[2019] UKFTT 170 (TC)

# TC07020

**Appeal number: TC/2016/02255**

***INCOME TAX – discovery assessments and closure notice in relation to certain deductions claimed as business expenses – expenses in relation to cost of materials disallowed but interest costs allowed – appeal allowed in part – penalties for careless inaccuracies – adjustment to penalties to reflect the outcome of the appeal in relation to the discovery assessments and the closure notice***

**FIRST-TIER TRIBUNAL**
**TAX CHAMBER**

**NIKOLAY DANGOV** **Appellant**

**- and -**

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

**TRIBUNAL: JUDGE TONY BEARE**

**Sitting in public at Taylor House, 88 Rosebery Avenue, London EC1R 4QU on 15 February 2019**

**The Appellant did not appear and was not represented**

**Mr Justin Kruyer, Officer of HM Revenue and Customs, for the Respondents**

DECISION

Introduction

1. This appeal relates to the following matters:

(a) an assessment to income tax (which was issued on 13 October 2015 and subsequently varied on 23 March 2016) in the amount of £6,063.68 in respect of the tax year of assessment (a "tax year") ending 5 April 2011 which reduces the repayment of tax due to the Appellant in respect of that tax year from £7,643.72 to £1,580.04;

(b) an assessment to income tax (which was issued on 13 October 2015 and subsequently varied on 23 March 2016) in the amount of £13,381.47 in respect of the tax year ending 5 April 2012 which requires the Appellant to pay additional tax of £638.14 in respect of that tax year instead of obtaining a repayment of tax in respect of that tax year of £12,743.33;

(c) an assessment to income tax (which was issued on 13 October 2015 and subsequently varied on 23 March 2016) in the amount of £16,607.18 in respect of the tax year ending 5 April 2013 which requires the Appellant to pay additional tax of £1,907.70 in respect of that tax year instead of obtaining a repayment of tax in respect of that tax year of £14,699.48;

(d) a closure notice amending the Appellant's self-assessment to income tax in respect of the tax year ending 5 April 2014 (which was issued on 14 October 2015 and subsequently varied on 23 March 2016) which reduces the repayment of tax due to the Appellant in respect of that tax year from £4,197.20 to £1,565.74; and

(e) an assessment to a penalty in respect of each of the tax years described in paragraphs 1(a) to 1(d) above (which was notified on 14 October 2015 and subsequently varied on 23 March 2016) in the aggregate amount of £9,284.10.

Preliminary matters

2. Before I turn to the specifics of the appeal, there are two preliminary matters which require attention.

3. The first is attributable to the fact that the Appellant did not attend the hearing. However, he wrote to the First-tier Tribunal on 31 January 2019 and 13 February 2019 to say that he might not be attending the hearing and to set out his position in relation to the appeal. I shall say more below about the content of the Appellant's submissions but, for present purposes, it suffices to note that I was satisfied that the Appellant had been notified of the hearing and had chosen not to attend. Consequently, I considered that it was in the interests of justice to proceed with the hearing.

4. The second preliminary matter is that, although the notice of appeal to the First-tier Tribunal properly referred to the review conclusion letter of 23 March 2016 as the subject matter of the appeal, that review was prompted, to the extent that the appeal relates to the discovery assessments in respect of the tax years ending 5 April 2011, 5 April 2012 and 5 April 2013, by the Appellant's appeal against the revised discovery assessments of 18 November 2015, and not the original discovery assessments of 13 October 2015.

5. As the review conclusion letter makes clear, those revised discovery assessments were invalid because they were issued at a time when the original discovery assessments had not been determined by agreement or by the First-tier Tribunal (see paragraph 67 of the review conclusion letter). The Respondents have not sought to make an issue of this and I infer from their approach that, so far as the discovery assessments are concerned, they are happy to treat the Appellant as having appealed against the original assessments of 13 October 2015. I believe that they are right to do so, given that they were in error in subsequently issuing the invalid assessments.

Background

6. The Appellant is a sub-contractor working in the construction industry.

7. The events which have ultimately led to these proceedings may be summarised as follows:

> (a) on 6 April 2013, the Respondents received the Appellant's tax return in respect of the tax year ending 5 April 2013;
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> (b) on 3 September 2013, the Respondents wrote to the Appellant requesting evidence of identity and asking him to forward to the Respondents all of the Construction Industry Scheme ("CIS") payment and deduction statements which he had received from his contractors for the tax year in question, along with the names and addresses of all the contractors for whom he had worked and a detailed analysis of his expenses;
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> (c) on 11 September 2013, the Appellant went to the Respondents' Winchmore Hill Enquiry Centre and produced evidence of his identity. He wrote to the Respondents on the following day advising them of this.
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> In his letter, the Appellant informed the Respondents that he had sent to the Respondents by recorded delivery all of his CIS payment and deduction statements in respect of the tax year ending 5 April 2013, along with receipts for building materials used during that tax year, a detailed breakdown of his building expenses during that tax year and a list of the clients for whom he had worked during that tax year.
>
> He also enclosed a copy of a receipt of posting for £1.70 dated 8 April 2013. The Appellant explained in that letter that he had sent the material to the Respondents without waiting to be asked for it because he wanted to speed up the receipt of the tax repayment which would result from it;

(d) on 26 September 2013, the Appellant sent a duplicate of this letter to the Respondents;

(e) on 10 October 2013, the Appellant wrote again to the Respondents to ask why he had not received the repayment of tax in respect of the tax year ending 5 April 2013 and pointing out that the delay in making that repayment was causing financial hardship to the Appellant;

(f) on 28 October 2013, the Appellant wrote again to the Respondents about the delay in his receiving the tax repayment. He pointed out once again that the delay in his receiving the tax repayment was causing him financial hardship and asked for the repayment to be expedited;

(g) on 8 November 2013, the Respondents wrote to the Appellant informing him they were having difficulty tracing the records he claimed to have sent in April, 2013. The Respondents said that they were still trying to locate that information but that, in the meantime, the Appellant should send to them the names and addresses of all contractors for whom the Appellant had worked in both the tax year ending 5 April 2013 and the preceding tax year;

(h) on 14 November 2013, the Appellant replied to the Respondents, stating that he had worked for only one contractor during the tax year ending 5 April 2013 – namely, Future Interior Contracts ("FIC") - and reminding the Respondents that their delay in sending him the tax repayment was causing him financial hardship;

(i) on 22 November 2013, the Respondents wrote to the Appellant to confirm receipt of the letter of 14 November 2013 and asking the Appellant to "wait for at least 6 weeks from the date of this letter before you contact [the Respondents] again regarding this matter";

(j) on 27 December 2013, the Appellant wrote to the Respondents purporting to reply to a letter from the Respondents of 18 December 2013 which was not in the document bundle for the hearing but which, from the terms of the Appellant's reply, must have asked the Appellant for the same information about customers as had been requested in the Respondents' letter of 8 November 2013.

The Appellant said that he had already replied to the Respondents' letter of 8 November 2013 by recorded mail but that he would set out again the details of the contractors for whom he had worked in the tax year ending 5 April 2013. In this letter, the Appellant provided the names of five further contractors, in addition to FIC, for whom he had worked in the relevant tax year. Those were Shakespeare Interiors UK Ltd ("Shakespeare"), RMF Construction ("RMF"), Planet Interiors, Worldexpand Projects Limited and Smileberry Interiors. Finally, he reminded the Respondents that the statements sought by the Respondents had been sent to them in April 2013 by recorded delivery;

(k) on 7 January 2014, the Respondents wrote to the Appellant to confirm receipt of the letter of 31 December 2013 (by which the Respondents must have meant 27 December 2013) and again asking the

Appellant to "wait for at least 6 weeks from the date of this letter before you contact [the Respondents] again regarding this matter";

(l) on 16 January 2014, the Respondents wrote to the Appellant, informing him that they had been unable to trace FIC, and asking the Appellant to provide further information in relation to FIC. The Respondents' letter went on to say that they had records showing that the Appellant had worked for many more contractors than the one contractor mentioned in the Appellant's letter of 14 November 2013 and enclosed a summary of the information held by the Respondents in relation to the work done by the Appellant for those other contractors.

The summary showed that the Appellant had worked during the relevant tax year for Shakespeare, RMF, J Graham Interiors ("JGI") and Specialist Ceiling Installations ("SIC"). (The first two of those had been mentioned in the Appellant's letter of 27 December 2013 but the latter two had not been mentioned in either the Appellant's letter of 14 November 2013 or the Appellant's letter of 27 December 2013). The details supplied by the Respondents showed that the Appellant had received the aggregate amount of £13,381 from the four contractors specified, from which £2,676.25 tax had been deducted.

The Respondents concluded by noting that this figure exceeded the amount which the Appellant had included in his tax return in respect of the relevant tax year and that "[n]o repayment will be released until this discrepancy has been resolved";

(m) on 22 January 2014, the Appellant replied, stating he was unable to provide any more information about FIC. He added that the reason why he had referred only to FIC in his letter of 14 November 2013 was that that was the contractor in relation to which he had incurred significant amounts on business materials and that he therefore thought that the Respondents would consider it important.

He also pointed out that the absence of any reference to FIC in the records enclosed with the Respondents' letter of 16 January 2014 showed that the Respondents' records were incomplete.

Finally, he reiterated that the statements sought by the Respondents had been sent to them in April 2013 by recorded delivery and suggested that, as the Respondents could not trace FIC, he was prepared to accept a reduced figure for his expenses in respect of the tax year ending 5 April 2013 of £2,676.25;

(n) on 19 February 2014, the Appellant wrote to the Respondents complaining about how long it was taking to process his repayment and referring to various calls which he had made to the Respondents' customer services in the hope of expediting it.

The Appellant reiterated that he had sent to the Respondents both the statements which they had requested (which the Respondents had not traced) and the information about the contractors for whom the Appellant had worked during the tax year in question. He again requested that the Respondents progress the matter;

(o) on 31 March 2014, the Respondents wrote to the Appellant to explain that they had been unable to trace the letter of 10 April 2013 enclosing the requested statements. (The reference to 10 April 2013 should have been to 8 April 2013 as that was the date set out on the recorded delivery receipt which the Appellant had provided to the Respondents on 12 September 2013).

The Respondents requested that the Appellant provide them with an analysis of the turnover figure of £76,893 shown on the Appellant's tax return in respect of the relevant tax year and pointed out that, if the Respondents were to reduce the tax figure for the relevant tax year to £2,676.25, as the Appellant had requested, no repayment would be due. (I assume that the reference to a reduction in the "tax figure" was intended to mean a reduction in the deductions claimed by the Appellant, as that is what the Appellant had suggested in his letter of 22 January 2014);

(p) on 11 April 2014, the Appellant wrote to inform the Respondents that he was temporarily abroad, that the figure of £76,893.00 which appeared in his tax return related to his business as a builder and that he had already forwarded to the Respondents – in the letter which the Respondents had yet to trace - all of his receipts, statements and other supporting documents for the relevant tax year.

He concluded by saying that he had already sent to the Respondents a detailed analysis of his business expenses for building materials used during the relevant tax year, amounting to £47,891.00 in aggregate – which he had, under cover of his letter of 12 September 2013 – and then set out that figure again, along with information about his other expenses during the tax year in question and his taxable profit;

(q) also on 11 April 2014, the Respondents received the Appellant's tax return in respect of the tax year ending 5 April 2014;

(r) on 25 June 2014, the Respondents wrote to the Appellant to inform him that they had still been unable to trace the Appellant's letter of April 2013 but that research on Royal Mail's website indicated that postage of £1.70 (which was the amount shown on the recorded delivery receipt provided by the Appellant) would relate to a small letter rather a parcel.

The Respondents suggested that, had the Appellant enclosed all his records, as he had been asserting, the postage would have cost more. They reminded the Appellant that he had a legal requirement to keep the records which formed the basis of his tax return and they requested copies of the Appellant's bank statements and specific information in relation to certain deductions claimed by the Appellant in respect of the tax year ending 5 April 2013.

Finally, the Respondents requested copies of all CIS statements which the Appellant had received from his contractors during the tax year ending 5 April 2014, along with an analysis of the expenditure which the Appellant had claimed in his tax return in respect of the relevant tax year and receipts and invoices evidencing those expenses;

(s) also on 25 June 2014, the Respondents wrote to FIC requesting details of any payments made to the Appellant during the tax year ending 5 April 2013, and enquiring whether FIC had supplied materials to the Appellant or reimbursed him for them. On the same day, the Respondents wrote to each of Shakespeare, RMF, JGI and SIC to similar effect;

(t) on 27 June 2014, the letter to FIC was returned to the Respondents marked "gone away";

(u) also on 27 June 2014, JGI replied to the Respondents stating that they had reimbursed the Appellant £7.99 for materials during the tax year ending 5 April 2013;

(v) on 30 June 2014, Shakespeare replied to the Respondents stating that the Appellant had neither supplied nor been reimbursed for materials, as Shakespeare itself had supplied all materials to the Appellant;

(w) the Respondents did not receive any reply from RMF or SIC;

(x) on 26 July 2014, the Appellant wrote to the Respondents informing them that the letter containing his receipts which he had sent to the Respondents was of a medium size and big enough for the material that he had sent to them.

He told the Respondents that he no longer received paper bank statements as he banked online and he did not enclose his CIS statements in respect of the tax year ending 5 April 2014 but he responded to the questions asked of him in relation to the tax years ending 5 April 2013 and 5 April 2014 by the Respondents in their letter of 25 June 2014, noting that the expenses for which he had claimed were perfectly normal for the construction industry;

(y) on 14 November 2014, the Respondents wrote to the Appellant to inform him that they were opening an enquiry into his tax return for the tax year ending 5 April 2014, which would look at his self-employment turnover and expenses. The Respondents requested a number of documents from the Appellant for this purpose;

(z) on 10 December 2014, the Appellant wrote to the Respondents informing them that his home had been flooded in July 2014 and that, as a result, "all my business papers including CIS certificates, receipts for business expenses (materials, travel, office costs…) some other certificates and other important documents were badly damaged and destroyed." However, the Appellant provided details of some expenses which he had incurred in the tax year ending 5 April 2014 which he said that he had kept stored on his laptop;

(aa) on 15 January 2014, the Respondents wrote to the Appellant, asking him to provide documentary evidence of the flooding, such as an insurance claim, photographs or receipts for replacing or repairing damaged items.

The Respondents also asked for details of the contractors for whom the Appellant had worked during the tax year in question and bank statements

to support the Appellant's claim for expenses for which he was unable to provide receipts.

The Respondents also raised certain questions in relation to travel expenses for which the Appellant had claimed;

(bb) on 9 February 2015, the Appellant wrote to the Respondents to say that he had already provided the details of the contractors for whom he had worked during the tax year in question in one of his previous letters. However, he provided the details of one contractor, Simplicity Mouldings ("SM"), and said that he had worked for one other contractor, which he thought to be SCI but was not sure, because of the time which had elapsed since the tax year in question.

He reiterated that the flood had destroyed all of his business papers but did not provide any of the evidence in relation to the flood which the Respondents had requested in their letter of 15 January 2015. In relation to his travel expenses, the Appellant said that one item of expense was in fact attributable to the previous tax year but provided details of his travel expenses for the tax year ending 5 April 2014. (His letter said that those details related to the tax year ending 5 April 2013 but, viewed in context, he must have intended to refer to the following tax year). The Appellant also provided information regarding his modes of transport;

(cc) on 18 February 2015, the Respondents replied to the Appellant, confirming that the Appellant had indeed worked for SM and SCI in the tax year ending 5 April 2014 and providing details, from the Respondents' records, of the payments made to the Appellant by those two contractors during the tax year in question.

The Respondents reiterated their request for the Appellant's bank statements and for evidence of the flood, noting that the Appellant had not mentioned the flood in his letter to the Respondents of 26 July 2014.

The Respondents also requested details of the Appellant's vehicle and the insurance for that vehicle.

Finally, the Respondents said that they were confused by the reference to the tax year ending 5 April 2013 at the top of the table of expenses sent by the Appellant in his previous letter;

(dd) on 11 March 2015, the Appellant wrote to the Respondents enclosing 18 pay slips from SM. These totalled considerably more than the figures mentioned in relation to SM by the Respondents in their letter of 18 February 2015.

The Appellant confirmed that the list of expenses in his letter of 9 February 2015 related to the tax year ending 5 April 2014. Finally, the Appellant informed the Respondents that he had no evidence of the flooding, had not kept bank statements, had since closed his account, and used a private car, not a commercial vehicle;

(ee) on 20 March 2015, the Respondents wrote to the Appellant in relation to the payslips which the Appellant had included in his letter of 11 March 2015.

The Respondents queried how the Appellant had been able to provide the payslips given his previous assertion that all of his business records had been destroyed by the flood. The Respondents noted that, as all but three of the payslips were not matched by a monthly return from SM, they had written to SM to request an explanation.

The Respondents again requested evidence in relation to the flood – for example, a copy of an insurance claim or details of the friends with whom the Appellant had stayed while the flat was drying out.

The Respondents noted that, in the absence of any receipts or bank statements to support the claims for deductions in respect of fuel, they would have to consider whether to accept the claims in full. In that regard, they asked the Appellant for his weekly expenditure on fuel.

Finally, the Respondents explained that they had asked for the details of the Appellant's vehicle in order to ascertain whether the expenses claimed by the Appellant in relation to materials were justified. In that regard, the Respondents pointed out that some of the materials which were the subject of those claims would not have fitted in a standard-sized car and that the delivery charges claimed by the Appellant were comparatively modest (only £131.50);

(ff) also on 20 March 2015, the Respondents wrote to SM, asking SM to confirm the total of the payments which it had made to the Appellant in relation to the tax year ending 5 April 2014 (and related tax deductions) and to explain why the CIS returns in relation to the Appellant for months ending 5 November 2013 et seq. had not been provided by SM.

The Respondents also asked SM whether the Appellant was required to provide his own tools and materials or whether those had been provided for him on site and for any reimbursement payments which had been made to the Appellant in respect of tools, materials or travel costs.

On the same day, the Respondents wrote to SCI, to similar effect;

(gg) on 9 April 2015, the Appellant wrote to the Respondents to explain that he had found the payslips while searching for something else and that the flood had not affected all the rooms in his house.

The Appellant said that he had not made an insurance claim following the flood as he did not have home insurance and refused to give details of the friends he had stayed with following the flood "because I do not want my friends to be disturbed by your letters".

Finally, the Appellant explained that the delivery charges he had claimed related to larger items he had purchased, and provided a list of smaller items which he had been able to transport in his car;

(hh) on 10 April 2015, the Respondents received an email from Mr Mike Ferrin, seemingly in reply to the Respondent's letter to SCI of 20 March 2015, confirming that the Appellant was required to provide his own tools and that no transport was provided but that the materials used by the Appellant were "bespoke factory formed GRG panels with specialist fixings these items were all supplied by the main contractor";

(ii) on 17 April 2015, the Respondents wrote to the Appellant, explaining that the Respondents required the details of the friend with whom the Appellant had stayed only to verify the explanation given by the Appellant for being unable to produce his records.

The Respondents also informed the Appellant they did not accept his explanation about delivery charges based on the terms of Mr Ferrin's email of 10 April 2015. (In fact, the Respondents said that they did accept the Appellant's explanation but their sentence makes sense only if one reads a missing "not" into it after "do".)

The Respondents added that they had yet to receive a response from SM to their letter of 20 March 2105 and that, subject to the terms of any such response, they had now to consider what to allow the Appellant as deductions for travel, materials and administration costs;

(jj) on 11 May 2015, the Appellant wrote to the Respondents and berated them for the time which it was taking to verify his payslips from SM and for accepting without any supporting evidence Mr Ferrin's statement that the Appellant had not provided any materials in relation to his work for SCI;

(kk) on 12 May 2015, the Respondents sent a chasing letter to SM;

(ll) on 3 June 2015, the Respondents wrote to the Appellant to confirm that they were still awaiting a response from SM and that, in the absence of any reply, they would send the Appellant, by the week ending 19 June 2015, their proposal for revising the figures in the Appellant's tax return in respect of the tax year ending 5 April 2014;

(mm) on 5 June 2015, the Appellant wrote to the Respondents to chase for a response to his letter of 11 May 2015. (This letter clearly crossed in the post with the Respondents' letter of 3 June 2015);

(nn) on 18 June 2015, the Respondents wrote to the Appellant to confirm that they had not received any reply from SM and to make their proposals in relation to the Appellant's tax return for the tax year in question.

In that regard, the Respondents said that they proposed to accept the figures on the tax return for turnover and tax deductions but that, in the absence of the necessary evidence, they were not prepared to accept all of the expenses which the Appellant had claimed.

The Respondents proposed that deductions of £5,753.00, which amounted to 20% of the Appellant's turnover, would be appropriate. They pointed out that the Appellant's claim was for expenses equal to 62% of his turnover, which seemed to the Respondents to be excessive. In consequence of the above, the Respondents proposed to reduce the overpayment of tax claimed by the Appellant of £4,197.20 to £707.05.

Finally, the Respondents enclosed information in relation to penalties;

(oo) on 2 July 2015, the Appellant wrote to the Respondents to refuse the proposal which the Respondents had made in their letter of 18 June 2015 and to complain once again about how the Respondents were dealing with their outstanding enquiries in relation to the Appellant with SM. The

Appellant made a counter-proposal that the overpayment in respect of the relevant tax year be halved to £2,098.60;

(pp) on 30 July 2015, the Respondents wrote to the Appellant to inform him that, in the light of the inaccuracies which they had discovered in the Appellant's tax return in respect of the tax year ending 5 April 2014, they wished to check for similar inaccuracies in relation to the Appellant's tax returns in respect of the tax years ending 5 April 2011, 5 April 2012 and 5 April 2013 respectively.

In relation to that check, the Respondents requested CIS certificates and receipts or other evidence to support claims for deductions in respect of each relevant tax year;

(qq) on 11 August 2015, the Appellant wrote to the Respondents to chase for a response to the proposal set out in his letter of 2 July 2015 and to ask why the Respondents were ignoring his payslips instead of investigating, or putting pressure on, SM;

(rr) on 28 August 2015, the Appellant wrote to the Respondents to the same effect. In addition, in relation to the enquiry into the Appellant's tax returns in respect of the tax years ending 5 April 2011, 5 April 2102 and 5 April 2013, the Appellant said that he had already provided all of his original CIS statements and receipts to the Respondents by recorded mail;

(ss) on 8 September 2015, the Respondents wrote to the Appellant to say that, contrary to the apparent understanding of the Appellant, as recorded in his letters of 11 August 2015 and 28 August 2015, the Respondents had accepted the Appellant's figures for turnover and tax deducted in respect of the tax year ending 5 April 2014. There was therefore no further need for them to chase up SM.

The Respondents confirmed that they were proposing to reduce the deductible expenses in respect of the relevant tax year to 20% of turnover, as set out in their letter of 18 June 2015.

In relation to the earlier tax years, the Respondents said that they had not received the CIS certificates or documentation in support of the expenditure claimed. Noting some discrepancies between declared turnover and tax deductions in comparison to the figures returned to the Respondents by the main contractors, and the absence of any receipts, the Respondents said that, in relation to those tax years, they would again accept the Appellant's turnover figures but would reduce the tax credits to the amounts reported by the contractors and again reduce the deductions in respect of each tax year to a total of 20% of the turnover in the relevant tax year.

The Respondents said that, in the absence of any further information from the Appellant on or before 8 October 2015, they would raise assessments in relation to each of the tax years ending 5 April 2011 to 5 April 2014 (inclusive) and assess any penalties which might be due;

(tt) on 13 October 2015 and 14 October 2015, the Respondents issued to the Appellant notices of assessment in respect of each of the tax years ending 5 April 2011, 5 April 2012 and 5 April 2013 and a closure notice

in respect of the tax year ending 5 April 2014 (each of which reflected the proposal set out in the letter from the Respondents of 8 September 2015) and a penalty explanation notice in respect of those tax years;

(uu) on 27 October 2015, the Appellant wrote to the Respondents to complain about the treatment he had received and, in particular, the penalties;

(vv) on 2 November 2015, the Appellant wrote to the Respondents referring to a letter from the Respondents to him of 14 October 2015. Presumably, this was the penalty explanation notice referred to above.

In his letter of 2 November 2015, the Appellant said that he had not received the letter of 8 September 2015 and asked for a copy of it to be sent to him. He also said that he had always co-operated with the Respondents and provided the Respondents with the information they had requested so that it would be wrong for him to suffer penalties.

Finally, the Appellant provided the Respondents with the name of the friend with whom he said that he had stayed after the flood;

(ww) on 20 November 2015, the Respondents wrote to the Appellant enclosing a further copy of their letter of 8 September 2015 but saying that the Respondents had, since that letter, revised their proposal. The Respondents set out in the letter their revised proposal.

This involved giving credit to the Appellant for the tax deduction figures which were shown in the Appellant's tax return in respect of each tax year.

The Respondents also explained that the penalties set out in their earlier penalty explanation notice had also been revised to reflect both the amendments to the Respondents' proposal described above and the fact that the Respondents were now prepared to regard the Appellant's behaviour as "careless" instead of "deliberate". This meant that the Respondents were able to offer a suspension of the penalties subject to the Appellant's compliance with various conditions.

The Respondents reiterated that, in relation to the tax year ending 5 April 2014, they were accepting the Appellant's figures for turnover and tax deducted (and therefore the Appellant was wrong to be focusing on the fact that the Respondents had not been able to contact SM) and that, in relation to the earlier tax years, the Respondents had not received any CIS statements or documentation to support the deductions claimed by the Appellant in respect of those tax years.

Finally, the Respondents enclosed revised notices of assessment in respect of the tax years ending 5 April 2011, 5 April 2012 and 5 April 2013, along with a revised penalty explanation notice and a copy of the penalty suspension conditions;

(xx) on 5 December 2015, the Appellant wrote to the Respondents to reiterate that he could justify the amount of his expenses in respect of each tax year and to ask the Respondents to trace the documentation which he had sent to them earlier.

He also pointed out that, contrary to the information shown in his on-line account with the Respondents, he had not received a repayment of tax in respect of the tax year ending 5 April 2013.

Finally, the Appellant appealed against the various assessments, the closure notice and the penalties and asked the Respondents to stop their debt management team from pursuing him;

(yy) on 15 January 2016, the Respondents wrote to the Appellant to say that they were treating the Appellant's letter of 5 December 2015 as an appeal against the various assessments, the closure notice and the penalties, to set out their view of the matter, to confirm that they agreed that no repayment had been made to the Appellant in respect of the tax year ending 5 April 2013, to confirm that they had asked the debt management team to suspend recovery action and to invite the Appellant to ask for a review of their decision or to appeal to the First-tier Tribunal if he still disagreed with the assessments, the closure notice and/or the penalties.

In that letter, the Respondents set out the figures which the Appellant had provided in respect of each relevant tax year to show that the Appellant must have been making a commercial loss in the first three of the tax years and only a small commercial profit in the tax year ending 5 April 2014;

(zz) on 9 February 2016, the Appellant wrote to the Respondents to agree to the penalty suspension conditions and reiterate his disagreement with the closure notice, assessments and penalties. He also reiterated that the expenses he had claimed were justified and that he had previously sent the evidence of those expenses to the Respondents by recorded delivery.

Finally, the Appellant explained the commercial losses and small commercial profit mentioned above by reference to the spiralling costs of materials and tools and by reference to the recession and said that he had used his savings to supplement his income;

(aaa) although the Appellant had not formally asked for a review, the Respondents treated his letter of 9 February 2016 as amounting to such a request and therefore wrote to the Appellant on 10 March 2016 to confirm that they would conduct that review;

(bbb) on 13 March 2016, the Appellant wrote to the Respondents to reiterate his position in relation to the matters which were under appeal;

(ccc) on 23 March 2016, the Respondents wrote to the Appellant with the results of their review. The Officer conducting the review (CW Agg) recited the history of the matter and then explained that, rather than approaching the question of the deductions in respect of each tax year globally, by reference to the percentage which the aggregate amount of the deductions in respect of the relevant tax year represented of the turnover in respect of the relevant tax year, it was more appropriate to examine each category of deductions separately.

Having done so, the Officer proposed, in respect of each tax year, to disallow:

- the expenditure on materials – because those contractors who had replied to the Respondents' enquiries had confirmed that the Appellant was not required to supply his own materials (apart from one contractor, who said that the Appellant had provided materials to the value of £7.99 and had been reimbursed for those materials), that, whilst it was possible that the Appellant might have supplied materials to contractors who had not responded, the Officer would have expected such contractors to reimburse the Appellant for such materials and that many of the materials which the Appellant claimed to have purchased were of a size which made it unrealistic for the Appellant to have transported them by public transport or private vehicle; and

– the interest – on the basis that, as interest was deductible only if it was incurred as a business expense and the Respondents were disallowing the expenditure on materials, it was reasonable to assume that the interest must have related to expenses other than business expenses.

The Officer proposed to allow all other expenses which the Appellant had claimed, which meant that "you will not have been penalised in any way for the fact that your records are not available".

The Officer then explained why each of the assessments issued in October 2015 was still in time and why those assessments still remained open, even though the assessments of November 2015 were invalid because each of the earlier assessments were still the subject of an existing appeal which had not yet been determined.

As a result of the conclusions described above, the Officer set out the revised amounts of tax or repayments of tax which were due in respect of each of the tax years of assessment. The adjustments made were as follows:

- in respect of the tax year ending 5 April 2011, the original discovery assessment of £7,330.70 was reduced to 6,063.68;
- in respect of the tax year ending 5 April 2012, the original discovery assessment of £23,103.79 was reduced to £13,381.47;
- in respect of the tax year ending 5 April 2013, the original discovery assessment of £30,031.91 was reduced to £16,607.18; and
- in respect of the tax year ending 5 April 2014, the original closure notice showing an additional tax liability of £3,490.15 was reduced to show an additional tax liability of £2,631.46.

Finally, the Officer confirmed that the penalties based on carelessness by the Appellant were correct, that the Appellant should not get a discount for making an unprompted disclosure (because he had not told the Respondents about the inaccuracies before the Respondents discovered those inaccuracies themselves) and that the quality of the Appellant's disclosure did not justify a reduction in the penalty to 15% instead of the 24% originally proposed.

As a result of the adjustments to the assessments and the closure notice described above, the penalties - at the rate of 24% of the difference, in respect of each tax year of assessment, between the amount of tax shown in the Appellant's tax return and the amount of tax assessed as described above - were £1,455.28 (in respect of the tax year ending 5 April 2011), £3,211.55 (in respect of the tax year ending 5 April 2012), £3,985.72 (in respect of the tax year ending 5 April 2013) and £631.55 (in respect of the tax year ending 5 April 2014).

The Officer informed the Appellant that he would have 30 days from the date of the letter to appeal the outcome of the review;

(ddd) on 2 April 2016, the Appellant wrote to the Respondents requesting additional time to notify his appeal to the First-tier Tribunal on the grounds that he had received the review conclusion letter only on 29 March 2016;

(eee) on 12 April 2016, the Respondents wrote to the Appellant to inform him that the 30-day deadline was statutory and that the Respondents themselves could not vary it. They pointed out that, although the First-tier Tribunal did have a discretion to allow a late notification of the appeal, the Appellant should try to notify the appeal on or before 23 April 2016. Finally, they apologised for the delay in the receipt by the Appellant of the review conclusion letter;

(fff) on 18 April 2016, the Appellant notified the appeal to the First-tier Tribunal;

(ggg) on 2 September 2016, the Appellant wrote to the Respondents to say that he had contacted two of the site managers who had worked with him previously to ask them to confirm that he had supplied his own materials in relation to that work.

He enclosed letters from those site managers, a Mr Robert Kodali, who had been employed by Mulligan Interiors and Finishing ("Mulligan") from 2007 until September 2015, and a Mr Lucas Mikonis, an employee of Doherty & Sons Interiors ("Doherty").

The letter from Mr Kodali said that the Appellant had worked for Mulligan in 2014 and supplied his own materials to the value of approximately £5,000.00 for that work and the letter from Mr Mikonis said that the Appellant had worked for Doherty in 2013 and supplied his own materials to the value of approximately £18,000.00 for that work.

The letter from the Appellant also enclosed a personal loan agreement of 21 July 2013 between the Appellant and a friend, Mr Daniel Petrov, for the sum of £4,500.00 and explained that a similar loan, in the amount of £4,000.00, had been made to the Appellant by Mr Petrov in 2012. (The Appellant was providing evidence in relation to these loans to show how he would have been able to afford the commercial losses and low commercial profit disclosed by the figures set out in his tax return in relation to each relevant tax year, as described in the Respondents' letter to the Appellant of 15 January 2016);

(hhh) on 28 September 2016, the Respondents wrote letters to Mr Kodali and Doherty to ask for further information about the dates the Appellant had worked for Mulligan and Doherty, the pay and tax figures during those periods, whether any costs in relation to materials had been reimbursed, and the total value of materials supplied. (The letter to Doherty contained quite material errors in that it referred to the work's being for Mulligan instead of for Doherty and referred to the work's being carried out in 2014 instead of 2013, as set out in Mr Mikonis's letter);

(iii) also on 28 September 2016, the Respondents wrote to the Appellant to ask why he had not previously mentioned having worked for Mulligan or Doherty during the course of the enquiry. The Respondents informed the Appellant that they had contacted both contractors in relation to the work which the Appellant alleged that he had carried out. In relation to the alleged loans from Mr Petrov, the Respondents asked to see bank statements to evidence the existence of the loans;

(jjj) on 21 October 2016, the Appellant wrote to the Respondents to say that he had sent emails to the ADR mediator on 31 May 2016 and 28 June 2016 setting out the names of his contractors (which the mediator had confirmed she had passed on to the Respondents).

The Appellant reaffirmed that he had supplied and paid for his own materials and provided the dates for which he had worked for the two contractors.

Finally, the Appellant said that the loans he had received from Mr Petrov had been advanced and repaid in cash;

(kkk) on 25 October 2015, a Mr Paul Cook, referring to himself as a site manager for Doherty, emailed the Respondents to confirm that the Appellant had worked for Doherty from October 2012 to March 2013, that the Appellant had supplied his own materials, that these had cost just under £18,000, and that the Appellant had not been reimbursed for the materials. However, Mr Cook said that he could not provide pay and tax figures in relation to the Appellant, on the grounds that it had been over three years since the Appellant had worked for Doherty;

(lll) on 27 October 2015, the Respondents wrote to Doherty, to ask why the company had retained information in relation to the dates on which the Appellant had worked for Doherty and the value of materials supplied, but not information relating to pay or tax.

The Respondents asked Doherty for its contractor reference so that it would be able to check the figures which had been supplied to the Respondents by the Appellant and for further details on the sites on which the Appellant had worked for Doherty.

Finally, the Respondents asked why both Mr Mikonis and Mr Cook were described as site managers for Doherty in the communications which had been sent by Doherty.

The documents bundle does not contain any response to this letter;

(mmm) on 21 November 2016, the Respondents wrote to the Appellant to inform him that the Respondents would not be able to make deductions for the materials that had been quoted by Mulligan or Doherty. This was because, in relation to Mulligan, no response had been received from Mr Kodali to the Respondents' letter of 28 September 2016 and, in relation to Doherty, Doherty had failed to provide the Respondents with details of the Appellant's pay and tax deductions and, as deductions could be made only from gross pay figures, no deduction could be claimed in the absence of that information.

The Respondents added that the pay from both contractors, together with the related tax deducted, had not been included in the Appellant's tax returns and that the Respondents had been unable to verify the contractors against the records held by the Respondents. The Respondents concluded by saying that, in order to consider an adjustment so as to include the figures from Mulligan and Doherty, they would need evidence directly from the contractors of pay, materials and tax deducted, bank statements from the Appellant for the periods 6 April 2010 to 5 April 2014 for each account held and contact details for the contractor/owner of each of Mulligan and Doherty; and

(nnn) on 17 December 2016, the Appellant wrote to the Respondents to say that his bank account had been closed in summer 2013, that he did not keep details of his bank account and that he relied on cash to purchase his materials. He provided the contact details for the site managers of both companies.

8. I have set out the chain of correspondence in some detail because I did not have the benefit of hearing from the Appellant directly at the hearing of the appeal and therefore, apart from his own written statement of case of 31 January 2019 and two emails from him to the First-tier Tribunal immediately prior to and immediately following the hearing, the content of the correspondence is my only means of ascertaining the Appellant's position in relation to the appeal.

9. As regards the additional material referred to in paragraph 8 above:

(a) on 31 January 2019, the Appellant submitted his own statement of case in relation to the appeal to the First-tier Tribunal. He said in that statement of case that he had sent the original documents in relation to his business expenses in respect of each tax year to the Respondents by recorded delivery and that he had subsequently provided to the Respondents receipts in relation to such postings. He added that he had tried as hard as he could to locate some of the contractors for whom he had worked in the relevant tax years but that the contractors were hard to trace. He had, however, located two of the contractors and given their names to the Respondents and those two contractors had subsequently confirmed to the Respondents information in relation to his materials;

(b) on 13 February 2019, the Appellant sent an email to the First-tier Tribunal to say that he had not received from the Respondents the documents bundle, authorities bundle and statement of case which the

Respondents were required to deliver to him 14 days prior to the hearing and to mention earlier defaults by the Respondents in complying with the procedural rules of the First-tier Tribunal; and

(c) on 18 February 2019, the Appellant sent a further email to the Respondents and the First-tier Tribunal to reiterate that the Respondents had failed to deliver the documents bundle for the hearing by the due date.

Should the Respondents be barred from the proceedings?

10. It is apparent both from the content of the correspondence mentioned in paragraph 7 above and from the Appellant's written submissions to the First-tier Tribunal mentioned in paragraph 9 above that the Appellant considers that the Respondents have not acted fairly towards him in relation to his tax affairs, both in the course of the enquiry which has led to the appeal and in the course of the proceedings in the appeal.

11. In relation to the former, I think that the Respondents have made some errors in the way in which they have dealt with the investigation into the Appellant and the ensuing assessments, closure notice and penalties. For instance, they could have shown greater expedition in dealing with the Appellant at the end of 2013 and the beginning of 2014 (when two of their letters told the Appellant not to contact them for at least six weeks), some of their letters contained errors – such as the reference to Mulligan instead of Doherty in their letter to Doherty of 28 September 2016 – and, by their own admission, they issued invalid revised discovery assessments to the Appellant in November 2015 when the original discovery assessments of October 2015 had not yet been determined (see the review conclusion letter of 23 March 2016). In addition, it was not appropriate for the Respondents, in issuing the discovery assessments and closure notice in October 2015, to have accepted the Appellant's figures for turnover in respect of each tax year to which the discovery assessments related but not the Appellant's figures for tax deducted in respect of those tax years. That was an inconsistency which was plainly unfair and which the Respondents ultimately corrected.

12. However, the above matters relate to the conduct of the Respondents in the period preceding the date on which notice of the appeal was given to the First-tier Tribunal – that is to say, during the period of the enquiry that led to the review conclusion letter which is the subject of the appeal. Any review of that conduct is not something which is within the jurisdiction of the First-tier Tribunal. Insofar as the Appellant has a justifiable grievance against the Respondents in relation to the conduct of the enquiry which has led to the review conclusion letter, the appropriate manner in which to progress that grievance is by following the formal complaints procedure in relation to the Respondents' conduct and, if he considers it necessary, ultimately pursuing a claim for judicial review. That conduct is not a relevant factor in the determination of the issues of law which are relevant to the appeal.

13. The above is not true of the conduct of the Respondents in relation to the appeal itself and, as the Appellant has fairly pointed out, the Respondents have, on more than one occasion, failed to comply with directions issued by the First-tier Tribunal in relation to the appeal.

14. By directions issued on 16 June 2016, the Respondents were required to deliver their statement of case to the Appellant by 4 November 2016. On 27 October 2016, the Respondents applied successfully for that date to be deferred until 1 February 2017 because the parties were in discussions and it was hoped that the present proceedings could be avoided. However, the Respondents then failed to comply with the revised deadline, which led the First-tier Tribunal to send an admonitory letter on 25 March 2017 pointing out that the Respondents were in breach of the directions and requiring them to produce their statement of case within 14 days. In the event, the Respondents did not provide their statement of case until 12 May 2017, more than a month after the revised deadline.

15. Similarly, by directions of 13 January 2018 which were varied by the First-tier Tribunal on 16 October 2018, the Respondents were required to deliver to the Appellant, on or before 14 days before the hearing, its skeleton argument, together with the documents bundle and the authorities bundle. This meant that the relevant documents should have been sent to the Appellant by no later than 1 February 2019. In fact, the documents bundle was not sent to the Appellant until 8 February 2019 and, as the Appellant has pointed out, once one allows time for post to be delivered, the Appellant would not have received the documents bundle until four or five days before the hearing. In addition, the Respondents did not deliver to the Appellant before the hearing either the authorities bundle or their skeleton argument.

16. In his email to the First-tier Tribunal of 13 February 2019, the Appellant applied for the Respondents to be barred from taking further part in the proceedings. I agree with the Appellant that both parties to proceedings before the First Tier Tribunal are required to comply with the rules in relation to proceedings before the First-tier Tribunal as set out in the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (the "Tribunal Rules"). It is not appropriate for the Respondents in this case to have been in default of their obligations under the Tribunal Rules at all, let alone on more than one occasion. I have therefore given serious consideration as to whether the defaults by the Respondents outlined above are such that I should bar the Respondents from taking further part in the proceedings and summarily determine all of the issues in the appeal against the Respondents pursuant to Rule 8 of the Tribunal Rules.

17. I have ultimately concluded, on balance, that I should not do that. This is because, in relation to the Respondents' failures described above, I can bar the Respondents from taking further part in the proceedings (under Rule 8(3)(b) of the Tribunal Rules, as the same is applied to the Respondents by Rule 8(7) of the Tribunal Rules) only if the Respondents have "failed to co-operate with the Tribunal to such an extent that the Tribunal cannot deal with the proceedings fairly and justly". After thoroughly reviewing the documents bundle (and, in particular, the correspondence which has passed between the parties in relation to the matters which are the subject of the appeal) and after reading the Appellant's own statement of case dated 31 January 2019, I believe that the failures on the part of the Respondents which I have outlined above have not prevented the Appellant from putting his case fairly and in full to the First-tier Tribunal and responding to the allegations that have been made by the Respondents in relation to the matters which are in dispute between the parties. Accordingly, those failures do not prevent me from dealing with the substantive issues in the appeal fairly and justly.

18. In particular, I am satisfied that, given all that has passed between the parties during the course of the enquiry and subsequently, since notice of the appeal was given by the Appellant to the First-tier Tribunal, the Appellant was sufficiently apprised of the Respondents' case and arguments in the appeal prior to the hearing and was not prevented by the failures of the Respondents from challenging that case and those arguments in his own communications to the First-tier Tribunal prior to the hearing. I have therefore decided that those failures do not preclude me from dealing with the proceedings fairly and justly and therefore that I should not bar the Respondents from taking further part in the proceedings (or summarily determine any of the issues in the appeal against the Respondents). Having said that, I consider that the Respondents have been deficient in the manner in which they have conducted the appeal and that they should take steps to ensure that the same does not happen in other cases.

The issues

19. The appeal raises three questions of law, as follows:

> (a) were the discovery assessments in respect of the tax years ending 5 April 2011, 5 April 2012 and 5 April 2013 properly made? In other words, did the Respondents satisfy the conditions which are set out in Section 29 of the Taxes Management Act 1970 (the "TMA") in relation to each of those assessments?
>
> (b) is the outcome shown in any of the above assessments or in the closure notice issued in respect of the tax year ending 5 April 2014 excessive? and
>
> (c) have the penalties under Schedule 24 of the Finance Act 2007 ("Schedule 24") been properly imposed?

20. The burden of proof in relation to the questions outlined in paragraphs 19(a) and 19(c) above is on the Respondents. In other words, it is for the Respondents to prove that, on the balance of probabilities, the discovery assessments were properly made and the penalties were properly imposed.

21. Conversely, the burden of proof in relation to the question outlined in paragraph 19(b) above is on the Appellant. In other words, it is for the Appellant to prove that, on the balance of probabilities, one or more of the assessments or the closure notice was excessive.

Findings of fact

22. All three of the questions outlined in paragraph 19 above turn on findings of fact in relation to the manner in which the Appellant has conducted his tax affairs in respect of the tax years in question. I therefore think that, before addressing each of the issues in turn, it would be helpful for me to set out my conclusions on that subject.

23. Before doing so, I should make it clear that I have no doubt that the Appellant genuinely believes that he has done all that he can to manage his tax affairs in an appropriate manner. However, I do not think that that conclusion is supported by the facts, as outlined in the correspondence which has passed between the parties. It is a

pity that the Appellant chose not to attend the hearing to present his case and give evidence on his own behalf and did not produce any witnesses who might have supported his submissions. For instance, he might have been able to proffer an explanation for some of the inconsistencies in his position which I have noted below and his witnesses might have been able to support his contention that he incurred meaningful amounts on materials during the tax years in question.

24. Based on the material with which I have been provided, I would make the following preliminary observations in relation to the facts in this case:

(a) the Appellant failed to keep copies of the CIS payment and deduction statements, the receipts for materials and the list of clients in respect of the tax year ending 5 April 2013 which he says that he sent to the Respondents on 8 April 2013 (or indeed of any payment and deduction statements, receipts for materials or lists of clients in respect of any of the other tax years which are relevant to the appeal and which he claims to have sent to the Respondents by recorded delivery, as to which, see paragraph 24(b) below).

The Appellant repeatedly asked the Respondents to find the letter of 8 April 2013 during the course of the protracted correspondence described in paragraph 7 above and the Respondents repeatedly said that they could not find it. Attempts were made at, and immediately following, the hearing to trace, on the Royal Mail's system, the person who signed for the letter but, since it is now almost six years since the letter was sent, those attempts failed (somewhat inevitably).

It is a pity that neither party thought it appropriate at the time when the missing letter was first mentioned to use the recorded delivery receipt to ascertain who at the Respondents had signed for the delivery of the letter. Had that been done, so that the Respondents then knew the name of the person in question, the process of tracking down the letter would have been made easier;

(b) in relation to the tax years other than the tax year ending 5 April 2013, although the Appellant has repeatedly alleged that he has sent to the Respondents, by recorded delivery, all of the CIS payment and deduction statements, receipts for materials and lists of clients in respect of those tax years – see the Appellant's letters to the Respondents of 2 November 2015 and 13 March 2016 – the documents bundle does not contain a recorded delivery slip in respect of any of those tax years.

The only recorded delivery slip which is in the documents bundle is the one in relation to the letter of 8 April 2013 and the documentation included in that letter related only to the tax year ending 5 April 2013 – see the Appellant's letter to the Respondents of 26 September 2013.

In his letter to the Respondents of 2 November 2015, the Appellant said that he was enclosing the evidence that he had sent the documentation in respect of each of the other tax years to the Respondents by recorded delivery but no such evidence was contained within the documents bundle and the Respondents in their letter to the Appellant of 20 November 2015 denied ever having received any such documentation;

(c) in his response of 14 November 2013 to the request made by the Respondents on 8 November 2013 for the names and addresses of all the contractors for whom the Appellant had worked during the tax year ending 5 April 2013, the Appellant provided only one name – that is to say, FIC. He then provided further names in his letter of 27 December 2013. Neither of those communications mentioned JGI or SIC, for whom the Appellant had also worked during the relevant tax year, as confirmed by the Respondents in their letter of 16 January 2016.

More recently, in his letters of 2 September 2016 and 21 October 2016, the Appellant alleged that he worked for Doherty during the relevant period – see also Doherty's email of 25 October 2015.

I believe that, when the original enquiry was made of him on 8 November 2013, the Appellant should have been able to provide the Respondents with the names of all of the contractors for whom he had worked during the tax year ending 5 April 2013, which had ended only a few months previously.

The fact that he did not casts doubt on the Appellant's submissions in relation to the identity of his contractors over the tax year ending 5 April 2013.

For instance, I find it hard to understand how, having worked for Doherty for six months between October 2012 and March 2013 (as set out in Doherty's email of 25 October 2015 and the Appellant's letter to the Respondents of 21 October 2016), the Appellant failed to mention Doherty in either of his responses to the Respondents at the end of 2013 in relation to the identity of his contractors during the tax year in question or even in his letter of 22 January 2014 in which he showed that he understood that the Respondents wanted details of all of the contractors for whom he had worked during the tax year in question. At the time of those responses, it was only a matter of months since the Appellant had apparently finished a six-month contract with Doherty and it is inexplicable that the Appellant failed to remember this;

(d) more generally, in relation to both Mulligan and Doherty, although the Appellant has produced letters from a former employee of Mulligan and an employee of Doherty attesting to the fact that the Appellant incurred significant expenditure on materials – see his letter of 2 September 2016 and its enclosures – the quality of that evidence is weak.

In the first place, no response from Mr Kodali was ever received by the Respondents when they sought to follow up with him on 28 September 2016 in relation to that expenditure. In the second place, although the Respondents received an initial response to their letter of 28 September 2016 from Doherty on 25 October 2016, that response was puzzling in that, as the Respondents fairly pointed out in their follow-up to Doherty of 27 October 2016, Doherty appeared to have a perfect recollection of the amount which the Appellant had spent on materials but no recollection (or records) in relation to the amounts which they had paid to the Appellant. The documents bundle does not contain any response from Doherty to that follow-up letter and the observation which it contained.

In addition, the Appellant did not include any income from either Mulligan or Doherty in his tax returns (see the Respondents' letter of 21 November 2016 which has not been contradicted by the Appellant in any of his correspondence or submissions);

(e) so far as the other contractors are concerned, I share the reservations of the Respondents (as set out in paragraphs 56 to 60 of the review conclusion letter) as to whether the Appellant ever incurred significant amounts on materials in relation to his work for those contractors.

First, I do not believe that the Appellant has adequately explained how he managed to transport materials of such significance on public transport or in a private vehicle.

Secondly, I am not convinced that the Appellant has adequately explained how he was able to support the commercial losses and minimal commercial profit which he made in respect of each tax year based on his figures for expenses – see the Respondents' letter of 15 January 2016.

The Appellant said initially that he had used his own savings to do so – see his letter of 9 February 2016. Subsequently, the Appellant produced a copy of a loan agreement with Mr Petrov and said that he had received loans from Mr Petrov in both 2012 and 2013 – see his letter of 2 September 2016.

The Appellant has provided no evidence of what form his savings took, how those savings had accrued or the amount of those savings. As for the loans, the Appellant said that the 2012 loan had been discharged (and the 2013 loan would have needed to have been discharged). Thus, they would not, in and of themselves, amount to a permanent substitute for the lack of profitability which the Appellant's figures disclose.

Thirdly, the Respondents' enquiries of each of FIC, Shakespeare, RMF, JGI and SIC produced no response from FIC, RMF or SIC, whilst the response from JGI was that the Appellant had incurred only £7.99 on materials (for which he had been reimbursed) and the response from Shakespeare was that the Appellant had not supplied any materials at all.

Similarly, SCI's response of 10 April 2015 to the Respondents' query in relation to the same subject was to say that all materials used by the Appellant had been supplied by the main contractor;

(f) the Appellant has failed to keep bank statements or to obtain copies of those bank statements from his bank. Even accepting the Appellant's assertion that many of his transactions took place in cash, one would expect those bank statements to have provided at least some information in relation to the business of the Appellant over the period in question. I do not understand why the Appellant did not request such copies from his bank and pass them on to the Respondents;

(g) the fact that so many of the Appellant's transactions took place in cash made it all the more important that the Appellant should retain invoices and receipts to show that he had incurred expenditure on materials.

The Appellant claims, first, that he sent all of that documentation to the Respondents by recorded delivery – see his letters of 2 November 2015 and 13 March 2016 – and I have already mentioned in paragraph 24(b) above that the documents bundle contains no evidence of that and that the Respondents deny having received the documentation.

However, he also claims that all of his business records were destroyed by a flood at his home in July 2014. The Appellant has provided no evidence of this in the form of photographs or any insurance claim. Moreover, after saying that all of his business documents had been destroyed by the flood (see his letters of 10 December 2014 and 15 January 2015), the Appellant then managed to produce 18 payslips from SM on 11 March 2015.

The Appellant has therefore produced no evidence of the flood and contradicted himself in relation to the extent to which the flood destroyed his business records.

In addition, as the Respondents pointed out in their letter of 18 February 2015, the Appellant made no mention of the flood when he wrote to the Respondents on 26 July 2014; and

(h) even if there had been a flood, as alleged by the Appellant, I believe that a person in his position exercising reasonable care in relation to his tax position should at that stage – ie just after the flood in July 2014 - have sought alternative evidence in relation to his income from, and expenditure on materials for, his contractors. For example, the Appellant could at that stage have asked the contractors in question to provide letters to that effect. The tax year in question had only recently ended and therefore one would have expected records in relation to the income and expenses still to be in existence.

By failing to do that, the Appellant made it less likely that he would be able to obtain the requisite evidence in due course. Thus, when the Appellant makes the fair point in his statement of case of 31 January 2019 that it is difficult at this stage to locate the contractors for whom he worked during the relevant tax years, he overlooks the fact that it has been open to him for some time to have taken the necessary steps to do that and that, by failing to act promptly, he has rendered the task more difficult, if not impossible.

25. Given the above observations, I have made the following findings of fact on the balance of probabilities:

(a) the Appellant did send to the Respondents on 8 April 2013 the originals of the CIS payment and deduction statements, the receipts for materials and the list of clients in respect of the tax year ending 5 April 2013 (see paragraph 24(a) above);

(b) the Appellant did not send to the Respondents the originals of the CIS payment and deduction statements, receipts for materials and lists of clients in respect of the other tax years (see paragraphs 24(b) and 24(g) above);

(c) the Appellant did not incur the expenditure of £5,000.00 and £18,000.00 respectively which he says that he incurred whilst working for Mulligan and Doherty and which are recorded in the letters from Mr Kodali and from Doherty (see paragraphs 24(c) and 24(d) above);

(d) the Appellant's business records were not all destroyed by a flood (see paragraph 24(g) above); and

(e) the Appellant did not incur the expenditure on materials which he claims to have incurred in relation to his work in the relevant tax years (see paragraphs 24(d) to 24(h) above).

The discovery assessments

26. The Respondents are entitled to issue a discovery assessment under Section 29 of the TMA where they discover that an existing assessment is insufficient and that insufficiency has been brought about carelessly or deliberately by the taxpayer (see Sections 29(1), 29(3) and 29(4) of the TMA). Section 118(5) of the TMA provides that a loss of tax or a situation is brought about carelessly by a person if that person fails to take reasonable care to avoid bringing about that loss of tax or situation.

27. Under Section 34 of the TMA, the Respondents are ordinarily entitled to make an assessment at any time up to four years from the end of the tax year to which the assessment relates but that is subject to, inter alia, Section 36 of the TMA, pursuant to which, in the case of an under-assessment brought about carelessly, the time limit is extended to six years from the end of the tax year to which the assessment relates.

28. In this case, the assessments in respect of the tax years ending 5 April 2012 and 5 April 2013 were made in October 2015 and therefore within the general four-year time limit set out in Section 34 of the TMA.

29. The assessment in respect of the tax year ending 5 April 2011, which was also made in October 2015, was outside the general four-year time limit set out in Section 34 of the TMA but within the extended six-year time limit set out in Section 36 of the TMA. Therefore, it is necessary to determine whether the Respondents have established, on the balance of probabilities, that the Appellant has been careless in relation to his tax return in respect of that tax year. This means that I need to ask myself whether the Appellant failed to take reasonable care to avoid the insufficiency of tax which appeared in his self-assessment tax return in respect of the tax year ending 5 April 2011.

30. Based on my observations in paragraph 24 above and my findings of fact in paragraph 25 above, I consider that the Appellant did not adopt the reasonable care in relation to the completion of his tax return in respect of that tax year which one might reasonably expect from a person in his position and was therefore careless. Some of the points specified in those paragraphs are specific to tax years other than the tax year ending 5 April 2011 (and are therefore not relevant to this question) but others are of general application (and are therefore so relevant). I consider that, to the extent that they are of general application, they show that the insufficiency in the tax which appeared in the Appellant's self-assessment tax return in respect of the tax year ending 5 April 2011 was brought about carelessly by the Appellant.

31. It follows from the above that, in my view, the discovery assessments which were made by the Respondents in relation to each of the tax years ending 5 April 2011, 5 April 2012 and 5 April 2103 complied with the requirements set out in Sections 29, 34 and 36 of the TMA and were therefore properly made.

The outcome of the closure notice and the discovery assessments

32. It is clear from the correspondence mentioned in paragraph 7 above and, in particular, the terms of the review conclusion letter, that the Respondents have accepted the figures which the Appellant has provided in his tax return in respect of each relevant tax year in relation to:

(a) his taxable income;

(b) the tax which has been deducted from that taxable income by the contractors for whom he worked; and

(c) his deductible expenses, with the exception of the deductions which he has claimed in respect of his materials and his interest costs.

33. Just pausing there, I think I should note that the Respondents have arguably been very generous to the Appellant in adopting that position. In particular, the Respondents have:

(a) accepted the figures for income and tax deducted which the Appellant has provided notwithstanding that there have been indications in the course of the enquiry that not all of the Appellant's income was included in his returns – see, for example, the discrepancies noted in the Respondents' letters of 16 January 2014 and 27 October 2015 and the confusion revealed by the correspondence over the contractors for whom the Appellant had worked in the tax year ending 5 April 2013; and

(b) accepted the claims to deduct expenditure other than the expenditure on materials and the interest costs, as described above, notwithstanding the absence of any receipts or other documentary evidence in relation to those costs.

34. Leaving that aside, it follows from the point made in paragraph 32 above that the only issue for me to determine in this section of my decision is whether the Respondents were correct in denying the Appellant relief for the cost of materials and his interest costs. That, in turn, depends on whether the Appellant has discharged the burden of establishing that (in the case of the expenditure on materials) the relevant costs were incurred and (in the case of the interest) the interest which he incurred was incurred for business purposes.

35. Based on my observations in paragraph 24 above and my findings of fact in paragraph 25 above, I believe that the Appellant has failed to establish that he incurred the expenses on materials which he claims to have done. In the absence of any receipts or other supporting evidence, I am unable to conclude that, on the balance of probabilities, the Appellant incurred the relevant expenditure.

36. The position in relation to the interest costs is very different because, as I understand the Respondents' position, they are not questioning whether the Appellant

incurred the relevant expenditure but rather saying that, because they are denying the Appellant relief for the cost of materials, it is "reasonable also to disallow the amounts claimed for interest".

37. I am afraid that I do not follow the logic of that position. Once it is accepted that the Appellant incurred certain deductible expenditure in the course of carrying on his business – which is to say, the expenses claimed by the Appellant in respect of each tax year other than the cost of materials and the interest costs themselves – then why does it follow that the interest which the Appellant is accepted by the Respondents as having incurred should be attributed wholly to the cost of materials which the Respondents say were not incurred? It seems to me that a more logical conclusion to be drawn from the propositions that:

(a) the Appellant did not incur any expenses in relation to materials;

(b) the Appellant did incur the other business expenses for which he has claimed (interest costs aside); and

(c) the Appellant did incur the interest costs,

is that the interest costs must have been attributable to those expenses which the Appellant actually did incur, whether those expenses were private expenses incurred for non-business purposes or business expenses incurred for business purposes.

38. And, since the Respondents have not put forward any logical reason why the interest costs in question should be attributed to the Appellant's private expenses, as opposed to the Appellant's business expenses, it seems to me that it would be unreasonable to deny the Appellant relief for the interest costs on that basis.

39. My conclusion therefore is that;

(a) whilst the Appellant has not discharged the burden of establishing that he incurred the cost of materials, and therefore that no adjustment to the discovery assessments in respect of the tax years ending 5 April 2011, 5 April 2012 and 5 April 2013 and no adjustment to the amendment to the Appellant's self-assessment tax return in respect of the tax year ending 5 April 2014 resulting from the closure notice (in each case, as revised by the review conclusion letter) should be made to allow the Appellant relief for those costs;

(b) such an adjustment should be made to allow the Appellant relief for the Appellant's interest costs in respect of each such tax year.

40. The discovery assessments and the amendment to the Appellant's self-assessment resulting from the closure notice (in each case, as revised by the review conclusion letter) should be amended to reflect the conclusion set out in paragraph 39(b) above but are otherwise upheld and stand good.

<u>The penalties</u>

41. Where a person carelessly makes an inaccurate tax return which understates his or her liability to income tax or inflates his or her claim to a repayment of tax, a penalty is payable under paragraph 1 of Schedule 24.

42. A person is "careless" for this purpose if the inaccuracy is due to a failure to take reasonable care (see paragraph 3 of Schedule 24).

43. The penalty which becomes due in that case is equal to 30% of the "potential lost revenue" (in relation to a tax return in respect of a tax year ending on or before 5 April 2011) and either 30%, 45% or 60% of the "potential lost revenue", depending on whether the inaccuracy falls within category 1, 2 or 3, (in relation to a tax return in respect of later tax years) (see paragraphs 4 of Schedule 24).

44. A matter such the present one, which does not involve any offshore element, falls within category 1 (see paragraph 4A of Schedule 24).

45. The "potential lost revenue" is "the additional amount due or payable in respect of tax as a result of correcting the inaccuracy or assessment" (see paragraphs 5 et seq. of Schedule 24). Paragraph 5(2) of Schedule 24 provides that the additional tax which becomes due or payable by reason of correcting the inaccuracy also includes amounts of tax which have been repaid to the taxpayer and amounts of tax which, but for the correction of the inaccuracy, would have been so repaid.

46. There are provisions in Schedule 24 which provide for a penalty to be reduced depending on whether the relevant inaccuracy is disclosed, the quality of the disclosure and whether the disclosure is prompted or unprompted (see paragraphs 9 and 10 of Schedule 24). In the case of a careless inaccuracy falling within category 1, those provisions can result in a reduction from 30% to 15% for a prompted disclosure or 0% for an unprompted disclosure, in each case depending on the quality of the disclosure.

47. Paragraph 11 of Schedule 24 allows the Respondents to reduce a penalty if they think it right because of special circumstances. For this purpose, "special circumstances" do not include the ability to pay (see paragraph 11(2) of Schedule 24).

48. Paragraph 13 of Schedule 24 states that, where a person becomes liable for a penalty under paragraph 1 of the schedule, the Respondents shall assess the penalty, notify the taxpayer and state in the notice a tax period in respect of which the penalty is assessed or the tax year to which the penalty relates. It also states that the penalty assessment must be made before the end of the period of 12 months beginning with the end of the appeal period for the decision correcting the inaccuracy or, if there is no assessment to the tax concerned, the date on which the inaccuracy is corrected.

49. Paragraph 14 of Schedule 24 allows the Respondents to suspend all or part of a penalty under paragraph 1 of the schedule for careless inaccuracy for up to two years, subject to the satisfaction by the taxpayer of certain conditions.

50. Paragraph 16 of Schedule 24 sets out the rights of the taxpayer to appeal against a penalty, the amount of a penalty, a refusal to suspend a penalty or the conditions of suspension and paragraph 17 of Schedule 24 provides that, in relation to any appeal against a penalty or the amount of a penalty, the First-tier Tribunal may affirm or cancel the Respondents' decision or substitute for the Respondents' decision another decision that the Respondents had the power to make

51. The Respondents sent a penalty explanation notice to the Appellant on 18 November 2015. This notice set out the amounts of the penalties which the Respondents had assessed and the tax years to which those penalties related. In addition, the assessments to the penalties were made within 12 months of the end of the appeal period in relation to the decisions which corrected the inaccuracies in the Appellant's tax returns. Accordingly, the terms of paragraph 13 of Schedule 24 have been satisfied in relation to the penalties.

52. The Respondents explained in their penalty explanation notice that they considered the behaviour which has led to the inaccuracies in this case to have been careless and the Appellant's disclosure to have been prompted (as opposed to unprompted).

53. I agree with both of those conclusions.

54. In relation to whether or not the Appellant was careless – that is to say, failed to take reasonable care – I believe that it was reasonable to expect the Appellant to have retained the business records which were needed in order to evidence the contractors for whom he had worked in the relevant tax years, the income he had received from those contractors, the tax which had been deducted from that income and, most importantly in the context of this appeal, the deductions which he was claiming. In relation to whether or not the disclosure was prompted or unprompted, I consider that the former is the case because the Appellant did not tell the Respondents about the inaccuracy before the Respondents discovered it.

55. The above means that a penalty in the range of 15% to 30% of the potential lost revenue is due under Schedule 24.

56. As the Respondents have explained in their penalty explanation notice, their practice is to adopt a sliding scale to reflect the quality of the disclosure (or "telling", "helping" and "giving", as it is referred to in the notice). Applying that scale in the present case, they have determined that the penalty in respect of each tax year should be equal to 24% of the potential lost revenue – that is to say, 6% below the maximum possible penalty and 9% above the minimum possible penalty. The basis for their conclusion is that:

> (a) whilst the Appellant "initially provided a breakdown of expenses [, he did] not however …do so for the earlier periods"; and
>
> (b) whilst the Appellant provided the Respondents with some information in relation to his business, he did not have the records to support his claims.

57. Save in one minor respect, I agree with the Respondents' conclusion in this regard. The one possible exception is that the language to which I have referred in paragraph 56(a) above might be read as saying that the Appellant provided a breakdown of his expenses only in relation to the tax year ending 5 April 2014 and not in relation to the three earlier tax years. In fact, the Appellant provided a breakdown of his expenses in respect of both the tax year ending 5 April 2014 and the tax year ending 5 April 2013. It was only in relation to the tax years ending 5 April 2011 and 5 April 2012 that he did not provide a breakdown. So, to that extent, the language used is potentially inaccurate. Nevertheless, I do not think that that potential

minor error is sufficient to disturb the conclusion reached by the Respondents in relation to the appropriate percentage to be applied in calculating the penalties.

58. Finally, the Respondents concluded that there were no special circumstances in this case which might justify a reduction in the penalties and I agree with that conclusion too.

59. The figures which are set out in relation to the penalties in paragraph 74 of the review conclusion letter appear to me to be correct. In particular, I agree with the Respondents that, once one takes into account, as part of the additional tax which becomes due or payable by reason of correcting the inaccuracy, both amounts of tax which have been repaid to the Appellant in respect of the tax years in question and amounts of tax which, but for the correction of the inaccuracy, would have been so repaid (as is required by paragraph 5(2) of Schedule 24), the potential lost revenue in respect of each tax year is as set out in the table which appears in paragraph 74 of the review conclusion letter.

60. The above means that the only adjustment which needs to be made to the penalties is to reduce the penalties to reflect the conclusions set out in paragraphs 39(b) and 40 above in relation to the deductions for interest. The penalties will remain suspended provided that the Appellant continues to meet the penalty suspension conditions to which he has agreed.

Conclusion

61. In conclusion, I consider that the Appellant's appeal against the discovery assessments and the amended self-assessment should be upheld solely to the extent that it relates to the denial of relief for his interest costs (which should be allowed as deductions) and that the penalties should be reduced to reflect the reduction in potential lost revenue which stems from those adjustments. The penalties will remain suspended provided that the Appellant continues to meet the penalty suspension conditions to which he has agreed.

Right of appeal

62. 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 Rules. 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.

**TONY BEARE**
**TRIBUNAL JUDGE**

**RELEASE DATE: 04 MARCH 2019**