TC02806

Appeal number: TC/2012/06976 & TC/2012/06977

Income Tax – Rental Income – properties jointly held – whether income assessable on one spouse – no – no declaration that properties held other than jointly – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

MR DEEPAK KOSHAL **Appellants**
MRS MINU KOSHAL

- and -

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

TRIBUNAL: JUDGE DR KAMEEL KHAN
JANET WILKINS, CTA, TEP

Sitting at Bedford Square, London on 9 May 2013.

Mr Brian Gibbor, Accountant, for the Appellant

Gloria Orimoloye, Higher Officer, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. The main issue for determination is whether where property is jointly owned by a husband and wife, the rented income should be wholly assessable on one party or should it be assessed equally between the parties. The matter concerns Discovery Assessments for 2000/01 to 2004/05 inclusive, and for 2006/07; Closure Notices for 2007/08 and penalty determination sought under s.95 Taxes Management Act ("TMA") 1970 for the period 2000/01 to 2007/08.

2. The Discovery Assessments were based on estimated figures of rental profit. The assessments were issued on 10 February 2009 and 4 February 2010. The Appellant later submitted actual figures on assessable profits.

3. The Closure Notices for 2007/08 was issued on 4 August 2011 and based on 50% of the actual figures of rental profit provided by the Appellant.

4. The Respondents amended the Discovery Assessments on 11 August in line with 50% of the actual rental figures provided.

Background facts

(1) On 21 August 2008 Her Majesty's Revenue & Customs ("the Commissioners") wrote to Mr D Koshal to make enquiries about income from land and property which should have been declared on his tax returns in 2005 and 2006. Mr D Koshal replied on 15 September stating that "with effect from 6 April 2004 all land and property matters were transferred to my wife and she will be reporting with regard to income and expenses in respect of these under separate cover".

(2) After some further correspondence between the parties and on 10 February 2009 a notice of assessment for the year 2004/2005 was issued to Mr D Koshal in the sum of £2,000. An assessment was also issued for the year 2006/07 for the sum of £4.000.

(3) On 16 February 2009 Mr D Koshal wrote to appeal the assessment on the ground that the rental income estimate was incorrect and "all the rental income belongs to Mrs M Koshal".

(4) On 30 September 2009 in writing to the Commissioners the Appellant stated:

> "Up to the year ending 5 April 2004 all income from properties were returned on my Tax Return. However because of my practice interest and the demand on my time, all the properties were handled by my wife. All income relating to the properties were apportioned to my wife who set up a bank account in her own name for the express purpose of dealing with these properties. I would, however, point out that the account was opened earlier but for the sake of convenience, the income up to 2004 was returned on my Tax Returns."

(5) On 28 January 2010 the Commissioners wrote to the Appellants explaining that if "the properties are held in joint names the profits are to be treated as arising to you and your wife in equal shares in accordance with the guidance at PIM 1030".

(6) On 14 June 2010, Mr D Koshal explained that the properties were managed by his wife and his only interest was "limited to the capital growth" which he intended to share with his wife. All income from the properties is banked in an account in the name of his wife and bills are also paid by her. He went on to explain the following:

> "My wife attends to dealings with managing agents, tenants, attends to repairs and maintenance. She consults with property managing companies and negotiates rent and refurbishment issues as appropriate. She deals with all correspondence. She maintains a list of suppliers, repairs and maintenance contractors. She negotiates with them, and visits the properties as and when required, often in the evenings/ weekends."

(7) On 21 July 2010, the Commissioners stated:

> "Although I have reviewed the further information concerning your wife's involvement with the rented properties, the legislation at s.836 ITA 2007 as explained in PIM 1030 applies. This legislation explains that where assets are held jointly, a married couple are treated as sharing the beneficial interests in the property equally. As each are beneficially entitled to the property equally, they are also equally entitled to the income and therefore jointly assessable."

(8) In his reply on 27 September 2010, the Appellant drew reference to the case of *King v. King* and *King v. Baker* [2004] SSCD 186 where only one party was assessable on income in a cohabited relationship.

(9) On 19 September 2011, the Commissioners wrote to the Appellant stating:

> "As it is considered that half of the rental income from jointly owned properties should have been included on your Tax Returns from 2001 onwards, a penalty is chargeable in accordance to s.95 TMA 1970 as there was a failure to notify this income and Schedule 7 TMA 1970 applies. Usually a contract settlement would be negotiated to include a penalty but as you cannot agree the position I intend to issue a formal penalty determination.
>
> The maximum penalty chargeable would be 100% of the duties lost of £4,697. However, this is reduced by abatement for disclosure, co-operation and seriousness. The maximum abatement for disclosure is 20% and I consider 10% abatement is appropriate as there was no voluntary disclosure and details of the rental income were only provided on request. Co-operation has a maximum abatement of 40% and 30% has been allowed as although the information has been provided there has been some delay. The maximum abatement of 40% for seriousness has been reduced to 30% in view of the large amount of income.

> The total abatements amount to 70% and the net penalty of 30% is applicable. The penalty chargeable on additional tax of £4,697 at 30% is £1,409."

(10) The total settlement amount was £4,697.99 for tax; £2,670 for interest and £1,409 for penalty amounting to £8,750 for Mrs M Koshal.

(11) The total settlement figure for Mr D Koshal was £25,242 for tax; £7,960 for interest and £7,572 as a penalty making a total of £40,750.

(12) On 12 June 2012 a review was undertaken in accordance with s.49 TMA 1970. The review concluded that income from property held jointly by married couples and civil partners are treated as beneficially owned by the individuals in equal shares under ITA 2007 s.836. Consequently, the Appellants are taxable on income on a 50:50 basis. This rule applies even if the individuals own the property in unequal shares. It was pointed out that there were no signed declarations (Form 17) stating beneficial interest was held in any other way.

(13) It was accepted in the review letter that the assessments issued for 2001, 2002 and 2003 were amended. The tax due for 2001 was nil, 2002 was £348.38 and for 2003 was £745.71.

(14) For the years ending 2004, 2005, 2006 and 2007 it was pointed out that though appeals were made, the tax for 2004 was capped, 2005 was not capped and 2006 and 2007 were capped. For the year ending 2008 the tax due was £89.40.

(15) In total therefore the tax liability sought by the Commissioners was £1,010.40 which comprised £89.40 for 2007/8 and £921 for 2008/9.

(16) The Commissioners relied in particular on the statement made by the Appellant on 19 March 2010 when he stated that both he and his wife took the view that property investment was the manner in which they wished to invest surplus funds. Further on 14 June 2010 they declared that the interest of Mr D Koshal was in the capital growth of the properties. From these two remarks, the Commissioners concluded that there was a joint venture and there was no intention for Mr D Koshal to surrender or alter the beneficial ownership of the properties which he held in equal shares to him and his wife. There was no declaration of trust.

Legislation

(1) For the years up to and including 2006/7 the relevant legislation is found at s.282A and B Income and Corporation Taxes Act 1988.

(2) This was superseded by ss.836 and 837 Income Taxes Act ITA 2007 which apply from the years 2007/8 onwards.

(3) Sections 28 and 29 TMA 1970 which deals with the closure of enquiries and Discovery Assessments.

(4) Section 95 TMA 1970 (penalties).

(5) Section 7 TMA 1970.

(6) Section 50(6) TMA 1970 which places the burden of proof on the Appellant to show evidence of being overcharged by the assessment or amendment.

Tax Manuals

(1) HMRC Manual CG 22020

(2) PIM 1030

Case Law

(1) *Kings v. King* and *Kings v. Baker* [2004] SSCD 186

(2) *HMRC v. Charlton Corfield & Another* [2012] UKFTT 770.

Findings of Fact

(1) The properties in question were jointly owned by the Appellants.

(2) There was no agreement between the parties which explained the ownership of the property portfolio.

(3) The properties were purchased in joint names so as to use the income from Mr D Koshal arising from his accountancy practice to obtain bank loans to purchase the properties. The purchase price was met by a combination of personal savings and bank loans.

(4) Mrs M Koshal dealt with the day-to-day running of the property portfolio and rental business. In addition to the portfolio properties, Mr D Koshal owned a property with a third party which he transferred to his wife around 2000.

(5) The initial income from the property appeared on the Tax Return of Mr D Koshal but after 2004 the total income was declared on the Tax Return of Mrs M Koshal.

Appellant's submissions

5. From the Appellant's statement of case the following points have been made:

(1) They have provided documentary and other evidence to illustrate that Mrs M Koshal undertook all work in relation to the investment properties and consequently was entitled to the income. Mr Koshal was not entitled to any income and his Tax Returns were complete and correct.

(2) The Appellants contend that under s.836 ITA 2007, a declaration of unequal split is not necessarily required.

(3) No declaration is required under PIM 1030 and HMRC Manual CG 22020.

(4) They refute the Commissioners' evidence that the properties are not owned in unequal shares or that on disposal the sale proceeds of the property would be allocated into unequal shares. The Appellants say that the split of the potential profit on the disposal of the properties in the property portfolio is irrelevant in determining the allocation of income.

(5) Mrs M Koshal undertook all the work in relation to the properties and maintenance and on that basis would have been entitled to a larger share of the income. The parties agreed that Mrs M Koshal would be entitled to all the income.

(6) The case of *Kings v. Barker* establishes a principle that profits can be shared other than on a 50:50 basis between cohabiting couples.

(7) Mr Koshal was not involved with the running or management of the properties in the property portfolio and therefore was not required to account for a share of the rental profit on his Tax Returns between 2000 to 2008.

(8) Mr D Koshal by not including rental income on his Tax Return had effectively advised HMRC that his rental income had ceased. The Commissioners should have been aware of this especially as there was no capital gains declaration. There is no overriding requirement for Mr Koshal to explain the changes in the profit shares in accordance with the case of *HMRC v. Charlton Corfield & Another* [2012].

(9) There should be no additional tax or penalties payable by the Appellant.

(10) In the circumstances the Appellant believes that he was not chargeable to any of the rental profits in the period 2000 to 2008 and this was reflected in his Tax Returns for that period. The Appellant asked the Tribunal to confirm that no disclosures were required in Mr Koshal's Tax Returns and said that the appeal should be allowed.

Respondents' Submission

6. The Commissioners say that Mrs M Koshal is only assessed on 50% of the profit from the rental properties, which are jointly owned with her husband. Where husband and wife jointly own properties, s.836 ITA 2007 states that the properties are held on a joint tenancy with each of them beneficially entitled to the property in equal shares. There is no evidence that this is not the case,

7. That fact that Mrs Koshal undertakes administrative duties and manages the property portfolio is not a relevant consideration in determining how the rental income should be assessed.

8. The Commissioners say that the case of *Kings v. Barker* is not a relevant case since the circumstances are different and it relates to cohabiting couples. The relevant legislation is s.282A ICTA and s.836 ITA.

9. A penalty should be charged since there was a failure to notify the Commissioners of income. The penalty has been reduced to 20% of the tax due which amounts to £940.

10. The Appellants have provided no evidence stating that the beneficial interest in the property is held other than on a 50:50 basis.

11. Accordingly, the Appellants have not discharged the onus of proof which was placed upon them or established their case on a balance of probabilities.

12. In the circumstances the Commissioners have asked the Tribunal to confirm the figures determined and to dismiss the appeal in its entirety.

Discussion

13. The properties in the portfolio, numbering 20, were purchased in the joint names of the two Appellants and funded by personal savings and bank loans. Mr D Koshal ran an accountancy practice and had income from that business and his wife had no job or income other than from the properties. Bank financing was therefore arranged through a joint mortgage since it was difficult to obtain a mortgage in the sole name of Mrs Koshal. It seems that the intention of the parties is that while the property was jointly owned the rental income would arise to the wife who was a lower rate taxpayer

14. The relevant provision dealing with jointly held property is found in s.836 ITA 2007 (previously s.282A ICTA 1988). These sections provide that where a husband and wife are living together they would be assessed on the income from jointly held property on a 50:50 basis. If the couple held the property or the income other than in equal shares they had the option to make a declaration of their beneficial interest in a specified asset and to have the income arising from that asset assessed in accordance with the respective proportions. The provision relating to the declaration is s.837 ITA 2007. The election is made on a Form 17 – declaration of beneficial interest in joint property and income – and cannot be backdated. It must be submitted to the Commissioners within 60 days of being made.

15. This position is reflected in HMRC's Property Income Manual (PIM 1030) where it is stated:

> "Where there is no partnership, the share of any profit or loss arising from jointly owned property will normally be the same as the share owned in the property being let. But joint owners can agree a different division of profits and losses and so occasionally the share of the profits or losses will be different from the share in the property. The share for tax purposes must be the same as the share actually agreed."

16. The Tribunal has seen no evidence of a declaration showing an unequal beneficial interest in the property.

17. The Appellants say that Mrs Koshal undertakes all administrative duties with regard to the managing of the rental properties and the rental income is paid into her bank account. The Tribunal finds that this is not evidence to rebut the 50:50 ownership of the jointly held properties.

18. In this case the parties did not complete a Form 17 which would provide evidence of the beneficial ownership of the properties being divided other than equally between the couple.

19. HMRC states the following in the Capital Gains Manual (CG 22020) with regard to the Form 17 declaration:

> "If such a declaration has been made you should treat it as evidence of the existence of an express agreement concerning the ownership of the assets and you should follow that split in assessing the gains on disposal of the asset."

20. The Appellant submits that the Capital Gains Manual recognises that an asset can be beneficially owned in different proportions. They also say that a couple cannot make a declaration where the split of ownership and income differ. This is not quite the position. The position is that the parties can make a declaration with regard to the beneficial ownership of an asset and the income. The declaration would be evidence of the split between the parties. In the absence of any factual evidence which determines the beneficial ownership, where there is joint legal title, a 50:50 ownership basis will apply towards income and capital gains.

21. The Appellant also say that making a declaration is not compulsory. It is correct to say that the parties are not obliged to make a declaration. A declaration need only be made on Form 17 where a couple hold an asset other than in equal shares and wish to have the income and gain assessed in accordance with the underlying ownership rather than a 50:50 split. The declaration would be a record of the beneficial entitlement of the spouses and would constitute a claim to have the income assessed in line with the declared underlying ownership. In the absence of such factual evidence to determine the beneficial ownership the Commissioners will apply the 50:50 Rule where property is jointly owned.

22. There are two further points. The first point relates to the case of *Kings v. King* [2004]. In this case Mr and Mrs King owned their home jointly but decided to move out and live elsewhere and to let the property given that they were experiencing financial difficulties. Mr King received all of the rental income in his own name which was paid into his personal bank account. The Tenancy Agreement was also in his name. The Special Commissioner said that Mrs King had signed over her rights to the rent and her partner should be taxed on the whole profit. Her partner was a higher rate taxpayer thus making the rental income liable to significantly more taxation. The Commissioner seemed to have based his decision on the fact that the person liable to tax is the person receiving or entitled to the profits. The Appellants relied on this case to make a similar submission – that Mrs Koshal had received all the rent and she should be taxed on those sums. It seems the reasoning has its origins in the fact that HMRC can collect tax from a person receiving the profits but it does not mean that it

is that person's income. However, the *King v. King* case can be distinguished on the grounds that the circumstances are different in that the parties were unmarried. In our matter, the parties are married and living together and their situation is governed by statutory provisions. Those statutory provisions do not apply to unmarried couples. The provision is clear that there is a presumption that income arising from property held in the joint names of a husband and wife shall, for the purposes of income tax, be treated as income to which they are beneficially entitled to in equal shares.

23. The second point made by the Appellant is in relation to the case of *HMRC v. Charlton, Corfield & Another* [2010]. The Appellants say that a reasonable officer should have picked up on the fact that Mr Koshal was not making disclosures of rental income nor on capital gains disposal and the officer should therefore have asked for an explanation and in the circumstances there can be no discovery assessment. The Commissioners are entitled to raise an assessment outside of the enquiry window if they discover an assessment to tax is insufficient. This has to be balanced against the taxpayer's entitlement to finality of their self-assessment return. In the *Charlton* case the Court looked at the reasonable awareness of an inspector where disclosures had been made. If appropriate disclosures had been made then it is expected that an officer would make appropriate enquiries and if they failed to do so then there could be no discovery assessment. In our case, there was not a disclosure of information and it was not reasonable to infer, based on the information provided in the Return, that the income arising on the jointly held property should be split otherwise than on a 50:50 basis. In the Tribunal's view, the taxpayer or their professional advisors should have laid out very clearly the details of the property ownership and the fact that the ownership structure had changed. This would have required supporting documentation to be provided to the Commissioners and there was no such supporting documentation to be provided. In the circumstances, it cannot therefore be said that because the taxpayer stopped declaring rental income the officer could have inferred that the rental income was now all to be charged in his wife's name. That is too high a burden to be placed on Revenue Officers. It must be remembered, that it is the obligation of the taxpayer to make full disclosure under the self-assessment system.

24. In the circumstances, the Tribunal has concluded that the rental income is to be jointly assessed on both Appellants. Mr Koshal was chargeable on his share of the rental profits in the periods 2000/01 to 2007/08 and failed to reflect this on his Tax Return for that period. He had not taken reasonable care in the compilation of his Returns and the abated penalty of 20% was reasonably arrived at.

25. The Tribunal was presented with no evidence to show that the parties intended there to be a split in both income and capital which was otherwise than 50:50 and to that extent has failed to discharge the burden of proof. It is not sufficient to say that Mrs Koshal ran the administration of the property rental business and paid all monies into her account. It would have required an irrevocable declaration jointly made on Form 17 which identified the source or sources of income to which it applied and the split in the underlying capital interest to have been filed with the Commissioners. This was not done. This would have allowed the income covered by the declaration to be allocated on a new basis which is to say other than jointly held.

26. In the circumstances the appeal is therefore dismissed.

27. 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.

DR K KHAN
TRIBUNAL JUDGE

RELEASE DATE: 26 July 2013