover in these earlier years. This seems to distinguish the collection of cases on this general topic conveniently gathered together in Simon's Taxes (online version) at section A5.136.

Alternative Basis

111.If, on the findings of fact we have made, we should (contrary to our views) have concluded that the Revenue have established that income that ought to have been assessed has not been assessed and that there has been a loss of income tax attributable to the fraudulent or negligent conduct of the Appellant, and we should therefore, on the material before us, have been able to use our best judgment to determine the extent to which the assessments for the tax years 2004/2005, and 2005/2006 should have been reduced, we would have used our assessed turnover of

£60,000 for the Enquiry Year of 2006/2007 as a starting point. However, we would have reduced it to £51,000 for each of the years 2004/2005 and 2005/2006. That reduction in assumed turnover recognises and acknowledges that in those two earlier years, the Appellant's premises were smaller, his health poorer, his time spent on the garage business was probably less, and he may have had fewer employees although this last point is not entirely clear.

112. The reduction of £9,000 (£60,000-£51,000) uses the same broad axe deployed by Lawrence Collins J in *Khawaja*, but it could be said to be a little sharper. It recognises that the declared turnover for those two years was too low but not by much. Having regard to paragraphs 13-15 and 86-88 above, £51,000 seems about right. It proceeds upon a turnover falling between the average of (a) four vehicles a day at about £60 for four days a week for a 50 week year (£48,000 i.e. 4x£60x4x50); this amounts to sixteen vehicles per week, and (b) the same daily throughput but assuming 4.5 days per week (£54,000 i.e. 4x£60x4.5x50); £51,000 represents a throughput of 17 vehicles per week. However, as we have already indicated this seems to us to be more guesswork than the exercise of good, far less best judgment as the calculation assumes an average of £60 per vehicle. However, there is no evidence of what the Appellant's average charges were in the years 2004/2005 or 2005/2006 (see paragraph 95 above).

Summary

113. We are issuing this decision in principle. We have decided in principle that

1 **The Appellant has been overcharged by the assessment relating to the Enquiry Year. The closure notice therefore overcharges the Appellant. The figure for omitted sales in the Takings Build-Up falls to be reduced to £17,223 (£60,000-£42,777). The penalty and interest fall to be reduced accordingly.**

2 **The Appellant has been overcharged by the assessments relating to the tax years 2004/2005, 2005/2006, and 2007/2008. As there is no basis upon which we can substitute another figure for any of the assessments, the assessments must be reduced to nil. The penalties and interest for these years will also be reduced to nil.**

114. We invite parties to intimate to each other and to submit to the Tribunal, within eight weeks of the date of the release of this decision, proposals in writing as to how the Tribunal should finally give effect to this decision in principle. Thereafter, the Tribunal will issue its final decision or if appropriate fix a further Hearing. We encourage the parties to discuss matters and attempt to agree as much as possible in the light of our decision in principle.

115. 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.

J GORDON REID, QC., F.C.I.Arb.,
TRIBUNAL JUDGE

RELEASE DATE: 22 NOVEMBER 2011