TC07710

Income tax – failure to declare income – discovery assessments made on the basis of deliberate behaviour – held not deliberate but careless – assessments made to best judgment and not displaced by appellants evidence – penalties assessed for fraudulent/deliberate inaccuracies – held not fraudulent/deliberate but negligent/careless – penalties reduced accordingly

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal numbers: TC/2017/08716
TC/2017/08720

BETWEEN

PALMINDER SINGH SANGHERA **Appellant**

- and -

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

NIRMAL KAUR SANGHERA **Appellant**

- and -

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

TRIBUNAL: JUDGE NIGEL POPPLEWELL
MR JULIAN SIMS

Sitting in public at Cardiff on 15 January 2020 with further submissions from the parties received in February 2020

Mr Martin Arthur for the Appellants

Mrs Corrine Buffong, Officer of HM Revenue & Customs, for the Respondents

DECISION

INTRODUCTION

1. This is an income tax case. The respondents (or "**HMRC**") submit that the appellants have under declared their income for the tax years ending 1998-2013 inclusive.

2. HMRC opened enquiries into the appellants tax returns for the tax year 2012-2013 which they then closed by issuing closure notices to the appellants (the "**closure notices**"). For this tax year they adjusted the appellants returns claiming that the first appellant owed additional income tax of £2,938, and the second appellant £2,411.60.

3. They have assessed both appellants under section 29 Taxes Management Act 1970 ("**TMA 1970**") for the tax years ended 1998-2012 (the "**assessments**"). They have assessed the first appellant to additional income tax of £26,244.56 for these years, and have assessed the second appellant to additional income tax of £9,709.19 for these years. These assessments are based on deliberate behaviour by each appellant.

4. They have also assessed the appellants to penalties (the "**penalties**"). For the tax years ending 1998-2008, those penalties have been determined under section 95 TMA 1970. For the first appellant these penalties amount to £5,244.82, and for the second appellant, £2,844.91. For the tax years ending 2009-2013, the penalties have been assessed under Schedule 24 Finance Act 2007 ("**Schedule 24**"). For the first appellant, these penalties amount to £10,803.78, and for the second appellant, £3,991.18.

5. The appellants have appealed against the conclusion in the closure notices, the assessments and the penalties.

6. The main issues in these appeals concern:

   (1) Firstly whether the method used by HMRC to compute the amount of tax set out in the assessments was a fair one (and so the assessments were prima facie valid) and if so, whether the appellants have provided satisfactory evidence to displace those assessments.

   (2) Secondly whether the appellants behaviour was fraudulent/deliberate (and so whether firstly, HMRC could issue the assessments for all the years, or just up to and including the tax year ending 2007, and secondly the basis on which the penalties have been assessed).

7. For the reasons given later in this decision, we have found that; the method used by HMRC to compute the amount of tax in the assessments was a fair one; the appellants have failed to provide satisfactory evidence to displace the amounts set out in those assessments; the appellants behaviour has not been fraudulent/deliberate but has been negligent/careless.

THE LAW

8. There was no dispute about the law (save as set out at [82] relating to HMRC's apportionment of the additional income between the two appellants). We therefore set out a brief summary of the relevant law below.

The closure notices

9. Under section 29A TMA 1970, where HMRC have opened an enquiry into a taxpayer's return, that enquiry is completed when HMRC gives the taxpayer a closure notice. A closure notice must state the Officer's conclusions and make amendments to the taxpayer's return to give effect to those conclusions. A taxpayer has a right of appeal against the amendments to his return.

The assessments

10. Under section 29 TMA1970 where an HMRC Officer discovers an insufficiency in the amount of tax assessed on a taxpayer, that Officer can issue an assessment to make good that insufficiency. Such assessments are colloquially known as discovery assessments. The ordinary time limit for making a discovery assessment is 4 years after the end of the year of assessment to which it relates. But where a discovery assessment involves a loss of income tax brought about deliberately by a taxpayer, that period is extended to 20 years. Where the loss of income tax is brought about by careless behaviour on the part of the taxpayer, that period is extended to 6 years. A taxpayer has a right of appeal against any discovery assessment. Under section 50(6) TMA 1970 an assessment shall stand good unless, on an appeal, the tribunal decides that the taxpayer has been overcharged by an assessment or a self-assessment.

Section 95 penalties

11. Under section 95 TMA 1970, where a taxpayer fraudulently or negligently submits an incorrect tax return to HMRC then an HMRC Officer may make a determination imposing a penalty under that section and notify the taxpayer of the determination. A taxpayer has a right of appeal against any such determination. HMRC has power to mitigate a penalty.

Schedule 24 penalties

12. Under Schedule 24, HMRC may assess a taxpayer for a penalty if a tax return contains a deliberate or careless inaccuracy. HMRC have power to reduce a penalty if there are special circumstances. A taxpayer has a right of appeal against any penalty assessment. On such an appeal the tribunal may affirm HMRC's decision or substitute for it another decision that HMRC had the power to make.

THE EVIDENCE AND FINDINGS OF FACT

13. We were provided with a bundle of documents prepared by HMRC which contained the documents for the hearing. We had also been served with a witness statement made by Officer Michael Adu-Boahen who gave oral evidence on behalf of HMRC. On 8 January 2020 (so a week before the hearing) Mr Arthur sent an email to HMRC and to the tribunal which attached a document which he asked to be regarded as a "skeleton argument and witness statement". It comprises a statement by the first appellant which sets out his view of the history of works done to, and occupation of, the relevant properties.

14. There have been two sets of directions dealing with the disclosure of witness statements and reliance on oral evidence, the first of which was dated 14 March 2018 and the second of which was dated 24 November 2018. The appellants complied with neither direction and so, in a letter of 21 June 2019 to the appellants, the tribunal told the appellants that they would not be able to give evidence at the appeal or call any other witnesses to give evidence without the permission of the hearing judge.

15. Unsurprisingly, in light of this, HMRC opposed the introduction of the first appellants witness statement and his right to give oral evidence along the lines of that statement. So the first thing we had to decide was a preliminary application by the appellants to allow the first appellant to give oral evidence along the lines of his witness statement.

16. We considered the position at the hearing following representations by both parties and concluded that the appellants were not entitled to adduce any oral evidence, including that of the first appellant, in these proceedings. We explained the reasons for our decision at the time, and told the parties that we would set out these reasons in this decision.

The preliminary application

17. Mr Arthur explained that failure to comply with the directions reflected no intention, nor any deliberate endeavour to avoid progress of the appeal. It was a simple mistake. It was his view that this mess had been caused by a combination of factors namely; that the appellants previous accountant who had been involved in this enquiry, dying in July 2017, something of which his firm was not made aware of until late in the day; although correspondence had been sent to the appellants, who did not respond to them, this was because of their distressed state of mind; Mr Arthur had been recruited to help out in this matter but the firm for whom he worked had ceased to trade in 2018 and this resulted in a number of disgruntled employees who, Mr Arthur thought, did not pass on the information about the appeal, to him (he was intending to carry on working for a select number of clients, including the appellants following the demise of his firm) until the deadlines had passed; Mr Arthur has been very unwell recently and unable to fully attend to the issues in this case; he had asked HMRC for documents so that he could review the case but initially received only correspondence. He eventually received a bundle of documents two weeks before the hearing and it was following disclosure of that bundle that he submitted the first appellants skeleton argument and witness statement. He submitted that we should give the appellants permission to introduce the skeleton argument and witness statement into the proceedings and allow the first appellant to give oral evidence.

18. Mrs Buffong opposed this application. The appeal has been on foot for a considerable time and Mr Arthur's firm, in the guise of Debono & Hamilton Forensic Accountants Ltd, had been involved since at least 2017 (she pointed out that HMRC first wrote to that company on 11 April 2017). This predated, by some considerable time, the two directions mentioned above. Furthermore in a letter dated 25 June 2018 to that firm, HMRC clearly referred to the first set of directions, and a copy of that letter was sent to the appellants (it is not clear to us whether this was sent to the appellants in person or to Mr Arthur) in 2019. Any correspondence sent to the appellants could have been readily passed on to their adviser. This was not a difficult thing to do. And it was open to Mr Arthur at any stage after he was instructed to have asked the appellants about the state of the case and to ask them to pass on to him any correspondence which they had received from either HMRC or the tribunal. It is his client's responsibility to comply with the directions of which they were fully aware. It is very late in the date to serve witness statement. There is no good reason for failure to comply with the directions. She recognised that if the first appellant was not permitted to give oral evidence, she could not cross examine him, and this might have an implication in respect of HMRC's allegation of deliberate conduct. But this, notwithstanding, she opposed the application.

19. We applied the threefold test set out in the Upper Tribunal decisions of *Martland* and *Katib*. This requires us to consider firstly the length of the delay and its seriousness and significance. In the context of a failure to comply with a direction, the serious and significance of that failure is the important issue rather than the length of the delay. Secondly we must

consider the reasons for that failure, and finally we need to undertake an evaluation of all the circumstances having regard to the particular importance that statutory time limits should be respected, as should directions given by the tribunal.

20. In our view the failure to comply with the directions is both serious and significant. Both sets of directions make it expressly clear that the appellants must provide witness statements from witnesses on whose evidence they intend to rely at the hearing. Furthermore the letter of 25 June 2018 sent to the appellants agent specifically points out that they have failed to comply. This should have put them on notice that the tribunal considered failure to comply was significant, and caused them, once they received the second directions, to attend to their obligations thereunder, with greater diligence. The appellants failure to comply with these directions is serious and significant.

21. We now turn to the reasons given for this failure which, in essence, boil down to a failure by the appellants agent. It is clear to us that although Mr Arthur said that his firm was instructed late in the day, it has in fact been involved since April 2017 and is identified as the appellants authorised representative in their notices of appeal dated 10 November 2017. We appreciate the operational and health difficulties put forward by Mr Arthur as justification for his failure to assist the appellants to comply with their obligations under the directions. But, as is set out in *Katib*, a decision which binds us, given the importance adhering to statutory time limits, and compliance with directions given by a tribunal, failures by a taxpayer's adviser are generally treated as failures by the taxpayer. The failure by an adviser to advise an appellant about time limits or to comply with directions is unlikely to amount to a good reason for failing to comply. But the adviser's failures are something which can be taken into account at the third stage of the process when we come to evaluate all of the circumstances.

22. We now turn to that evaluation. When doing so we remind ourselves that compliance with directions should be respected and failure to do so should be regarded as the exception rather than the rule. We can consider at this stage the prejudice which might be caused to the appellants by not permitting the first appellant to give oral evidence. But this must be weighed up against the prejudice caused to the respondents by allowing this information to be adduced at this late stage. We can see that there is prejudice to the appellants since his statement deals with the use to which the rental properties were put, and is relevant to the issue as to whether the "read back" of the additional percentage by which HMRC have uplifted the taxable income for the year of enquiry, into previous years under the principle of the presumption of continuity, is justified since the properties are not the same for previous years as in the year of enquiry. But some of this evidence is before the tribunal since it was given by the first appellant at the meeting with HMRC on 8 April 2015. It was also provided in a document sent by the appellants previous advisers to HMRC on 30 December 2015. And it is clear from the correspondence that HMRC have taken into account these representations when coming to their final view of the matter. We would finally observe that if we allow this application, there is prejudice to the respondents, not in the form of ambush, but because they will not be allowed to cross examine the first appellant. This is something that Mrs Buffong has recognised is a consequence of her opposition. So the rejection of the appellants application may have an unintended benefit to them.

23. Drawing all these threads together, our evaluation of the circumstances of this application leads us to reject it. The failure to comply with the directions is serious and significant. No good reason has been given as to why there was this failure. Failure by the appellants agent is treated as failure by the appellants. Given that the information in the witness statement was readily available in written form as long ago as December 2015, it would not have been difficult

for this to have been formalised as a witness statement and submitted in response to the directions. The balance of prejudice does not favour granting the application, and it is rejected.

The evidence and findings of fact

24. We divide this section into three. Firstly the uncontroversial chronology. Secondly the evidence and findings in connection with the assessments. And finally the evidence and findings in connection with the penalties.

25. As set out above, Officer Adu-Boahan had tendered a witness statement and gave oral evidence. He had not made such a witness statement in time to comply with the directions mentioned above. His statement is dated 26 November 2019. However the purpose of this statement is to adopt the witness statement of the HMRC Officer who was largely responsible for issuing the assessments and the penalty notices, Officer Grace Knights, and her witness statement, dated 17 May 2018 complied with directions. Mr Arthur took no point that the respondents were in breach of the directions, and the findings we make below are based on the witness statement of Officer Knights as adopted by Officer Adu-Bohan.

Chronology

26. HMRC opened enquiries into each of the appellants tax returns for 2012-2013 on 12 December 2014. For this tax year, the first appellant had income from his self-employment as a mini cab driver and from property. The second appellant had income arising from property. Both declared profits from those activities in that tax year. As part of the enquiry, HMRC asked for information and documents which were not supplied by the deadline they had suggested. Accordingly, information notices were served and a partial response to those was received by HMRC in February 2015. That information did not however include records of rental income received from the properties. Following communications with the appellants agent, in February and March 2015, a meeting was scheduled for 8 April 2015. That meeting took place (the "**April 2015 meeting**") and the notes of meeting are dealt with in more detail below (the "**meeting notes**").

27. The meeting notes were sent to the appellants agent later in April 2015 along with a request for further information and a statement of assets and liabilities. The information requested was not forthcoming voluntarily and so a notice to provide the information and documents were sent to the appellants in July 2015. Following receipt of that information, the Officer carried out a review and sent the appellants a revised computation of their liabilities on 29 October 2015.

28. There then followed further correspondence between that Officer and the appellants agent in which that agent indicated their disagreement with the revised computation, told the Officer that they would provide reasons for this along with supporting documents by 15 December 2015, and subsequently provided "documentary evidence" which they said suggests why the Officers computations were incorrect, on 30 December 2015. One of the documents supplied comprised a note from the appellants to the enquiry Officer setting out the use to which the properties had been put and the changes that had been made to them and their history of occupation since they were acquired.

29. A further meeting between HMRC and the taxpayers and their agent took place on 19 April 2016 and following that meeting bank statements were received from the appellants by HMRC on 20 May 2016. Further records were requested by HMRC in June 2016 which were received by HMRC at the end of August 2016. Following receipt of those bank statements and

records, Officer Knights wrote to the appellants on 27 September 2016. In that letter she summarised her view of the rental receipts for the properties for the year under enquiry and her figures showed £65,016.84 more than the declared rent in that year. She corroborated this by evidence from the bank accounts which suggested that more money had been paid into them than the income that had been declared. She also dealt with capital allowances and mini cab income.

30. A substantive response to this letter was sent by the appellants agent on 23 November 2016 to which Officer Knight responded on 7 December 2016. She also requested further information which was received from the appellants in January 2017 resulted in Officer Knights letter to the appellants and their agent on 7 February 2017 setting out a means calculation which is based on the bank account details and the business and private expenses of the appellants. It also included her calculations of the penalties and interest for which in her view the appellants were liable. She included with that letter penalty explanations and schedules. In response to this, the appellants agent sent her a schedule which they said indicated that Officer Knights had double counted some of the expenses. She responded to the agent on 24 March 2017 with revised calculations. She had been told in an earlier letter that the appellants had instructed a new agent (Debono and Hamilton), and started to communicate with them. She supplied information as requested by them and following a lack of response, raised formal assessments on 1 June 2017 and issued the closure notices, on that date, together with assessments for additional revenue for the years 1998-2012 and associated penalty assessments.

31. The appellants agent appealed against the penalty assessments to HMRC on 29 June 2017. It was not clear to HMRC whether this was an appeal against only the penalties or against both the penalties and the tax assessments. Officer Knights issued her view of the matter letter regarding the penalties on 5 July 2017. On 28 July 2017 the taxpayer's agents asked that their letter of 29 June 2017 should be treated as an appeal against the tax assessments as well as the penalty assessments since they had made a typing error. Although this was, strictly speaking, a late appeal, it was accepted by HMRC and Officer Knights issued her view of the matter letter regarding the tax assessments on 3 August 2017. A statutory review was completed on 17 October 2017 which upheld Officer Knights' view of the matter, and the appellants notified their appeals to the tribunal on 10 November 2017.

The assessments and closure notices

32. In his letter to the appellants agent dated 29 October 2015, the HMRC Officer who at that stage was dealing with the enquiry noted that there was a discrepancy between the bank account deposits and declared income from the minicab business and from the property business, in that the deposits were greater than the declared income by about £600. He also explained that the appellants properties were inspected by HMRC Officers in December 2014, and in light of their observations, and the appellants explanations concerning vacancies of properties and use of outbuildings, he was not satisfied with those explanations. He explained that he had analysed meter readings from the utilities serving the properties and there seemed to be an inconsistency between those and what he had been told by the appellants. He could accept that loft conversions were started after the end of the year under enquiry. He had considered the tenancy agreements with which he had been provided and some of the rent appeared greater than the amounts included in the appellants tax returns. He then used estimated amount for rental figures for properties where no tenancy agreements had been provided, and enclosed, with that letter, a schedule of rental income, based on his observations of the properties at the inspection in December 2014, the amount of rent due under the tenancy

agreements and other information held by HMRC. He estimated that the additional rental income was approximately £95,000 and he split it between the first appellant and the second appellant on a 70:30 basis. He also dealt with capital allowances in relation to the first appellants minicab activities and enclosed computations based on these estimates.

33. The appellants agents wrote to HMRC on 30 December 2015 enclosing with that letter, a lengthy document signed by the appellants which, as mentioned above, set out details of the operational use of, and changes to the structure of , the properties since their acquisition. It also included planning documents and statements from individuals who had occupied the properties.

34. Under cover of a letter dated 30 June 2016 the appellants agent sent copies of the appellants bank statements to HMRC.

35. In a letter dated 27 September 2016, written by Officer Austin, HMRC updated their position following a "full review of the matter". She confirmed that it was agreed that outbuildings at two of the properties were built in 2012 – 2013 tax year and that no rental income had been received from them during the year of enquiry. She explained that from evidence provided to the previous enquiry Officer, two other properties had been rented out notwithstanding protestations to the contrary from the appellants. For a fourth property she agreed that an outbuilding behind the property had been used as an office and no rent had been received from that.

36. She provided a schedule in which the total rent shown was £65,016.84 more than the declared rent of £111,720. She bolstered this conclusion from evidence derived from bank deposits. In her view the total money paid into the appellants bank accounts was £155,622.29, which amount exceeded total income declared by £9842.29. She also observed that insurance policies for each property showed an amount covered for 12 month rental loss which, in most cases, was more than twice the declared rent received. Finally she analysed the business profits (from both the properties and the minicab business) and observed that there was a deficit of income over expenses of £1,384.39. It was her view that the appellants had accepted that over and above this, personal and private expenditure had been paid in cash and estimated that the cash expenditure was £71,420.60 per year which thus increased the excess of expenses over income.

37. She took the total additional rental income which she believed to have been under declared (namely the £65,016.84) and, in accordance with section 836 Income Tax Act 2007, split that additional rental income between the appellants on a 50:50 basis.

38. She also added back capital allowances which she thought had been over claimed by the first appellant on vehicles which had been used for private purposes, and also added additional minicab income to his return income. With that letter she enclosed revised tax calculations for 2012-2013 based on the figures set out in her letter. She confirmed that these checks confirmed her view that there had been a total underassessment of taxable profit of £24,469.10 by the appellants, that she may need to look at earlier returns under the presumption of continuity, and that she believed that the errors had occurred due to the appellants deliberate actions and requested comments on that issue.

39. On 7 December 2016, following representations from the appellants agent, Officer Austin set out her revised position. In her view the receipts paid into the bank account exceeded declared turnover by £9,842.29, and that the appellants used cash from the taxi property businesses to pay for various business and private expenses indicating there would have been

further income other than that which was paid into their bank account. HMRC had accepted that outbuildings at two of the properties were built during the year of enquiry and no rental income had been received from those premises in the year of enquiry, and that an outbuilding at another property had been used as an office. Outbuildings at two other properties, however, having been built with brick insulated walls and tiled pitched roofs were, in her view, built for the purpose of habitation rather than storage and were likely to have been let out at the earliest possible opportunity generating rent which was received during the year of enquiry. In relation to small rooms in each of the properties, it was HMRC's view that these would have been exploited before the outbuildings were built and would have generated income in 2012-2013.

40. She said that she had not been provided with a clear indication of rental income. She also repeated her expenses analysis set out in her letter of 27 September 2016 and sought a response to further matters regarding expenses. She also dealt with comments made by the appellants agent concerning capital allowances and a 25% private use adjustment.

41. On 7 February 2017, Officer Knights wrote to the appellants agent. With that letter she enclosed a means calculation based on "the actual transactions from the bank accounts and also the business and private cash expenses of your client".

42. She went on to explain her calculation which she said showed that the appellants needed an additional £27,865.07 to meet all of their expenses and it was that figure which would be split 50:50 between the appellants and added to the turnover figures for the year under enquiry. She included tax calculations which indicated that was additional tax due of £3880.38 for the first appellant and £2786.40 for the second appellant.

43. Using the presumption of continuity, she then considered adjusting the profits for the tax years 2011-12 back to 1996-97. She did this by uplifting the declared property "profits" by 80% on the basis that 80% was the amount by which she had increased the profits for the year of enquiry. She split these additional profits on a 50:50 basis and enclosed tax calculations for all of these years with the letter. She also explained that she believed the errors in the returns were due to deliberate actions, assessed penalties under the old penalty rules(s95 TMA 1970) and under Schedule 24 on the basis of a 20% reduction for cooperation and 20% reduction for seriousness (as regards the old rules), and summarised the total additional liabilities. These amounted to £65,855.39 for the first appellant and £29,691.46 for the second appellant.

44. The appellants agent, in their letter to HMRC dated 6 March 2017 enclosed a schedule detailing why, in their view, some of the HMRC numbers had been "double counted". Officer Knights responded to this in her letter of 24 March 2017 which takes into account the representations on those figures by the appellants agent and enclosed with it a revised means calculation showing that the appellants required an additional £24,116.53 to meet all of their expenses and that was the revised figure that she then added to their turnover (which was split, again, on a 50:50 basis). That revised figure meant that the profit uplift for the year of enquiry was not 80% but 70%, and used this revised percentage increase to revise her additions to taxable profit for the years 2011-12 to 1996-97. Revised calculations for these years were also included with that letter.

45. On 3 August 2017, Officer Knights wrote to the appellants new advisers, Debono and Hamilton. This was her view of the matter letter as regards the assessments. Her view of the matter was that: the total deposits paid into the bank account exceeded the turnover declared on the return indicating under declared turnover; a full reconciliation of the property expenses was carried out which married up both with the invoices provided and the transactions reflected

in the bank statements; it was not possible to carry out a full reconciliation of the rental income since there were no clear records. There was only a one-sided handwritten piece of A4 paper available with rental receipts and dates. Only some tenancy agreements had been provided and it was not possible to reconcile income receipts as deposits into the bank were mostly cash with no references; computations were made on the basis of a full cash flow and means test using actual information from the bank statements and figures provided by the appellants in relation to their business and private cash expenditure. Detailed calculations were sent at various times to the appellants agents, but by the time that she had decided to close the enquiry (1 June 2017) the appellants had provided no evidence to show that her figures were incorrect and had not provided alternative figures together with evidence to show what was, in their view, the correct position; the levels of profit for the year of enquiry and in previous years were not excessive and showed that they were required to meet the appellants living expenses. Over and above this, the appellants would have required funds to be able to purchase a number of properties over the years and carry out works to these properties; the errors in the year of enquiry showed property profits were underdeclared by 70% and under the principle of the presumption of continuity she had uplifted the rental income for the previous years by the same percentage. Her view was that nothing had changed since her letter of 24 March 2017 and she confirmed the calculations sent with that letter.

46. A review conclusion letter dated 6 October 2017 was sent to each appellant by Officer Smith, the review Officer, who concluded that HMRC's view of the matter in respect of the assessments, set out in the letter of 3 August 2017 was upheld.

The penalties

47. The possibility of visiting penalties on the appellants was first raised by Officer Austin in her letter dated 27 September 2016. No reasons were given for her comment that she believed that the errors in the tax returns had occurred due to the appellants deliberate actions. In that letter she asked for comments on that allegation from the appellants agent.

48. However, in her letter of 7 February 2017, Officer Knights restated HMRC's belief that the errors were due to the appellants deliberate actions but went further and enclosed, with that letter, penalty explanations together with schedules detailing the penalties.

49. The penalty explanation schedule states that "the total deposits paid into the bank account exceeded the turnover declared on the return. The properties were inspected in December 2014 and the number of tenants and rent shown on the rental agreements did not match the figures. Little or no records were kept in terms of rental income however in comparison the expenditure invoices were all kept and could be reconciled with the bank statement".

50. It goes on to say this:

> "We consider that the behaviour was "deliberate". This is explained below.
>
> > A thorough review of the bank statements was carried out, this involved assessing the level of deposits made into the bank compared to the turnover for both the taxpayer's self-employment and property income and also a means test for private cash expenditure. The deposits and cash expenses greatly exceeded the turnover and there was no explanation as to why. The records relating to income was also very poor, there was only a one sided handwritten piece of A4 paper available with written dates and amounts received and some of the tenancy agreements were provided. This was contrasted to clear records the taxpayer had for expenses,

numerous invoices and paperwork to reconcile the expenses. This shows that the taxpayer did not want to show the true extent of the turnover has the information and documents provided were purposely sparse."

51. The same explanations were given to both appellants.

52. The letter of 24 March 2017 enclosed penalty calculations, based on fraudulent/ deliberate behaviour, under the old penalty rules and Schedule 24. But nothing in that letter provided any further explanation as to why HMRC thought that the appellants behaviour was fraudulent/ deliberate, and the same is true of the letter of 1 June 2017 which closed the enquiry for the 2012-2013 tax year. Officer Knights view of the matter letter relating to the penalties, dated 5 July 2017, doesn't take matters much further either. It simply states that "the behaviour which led to the inaccuracy was deliberate and no comments or defence were received in relation to this behaviour when it was put forward."

53. The review conclusion letter dated 6 October 2017 did not provide much more detail either. It simply indicated agreement with HMRC's position that the inaccuracies in the returns and specifically the under declaration of rent was deliberate. Although the appellants may well have not known what the actual figures of rental income were, the reviewing Officer was "equally persuaded that you knew the tax return entries to be incorrect and less than the full amount received."

Mr Arthur's challenge and findings of fact

54. In cross-examination, Mr Arthur challenged four aspects of HMRC's position. The first concerned the presumption made by HMRC that the outbuildings at two of the properties would have been exploited at the earliest possible opportunity. He also challenged their view that the extra small rooms would have been fully exploited before the outbuildings were built. Obviously the reasonableness of such presumptions is a matter for our consideration, and we consider it below. But he was not able to lead any evidence from the first appellant to support any submission that HMRC's presumption was rebutted by the actual position. Secondly he challenged the basis on which HMRC had split the additional income between the appellants on a 50:50 basis. Thirdly he pointed out that HMRC had not exhibited, in their bundle of documents, the actual bank statements on which they based their conclusion that the appellants income exceeded deposits, and thus the fundamental basis of the assessment was unsustainable. Finally he questioned the extent to which Officer Adu-Bohan had discussed the case with Officer Knights. Notwithstanding these challenges, we find the facts as set out above. Indeed these facts are, in most cases, simply a record of what HMRC said in correspondence to the appellants or their agent, and thus speak for themselves.

Burden and standard of proof

55. The burden of proving that the assessments are valid in time discovery assessments lies with HMRC. If we find that they are, then the burden switches to the appellants to displace those assessments. In each case the standard of proof is the balance of probabilities, or whether it is more likely than not.

56. The burden of proving that the appellants have exhibited fraudulent/deliberate behaviour, which of course is relevant to both the assessments and to the penalties, also lies with HMRC. It is a subjective test. The standard of proof is the balance of probabilities.

57. If we decide that the appellants have not behaved fraudulently/deliberately, then HMRC

have alleged negligent/careless behaviour in respect of the penalties, and it is for the appellants to show that they have not been negligent/careless. The standard of proof is also the balance of probabilities.

58. In the discussion below, and unless the contrary appears, "deliberate" include fraudulent, and "careless" includes negligent.

DISCUSSION

The validity of the closure notices and the assessments

59. We were unable at the hearing to hear closing oral submissions from the parties, since we ran out of time. Accordingly we issued directions that the parties should submit written closing submissions dealing with a number of matters. The respondents responded substantively to those directions and provided a 16 page written closing submission. In response, Mr Arthur set out his criticism of this submission indicating that it was a restatement of HMRC's case; that the taxpayer was unable to address it because of administrative evidential procedures; that it was "dependent on assumptions and hypotheses, along with a focus on unguarded and not properly explained by the taxpayer of the handling of cash funds"; and was a "weak and pathetic pleading".

60. Accordingly it is not possible to be absolutely clear of the basis on which the appellants are challenging the closure notices and the assessments.

61. What is clear however from both the correspondence and HMRC's closing submissions, is the basis for raising the assessments and issuing the closure notices. These are fully set out in the view of the matter letter dated 3 August 2017 (set out above) and summarised in HMRC's closing submissions. The basis was that HMRC undertook a cash flow and means test, which considered all business and private expenses paid from the appellants bank accounts and the expenses that they paid in cash, and identified from that exercise that the appellants requires an additional £24,116.54 to meet their living expenses for the year of enquiry. The basis for the private cash expenses was a personal expenditure form completed and submitted by the appellants and further information regarding expenses set out in the appellants agents letter to HMRC dated 19 January 2017.This letter included a suggestion that travel expenses for both appellants amounted to between £5 and £10 per week which was rejected by HMRC. The private banking expenses were based on actual deposits reflected in the bank account. The business cash expenses were based on the actual paid expenses from self-employment from the first appellants tax return. The figure of £24,116.54 was the figure used not just for the year of enquiry, but also as the basis for the assessments. HMRC took the view that in the year of enquiry, the additional income was 70% more than the income declared by the appellants. They therefore uplifted the income declared by the appellants in previous tax years by that amount. This was expressed to be under the presumption of continuity.

62. Our understanding of the appellants challenge is that HMRC had insufficient information on which to base their assessments and if they did have sufficient information, they did not act fairly since they did not take into account everything that the taxpayers had said about the exploitation of the properties during the year of enquiry and in previous tax years. There was also an element of double counting.

63. When considering whether HMRC have issued a valid closure notice, then the legal test to be applied is very similar to the legal test which is to be applied when considering their position regarding the assessments.

64. With regard to assessments, as Walton J said, in *Johnson v Scott (HM Inspector of Taxes)* (1978) 52 TC 383 at 394, in a passage approved by the Court of Appeal (at 403) in that case:

> "Of course all estimates are unsatisfactory; of course they will always be open to challenge in points of detail; and of course they may well be under-estimates rather than over-estimates as well. But what the Crown has to do in such a situation is, on the known facts, to make reasonable inferences. … The fact that the onus is on the taxpayer to displace the assessment is not intended to give the Crown carte blanche to make wild or extravagant claims. Where an inference of whatever nature falls to be made, one invariably speaks of a 'fair' inference. Where, as is the case in this matter, figures have to be inferred, what has to be made is a 'fair' inference as to what such figures may have been. The figures themselves must be fair."

65. It is our view that a similar position applies to closure notices. We do not think that HMRC needs to be certain that the figures that they have posited are wholly accurate before they issue a closure notice. It is inevitable that, during an enquiry, they may not be provided with sufficient information to enable them to achieve that level of certainty. In our view what is required is that the Officer issuing the closure notice has conducted his or her enquiry to a point where it is reasonable for him or her to make an informed judgment as to the matter in question so that exercising that judgment he or she can state his or her conclusions and make any related amendments to the taxpayer's return.

66. In other words, the Officer issuing the closure notice must act reasonably and fairly on the basis of the information before him or her.

67. And it is our view that both as regards the closure notices and the assessments, the relevant HMRC Officers have acted wholly fairly as regards these taxpayers. Although the appellants agent may disagree with this, it is our view that this is almost a textbook enquiry. This is illustrated by the documentary evidence which we have set out in considerable detail above and is one reason why we have set it out in such detail.

68. As can be seen from the chronology and the documentary evidence, having opened their enquiry HMRC sought information voluntary which was not immediately forthcoming and necessitated the use of a schedule 36 notice. Once that initial information was before them, HMRC convened the April 2015 meeting. The first appellant was given an opportunity to explain his side of the story, and the information provided by the appellants at that meeting, bolstered by information provided by the appellants thereafter, enabled HMRC to come to a view concerning additional rental income. They also came to a tentative view regarding penalties and sought the appellants explanation as to why there was underdeclared income. Following further correspondence between the parties and the provision of additional information by the appellants agent, including, importantly, the appellants bank accounts, HMRC then changed the basis on which they were alleging under declaration of rental income, and ultimately based their assessments, as set out above, on a cash flow and means test exercise.

69. What is clear, however, is that HMRC gave the appellants every opportunity to provide information to displace their original tentative, and subsequent firmer views, an opportunity which the appellants took to a certain degree. The notes of meeting show that the first appellant provided a reasonably comprehensive explanation of the exploitation and changes to the structure of the properties that generated the rental income in question.

70. What is equally clear is that HMRC took this information into account when considering the additional rental income for both the year under enquiry and the years of the assessments.

They did not accept everything that first appellant told them, but there is no obligation on them to do so. At this stage of the process all they have to do is consider the material before them and come to a reasonable and fair conclusion about a taxpayer's liability based on that material. Simply because a taxpayer says something does not mean that HMRC are bound to accept it. They are entitled to test it, and in this case HMRC did precisely that. And when they told the appellants why they had not taken their word, HMRC, very properly, gave their reasons for this.

71. HMRC have clearly considered the information that they were provided with, and evidence of that is not just the testimony of Officer Knights, but can also be clearly seen from the documentary evidence. Following the provision of further information HMRC rejected their original uplift for the year of enquiry which was 80%, and reduced it to 70% which was the figure that he then used to uplift the previous years. This was consistent with their methodology that it was more likely than not that if the appellants had under declared their income by a certain percentage in the year of enquiry, it was likely that they had done so in previous years.

72. The presumption of continuity is just that; a presumption. It can be displaced by evidence to the contrary. In this case HMRC have gone back into previous years and uplifted the appellants declared income by the same percentage as they used in the year of enquiry. This is a rational basis on which to base the assessments and, in our view, fulfils HMRC's obligations to make a fair inference.

73. As we have explained to the appellants, we have not granted them permission to adduce oral evidence in this case. The appellants are not, therefore, able to challenge the basis on which HMRC have dealt with the exploitation of the properties in the assessments. But it is entirely open to them, as has been explained to them by HMRC, to come up with alternative figures for the rental income that they actually received for the year of enquiry and for the previous years. But they have not done this either to HMRC, nor indeed in oral or written evidence or submissions to this tribunal. We deal with this below, but at this stage all we are considering is whether the closure notices and the assessments were validly made in the sense that they were a result of a fair process undertaken by HMRC who came to a reasonable conclusion on the basis of the material which was before them. It is our firm view that they did, and that the closure notices and the assessments are valid.

74. Finally, for completeness, we should mention that in our directions regarding closing submissions, we specifically directed that over and above any other submissions which the appellants agent might wish to make, his closing submissions should deal, in detail, with any challenge which the appellants are making to the basis and methodology of HMRC's assessments to both tax and penalties. As will have become apparent from our foregoing comments, no such detailed challenge was made by the appellants agents in his comments on the respondents closing submissions.

Displacement of the assessments

75. Generally, the burden lies on a taxpayer to establish the correct amount of tax due:

> "The element of guesswork and the almost unavoidable inaccuracy in a properly made best of judgment assessment, as the cases have established, do not serve to displace the validity of the assessments, which are prima facie right and remain right until the taxpayer shows that they are wrong and also shows positively what corrections should be made in order to make the assessments right or more nearly right." (*Bi−Flex Caribbean Ltd v*

Board of Inland Revenue (1990) 63 TC 515, 522−3 PC, per Lord Lowry).

76. This is a consequence of the application of section 50(6) TMA 1970 which essentially obliges us to uphold an assessment unless we decide that the appellants have been overcharged. In order to come to that decision the appellants must show that the assessments are wrong and must make out a positive case. In order for us to come to a conclusion that the amounts in the assessments overcharged them, the appellants need to provide evidence as to what the correct amount is more likely than not to be.

77. Essentially the same applies to displacing the conclusion set out in the closure notices. If the appellants consider that that conclusion is incorrect they are entitled, as they have done, to appeal to both HMRC and then to the tribunal. On an appeal to the tribunal they must show that on the balance of probabilities HMRC's conclusion is incorrect. Again, to do this, they will need to lead a positive case which establishes what the correct amount is more likely to be.

78. We are not absolutely clear of the appellants position regarding the inaccuracies which they believe to be present in the closure notices and the assessments. There has never been a positive case put forward by the appellants as to a different amount of income from that reflected in their tax returns either to ourselves or to HMRC. Their notices of appeal simply state their view that HMRC's decision is estimated and excessive and it appears that HMRC may in fact have double counted some of their calculations. In correspondence, some figures have been supplied by the appellants agent, over and above the primary documentation such as bank statements, and these do appear to have been taken into account by HMRC when reaching their conclusion in the closure notices and thus in the amounts included in the assessments. But there has never been any forensic unpicking of the calculations set out in several of HMRC's letters. We suspect that this is largely because they do not have the records to undertake such a forensic analysis. It it is notable that in response to a direction that the appellants agents should deal, in detail, with any challenge which the appellants wish to make to the basis and methodology of HMRC's assessments, the appellants made no such detailed challenge.

79. It seems, therefore, that the appellants position is that the amounts set out in their tax returns accurately reflect the amounts of income that they received during the year of enquiry. Support for this can be gleaned from the notes of meeting. When asked how the accounts were prepared, the appellants agent said they only prepared a profit and loss account not a balance sheet and that the income was arrived at by asking the first appellant how many rooms there were, the average income per room, and the number of weeks occupancy. The agent also indicated that there were no tenancy agreements and he just had the bills, mortgage statements and bank statements and that he did check that the "bankings tied up with the income". The agent also said that there were no missing bills and the accounts were prepared on a cash basis.

80. Unfortunately for the appellants, there is insufficient evidence on which we can conclude that the amounts set out in those returns was accurate. We have said that the method used by HMRC to arrive at what in their view was additional income for the year of enquiry, was a fair and reasonable method. Throughout the enquiry HMRC provided a number of calculations of the income and expenses which they believed were more likely than not to be correct (compared with those actually supplied by the appellants). The appellants protested against some of these, and, as we have said above, HMRC very fairly took into account some of those protestations but not all. At no stage during the enquiry, or since, have the appellants taken those calculations and provided specific evidence as to why those figures were incorrect. They have simply said that some of the expenditure figures were wrong and that the assumptions

made by HMRC regarding the exploitation of the properties is incorrect. They have put forward no positive case as to what the correct amount of rental income is other than to say that it is as set out in their returns. Indeed the first appellant specifically stated this in the interview when asked whether he wished to change anything in the accounts or in his tax return, and apparently replied that there was not. This answer has not been been seriously challenged by the appellants.

81. And so in the absence of any evidence, let alone cogent evidence, that the figures set out in the closure notices and in the assessments are more likely than not to be incorrect, we conclude that those figures are accurate and that the closure notices and assessments accurately reflect the under declared income for the years in question.

The 50:50 split

82. In his witness statement, Officer Adu-Boahen explained that the reapportionment of the additional income from a 70:30 split as originally reported by the appellants on their returns, to a 50:50 split was based on PIM 1030. Mr Arthur challenged this on the basis that document had no statutory force which is indeed is the case. However there is a statutory basis which underlies both the reapportionment and PIM 1030. This is section 836 Income Tax Act 2007 which provides that where income arises from property held in the names of married individuals who live together, those individuals are treated for income tax purposes as beneficially entitled to the income in equal shares. This statutory reference was set out in HMRC's letter to the appellants dated 27 September 2016. Mr Arthur did not challenge the 50:50 split on the basis it was contrary to that legislation. We therefore find that this reapportionment was reasonable and fair, the appellants have not challenged the fact that it was contrary to the legislation, and so we confirm that the additional income set out in the closure notices and the assessments has been correctly reapportionment on a 50:50 basis.

The appellants behaviour

83. We now turn to the important question of the appellants behaviour. It is HMRC's view that the appellants failure to accurately declare their income for the tax year 2012-2013 is based on deliberate behaviour. They say that the appellants knew that their income was greater than the amount declared and deliberately failed to declare the correct amount on their tax returns.

84. This is relevant to two matters. Firstly the number of years that can be validly assessed by discovery assessments. And secondly the level of penalties, and the broader issues surrounding penalties under Schedule 24.

85. The definition of deliberate behaviour is not defined in the legislation dealing with either the assessments or the penalties, but we have derived help in interpreting the phrase, firstly from the case of *Auxilium Project Management v HMRC* [2016] UKFTT 0249, where Judge Greenbank said as follows:

> "62. Schedule 24 Finance Act 2007 does not further define the word "deliberate". HMRC's manuals state that "a deliberate inaccuracy occurs when a person gives HMRC a document that they know contains an inaccuracy" (HMRC Compliance Handbook CH81150). We adopt a similar approach.
>
> 63. In our view, a deliberate inaccuracy occurs when a taxpayer knowingly provides HMRC with a document that contains an error with the intention that HMRC should rely upon it as an accurate document. This is a subjective test. The question is not whether a

reasonable taxpayer might have made the same error or even whether this taxpayer failed to take all reasonable steps to ensure that the return was accurate. It is a question of the knowledge and intention of the particular taxpayer at the time.

64. The test of deliberate inaccuracy should be contrasted with that of careless inaccuracy. A careless inaccuracy occurs due to the failure by the taxpayer to take reasonable care (see paragraph 3(1)(a) of Schedule 24 Finance Act 2007 and *Harding v HMRC* [2013] UKUT575 (TCC) at [37])."

86. And secondly, from *HMRC v Raymond Tooth* [2018] UKUT 38 in which (and oddly enough the paragraphs are exactly the same as in *Auxilium*). The Tribunal said as follows:

"62. Assuming, for this purpose, that the Return and the Computation were inaccurate within the meaning of section 118(7) TMA, the next question is whether such (putative) inaccuracies were deliberate.

63. It is clear that, in terms of the applicable time limits, the relevant legislation contains a hierarchy based upon culpability. As was set out in paragraph 25 above in the case of discovery assessments, the normal period is one of 4 years, increasing to 6 in the case of carelessness and to 20 in the case of deliberation. An allegation of deliberately bringing about a tax loss is a serious one, tantamount to an allegation of fraud.

64. Self-evidently, the mere completion of a return – whilst a deliberate act, in the sense that the taxpayer deliberately fills it in and submits it – cannot of itself amount to a deliberate inaccuracy in a document. The deliberation must relate to the inaccuracy, not merely the completion and submission of the document."

87. We emphasise two points made in the foregoing extracts. Firstly the test is a subjective one. It is for HMRC to establish, on the balance of probabilities, that these appellants submitted their tax returns to HMRC for the year of enquiry (and for the previous years under assessment) knowing them to be incorrect and intending HMRC to rely on them as being correct; and secondly the finding of deliberate behaviour is tantamount to finding that the appellants have behaved fraudulently, i.e. dishonestly. Although, therefore, the standard of proof is the balance of probabilities, we will require extremely cogent evidence if we are to find that the appellants have acted dishonestly. It is for HMRC to provide that evidence. And they have not been able to cross examine the appellants on their behaviour by dint of the fact that they opposed the application by the appellants that they should be allowed to adduce oral evidence, and we have dismissed that application.

88. Furthermore the concepts of deliberate and careless behaviour have replaced the concepts of fraudulent and negligent behaviour. It is our view that the new legislation was not intended to make dramatic changes to the previous regime. Hence the reason why, in our view, in order to find deliberate conduct, a finding of dishonesty is also required.

89. HMRC have set out their view as to why the appellants deliberately submitted incorrect returns, in a number of places.

90. Firstly in the penalty explanation schedule for the schedule 24 penalties, HMRC say that the bank deposits and cash expenses greatly exceeded the declared turnover and there was no explanation as to why this was. The records relating to income were very poor but this is contrasted with the clear records of expenses. Their view is that this illustrates that the appellants did not want to show the true extent of their turnover.

91. Secondly in their written closing submissions. This was in response to directions which directed that they should set out the evidence on which their view of deliberate behaviour was based. In those submissions they make the following points. Firstly they refer to the notes of meeting. They point to two answers given by the first appellant. "*4.2 ST asked if all sales* were *banked and PS said the cash was just mixed into the cash from the rent receipts. PS does not retain any specific amount".* And "*2.2 ST asked if the books and records for the year fully reflect all business transactions and PS replied they did*".

92. The first of these is the evidence on which HMRC make their submission that "*the appellants admitted that not all expenditure goes through the books"*. But we cannot see that that record does constitute the admission which HMRC suggest, and it is abundantly clear from both the overall record of that interview as well as HMRC's calculations that they knew that the appellants paid expenses in cash. Indeed HMRC's criticisms of the appellants behaviour in the penalty explanation schedules was that whilst there was a paucity of information regarding the income, there was a great deal of information about the expenditure. Whilst there might have been some subsequent adjustments to that expenditure during the process of the enquiry, it was the appellants position as evidenced in some of the correspondence that HMRC's adjustments were incorrect. And that their expenditure was greater than that which HMRC have given them credit for in the assessments. As regards the assessments, then there is no obligation for HMRC to believe what the appellants say. But as regards the allegation of deliberate inaccuracies, and dishonesty, then they need to go further. This record is not evidence of dishonesty.

93. The second of these extracts reflects HMRC's broader submission that because the appellants kept no records of their rental income and simply used a broad brush, rule of thumb, method to calculate that rent (number of rooms, average income per room and occupancy levels) they could not have actually known the correct amount of rent which they received and so it was simply impossible for the books and records to accurately reflect that rent. So the appellants must have known that the figures submitted in the accounts and their tax returns were incorrect. Whilst they might have been a best guess, they were still just that.

94. One question that HMRC might have wished to ask in cross examination concerning this extract is whether "fully reflected" meant that the books and records "accurately reflected" all the business transactions or whether they simply accurately reflected the number of lettings but not the precise amounts derived therefrom. We can see that the former is a tenable interpretation of the record, and in the absence of any challenge, we cannot take that extract as an admission by the first appellant that he accepted that the books and records were an entirely accurate reflection of the "correct" amount of income that he had received during the year of enquiry.

95. HMRC also point to a number of occasions, including that meeting, where they have offered the appellants the opportunity to provide accurate information, or to clear things up, and the appellants have not chosen to take advantage of that opportunity, something which points towards deliberate behaviour. This is based on their submission that the appellants were fully aware that the figures that they had supplied were inaccurate.

96. We are sympathetic with HMRC's position. The appellants have claimed that they did have records of rents received and tenancy agreements, but these were uplifted during a police raid. HMRC are suspicious of the claim that they were so uplifted. But we would observe that although at certain points the appellants have denied there were any tenancy agreements, they were in fact able to supply some to HMRC, and HMRC used these as part of their basis for the

closure notices and the assessments. HMRC make nothing of the fact that there appears to be an inconsistency in the appellants position regarding tenancy agreements and this is not cited as an indication of deliberate behaviour. We therefore take this point no further. However our view is that the appellants, if they did originally have such records, did not use them as the basis for the declared income for the year of enquiry. For that year they appear to have no records of the rents, no comprehensive set of tenancy agreements and simply used an approximation based on average rents number of rooms and occupancy. The declaration of income for that year was not based on specific rents from specific lettings.

97. But we do not accept HMRC's submissions that what the first appellant is reported to have said in the April 2015 meeting constitute admissions that the appellants knowingly submitted incorrect figures. It is worth observing that we had cause to discuss a number of issues with the first appellant during the course of the hearing and it seemed to us that he did not fully grasp what was going on. We suspect the same might have been true of the April 2015 meeting.

98. We have found that the assessments were fairly arrived at, and the appellants have produced no cogent evidence to enable us to find that they were wrong. So it follows that the appellants under declared their income. And the fact of the matter is that the appellants did not know precisely how much income they had derived from the properties during the year of enquiry.

99. But there is a big difference between someone who makes a reasonable attempt to calculate their income, and submits that figure to HMRC, and another person who actually knows that the figure that he is submitting to HMRC is incorrect either because he knows the true figure or because he is taken no care whatsoever to arrive at that figure.

100. The appellants have attempted to provide an accurate amount of their rental income by using a fairly rough and ready approach. But the approach is not an unreasonable one. It just happens that, in the circumstances, it has understated the appellants income. They have made an attempt to come up with an accurate figure. They have not cynically known that that figure is inaccurate. Or, more relevantly, HMRC have not in our view established that that was the case.

101. Even though the amount not incorrect, HMRC have not in our view established that on the balance of probabilities the appellants knew that the amount submitted was incorrect even though they must have had some misgivings given that they did not have accurate records of the precise income they had received from the tenancies for the year of enquiry. The appellants behaviour does not appear to us to have been dishonest, even though we find it to be careless, something which we discuss below.

102. Although this is very finely balanced, we have come to the conclusion that the appellants have acted neither deliberately, nor fraudulently. The effect this has on the assessments and the penalties is discussed below.

Careless

103. It is open for us, if we decide that the behaviour was not deliberate or fraudulent, to come to a decision that the behaviour was, however, careless or negligent.

104. In the First-tier Tribunal case of *Mr J R Hanson v HMRC* [2012] UKFTT 314, Judge Cannan set out what he considered the test for carelessness (or failing to take reasonable care.).

We set it out below.

> "19 In my view carelessness can be equated with "negligent conduct" in the context of discovery assessments under section 29 Taxes Management Act 1970. In that context, negligent conduct is to be judged by reference to the reasonable taxpayer. The test was described by Judge Berner in Anderson (deceased) v Revenue and Customs Commissioners [2009] UKFTT 206 at [22], cited with approval by the Upper Tribunal in Colin Moore v Revenue and Customs Commissioners [2011] UKUT 239 (TCC):
>
> > "*The test to be applied, in my view, is to consider what a reasonable taxpayer, exercising reasonable diligence in the completion and submission of the return, would have done.*""

105. Although Judge Cannan's view is not binding on us, we agree with it and adopt it as the test which is to be applied in this case.

106. In our directions, we specifically directed that if HMRC alleged careless behaviour, then they should clearly set out in their written closing submissions. They did this. We also directed that if HMRC alleged careless behaviour in their submissions, and the appellants agent should deal with this in his submissions. He failed to do so.

107. It is clear to us that the appellants have acted negligently or carelessly. A reasonable taxpayer in their position would have kept records which would have enabled them to have submitted a return based on more accurate data and would not have needed to have relied on the rough and ready approach which they have adopted. It is true that the appellants then agent, in the April 2015 interview, accepted that he checked that the appellants banking tied up with their income. This is a check that HMRC also undertook, and clearly came up with a very different conclusion given that they based their assessments on the difference between the banked income and the expenses. One might have expected the appellants then agent, having undertaken a similar exercise to have tested their clients as regards expenses which did not go through the banking system. But ultimately the responsibility for submitting an inaccurate returns lies with the taxpayer. And had they kept accurate records and submitted their returns based on those records, this issue would not have arisen. A reasonable taxpayer in the appellants position would have records and would thus have been able to submit a more accurate return. It is our view that the appellants have acted negligently or carelessly when completing their tax return for the year of enquiry, and for the years of assessment.

Impact on the assessments

108. In their written closing submissions, HMRC have asked us to find that if we find the appellants to have been careless or negligent, rather than deliberate or fraudulent, that we uphold the following as regards the assessments and the closure notices:

assessments

Year	**Mr Sanghera**	**Mrs Sanghera**
2011/12	£5,155.80	£1,549.60
2010/11	£5,431.20	£760.60

2009/10	£3,784.60	£590.80
2008/9	£3,131.60	£2,044.40
2007/8	£872.08	£871.86
2006/7	£652.30	£652.30

closure notices

Year	**Mr Sanghera**	**Mrs Sanghera**
2012/13	£2,938.00	£2,411.60

The penalties

109. In those submissions they have also asked us to find, on the question of penalties under s 95 TMA1970, the following:

Year	**Mr Sanghera**	**Mrs Sanghera**
2006/7	£391.38	£391.39
2007/8	£523.25	£523.12

110. Finally as regards the Schedule 24 penalties for the tax years 2008-2009 to 2012-2013, we find that the amounts assessed by HMRC on the appellants for each of those periods as set out in the appendices to their closing submissions are correct. These amount to £10,803.78 for the first appellant and £3,991.18 for the second appellant. HMRC have, however, indicated in their closing submissions that if we come to a finding of careless behaviour for the Schedule 24 penalties, they would consider setting suspension condition. We direct that if the parties cannot agree appropriate suspension conditions then either party may apply to the tribunal to consider the matter further.

CONCLUSION AND DECISION

111. Drawing the strands together. We have concluded that the respondents have adopted a fair methodology in making the assessments and the appellants have failed to displace them. The appellants have also failed to displace the conclusion set out in the closure notices. However HMRC have failed to establish deliberate or fraudulent behaviour on the part of the appellants, and so the number of years for which HMRC can validly assess the appellants to under declared income does not extend beyond 2006-2007. This is true, too, of the penalties.

112. We therefore dismiss the appellants appeals against the assessments to both tax and penalties for the years 2012-2013 to 2006-2007 inclusive, but allow the appellants appeals against the assessments and the penalties for earlier years.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

113. 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.

NIGEL POPPLEWELL
TRIBUNAL JUDGE

RELEASE DATE: 15 MAY 2020