[2019] UKFTT 713 (TC)

TC07485

INCOME TAX/VALUE ADDED TAX – whether Appellant had undeclared trading income – time limit for issuing discovery assessment – whether Appellant's VAT returns were inaccurate – whether Appellant liable for penalty for failure to file self-assessment tax returns – s 93 Taxes Management Act 1970 – whether Appellant's conduct dishonest/deliberate – s 60 Value Added Tax Act 1994 – schedule 24 Finance Act 2007 – appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2016/04277

BETWEEN

GOLAMREZA QOLAMINEJITE
(AKA ANTHONY COOPER) **Appellant**

-and-

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

TRIBUNAL: JUDGE ROBIN VOS
DR CHRISTINA HILL WILLIAMS
DL M.A. F.R.G.S F.R.S.A.

Sitting in public at Taylor House, London on 14-15 October 2019

Ross Birkbeck, Counsel for the Appellant

Ashley Wilkinson, litigator of HM Revenue and Customs' Solicitor's Office, for the Respondents

DECISION

INTRODUCTION

1. The Appellant, Mr Qolaminejite prefers to be known as Anthony Cooper. In this decision we therefore refer to him as Mr Cooper.

2. Prompted by an application by Mr Cooper in April 2010 to register his business for VAT, HMRC launched an investigation into his business affairs, initially in relation to VAT but extended in August 2011 to cover direct tax issues as well. This later investigation was conducted under Code of Practice 9 (which applies where there is a suspicion of fraud).

3. As a result of these investigations, in December 2013 HMRC issued discovery assessments for each of the tax years ended 5 April 2007 - 5 April 2010 totalling approximately £435,000, assessments for associated penalties for failure to file tax returns for the relevant years totalling around £215,000, a VAT assessment for the 06/10 accounting period of just under £70,000 and, as they believed Mr Cooper had been dishonest, charged a civil evasion penalty for that VAT period of just over £30,000.

4. In addition, HMRC reduced Mr Cooper's claim for a repayment of VAT for the 09/10 VAT period by approximately £65,000. They charged him a penalty of almost £31,000 in respect of this inaccuracy which they considered to be deliberate.

5. Mr Cooper appeals against all of these assessments and penalties.

LATE APPEAL

6. Mr Cooper notified his appeal to the Tribunal outside the statutory time limit. The Tribunal has however previously given permission for Mr Cooper to notify his appeals out of time and so this was not something we needed to deal with at the hearing.

WRITTEN SUBMISSIONS

7. The Tribunal requested the parties to make written submissions dealing with the question as to whether, in deciding whether Mr Cooper had been overcharged by the discovery assessments, it was able to take into account points not put in issue or pleaded by either party. Both parties have provided such submissions and this decision takes those submissions into account.

THE EVIDENCE

8. The Tribunal was provided with four bundles of documents and correspondence. Mr Birkbeck applied at the beginning of the hearing on behalf of Mr Cooper for a further small folder of documents to be admitted as part of the evidence. These documents were all provided in support of statements made by Mr Cooper about the source of various payments into his bank accounts. The bulk of the documents had been provided to HMRC on 7 October 2019 (i.e. a week before the hearing). A small number of documents however had only been provided to HMRC the day before the hearing.

9. Based on the decision of the High Court in *Mobile Export 365 Limited v HMRC* [2007] EWHC 1737 (Ch) and the decision of the First-tier Tribunal in *Earthshine Limited v HMRC* [2010] UKFTT 67 (TC), Mr Birkbeck submitted that, if the evidence is relevant, there is a presumption that it should be admitted unless there are compelling reasons why it should be excluded.

10. In this context, Mr Birkbeck submits that there were no compelling reasons to exclude the evidence. In particular, he argues that this is not a case where HMRC have been ambushed or surprised as the evidence simply supports what Mr Cooper has already said. In addition, it would not be expected that HMRC would seek to produce any evidence to rebut the evidence

which he asks the Tribunal to admit given that the burden of proof is on Mr Cooper and he is the only person in possession of the relevant evidence.

11. Mr Wilkinson objected on behalf of HMRC to the new evidence being admitted. He made the point that, unlike in *Earthshine*, HMRC had never seen the documents before and therefore could be said to be surprised or ambushed by the new evidence. In addition, although he accepted that HMRC would not be looking to provide any contrary evidence, he argued that giving HMRC time for rebuttal included not only producing other evidence but also having time to formulate their submissions based on the new evidence.

12. Our decision was to allow the new evidence to be admitted. Most of the cases (discussed in *Earthshine*) where the Tribunal has refused to admit evidence have been in situations where the application is made after the hearing has begun and therefore has potentially affected the way in which the other party would have conducted its case.

13. In this case, the new evidence is simply intended to corroborate what Mr Cooper has already said and, for the most part, has been in the possession of HMRC for a week, which should have given them plenty of time to consider how they wished to deal with that evidence either in their submissions or in cross-examination of Mr Cooper.

14. On the second day of the hearing, Mr Birkbeck made an application for the Tribunal to admit as part of the evidence a copy of a loan agreement between Mr Cooper and a business associate of his, Mr Sami Evans. By this time, both Mr Cooper and Mr Evans had given their evidence. Mr Cooper did not attend on the second day of the hearing.

15. We refused permission for this further evidence to be admitted as it would have prejudiced HMRC in the conduct of their case given their inability to cross-examine the witnesses about the document.

16. In addition to the documentary evidence, we also heard oral evidence from Mr Cooper, Mr Evans and HMRC's investigating officer, Darren Woods.

17. It will be apparent from what we say below that, taking into account the other evidence before us, there are areas where this oral evidence has not been sufficient to discharge the burden of proof on the relevant party.

BACKGROUND FACTS

18. There are significant factual disputes in this case and we deal with those more contentious areas in other parts of our decision. The following is a summary of the background facts in relation to which there is no significant disagreement.

19. Mr Cooper came to the UK from Iran in 1996. Relatively soon after arriving in the UK, Mr Cooper stayed at a hotel in Paddington owned by Mr Evans' family. They had a shared interest in engineering, in Mr Evans' case in relation to aircraft and in Mr Cooper's case in relation to boats. They became good friends.

20. In 2003, Mr Cooper set up a business as a sole trader known as Ship & Ocean ("SO"). At around the same time, Mr Evans set up a company called Ships D & S Limited ("SDS").

21. In 2004, Mr Cooper also set up a company which was called Ship & Ocean Limited ("SOL").

22. Prior to leaving Iran, Mr Cooper had inherited valuable assets from his grandfather, mainly comprising land but also including some liquid assets.

23. Mr Cooper submitted a self-assessment tax return for the tax year ended 5 April 2004. This disclosed a certain amount of trading income which was described as work as a handyman but in fact related to boat repairs carried out by Mr Cooper trading as SO.

24. Mr Cooper did not submit any further self-assessment tax returns during the period in question.

25. SOL was listed at Companies House as a dormant company and has never filed any UK tax returns. It was dissolved in January 2010.

26. Mr Cooper initially rented an office for SO in Epping.

27. In October 2007, either SO or SOL (as to which, see further below) entered into an agreement with Pars Company in Iran for the sale of three barges to Pars Company for $9 million. A deposit of 15% (approximately £730,000) was paid into SOL's bank account on 31 October 2007. The following day, Mr Cooper transferred £150,000 into his personal bank accounts, £450,000 to his wife as part of a divorce settlement and used £67,500 to purchase a Bentley. By mid-December 2007, SOL's account was overdrawn.

28. At some point in 2008, Mr Cooper rented industrial premises in Epping for SO from Padfield (Hayleys) Limited ("Padfield").

29. On 15 February 2010, SO entered into a contract to manufacture and sell four hovercraft to Mr Evans' company, SDS for a total of £100,000 (£85,106.38 plus VAT of £14,893.62).

30. On the same day, SO contracted to manufacture and sell to SDS a tug yacht for a total of £340,000 (£289,361.70 plus £50,638.30 of VAT).

31. On 9 April 2010, Mr Cooper applied for SO to be registered for VAT with effect from 15 April 2007. This was initially resisted by HMRC but in June 2010 they ultimately registered SO for VAT with effect from 15 April 2007 as requested with the first VAT return to cover the period from 15 April 2007 to 30 June 2010.

32. On 5 May 2010, SO issued an invoice to World Budget Travel 4 All (another company owned by Mr Evans) for the sale of a hovercraft plug for £25,000 (£21,276.60 plus £3,723.40 of VAT).

33. SDS made an initial payment of £20,000 for the hovercraft (20% of the total) and £17,000 for the tug yacht (5% of the total) on or around 25 February 2010. In both cases, the amounts paid were inclusive of VAT.

34. SDS claimed repayment of the input tax in relation to the four hovercraft and the tug yacht totalling £65,598.38. This was paid to SDS by HMRC.

35. Out of this, SDS paid £61,500 to Mr Cooper on 29 June 2010.

36. Mr Cooper did not include the full amount of the invoices for the sale of the hovercraft or the tug yacht on SO's VAT return for the 06/10 period of account. He also did not initially include the sale of the hovercraft plug. However the sale of the hovercraft plug was subsequently reported to HMRC for VAT purposes in August 2010.

37. On 5 September 2010, SDS issued an invoice to SO for the sale by SDS to SO of the design for a "wing in ground" ("WIG") boat for £320,000 plus VAT of £56,000 (making a total of £376,000).

38. On the same day, SDS issued an invoice to SO for the sale by SDS to SO of various model aircraft, tools and accessories for a total of £147,932.50 (£125,900 plus VAT of £22,032.50).

39. SDS included the sale of the WIG boat and the model aircraft in its VAT returns. Mr Cooper claimed repayment of the input tax on these purchases in SO's VAT return for the 09/10 VAT period.

40. HMRC refused to repay the VAT which SO had claimed pending an investigation into Mr Cooper's business affairs. As part of this investigation, an officer of HMRC visited SO's workshop in April 2011.

41. In June 2011, Padfield repossessed SO's workshop as a result of unpaid rent. They confiscated all of the contents of the workshop including the unfinished hovercraft/tug yacht.

42. As a result of the repossession by Padfield of SO's workshop, the tug/hovercraft contracts could not be completed. SDS made no further payments in respect of these contracts other than the initial payments mentioned above.

43. Mr Woods was passed the papers for the investigation by his VAT colleagues in August 2011 and opened an investigation under Code of Practice 9 in relation to Mr Cooper's direct tax liabilities.

44. Mr Woods met with Mr Cooper and his accountant on 8 March 2012 to discuss his business activities. Mr Woods prepared a note of that meeting and sent it to Mr Cooper.

45. Following that meeting, Mr Cooper provided a certain amount of information requested by Mr Woods. He also wrote to Mr Woods in May 2012 to say that the notes of the meeting were not verbatim and contained some inaccuracies.

46. Mr Woods had a further meeting with Mr Cooper on 30 January 2013 and again sent a copy of the notes of the meeting to Mr Cooper.

47. In the absence of any further information from Mr Cooper following that meeting, in December 2013 Mr Woods made the discovery assessments and the VAT assessments and imposed the penalties which are the subject of this appeal.

THE DISCOVERY ASSESSMENTS

Discovery

48. Mr Birkbeck did not take issue with the validity of the discovery assessments for each of the relevant tax years (as opposed to their quantum). He accepts that Mr Woods had made a discovery which justified the issue of the assessments. It is clear to us that, as a result of his investigations, Mr Woods had made a discovery of a suspected loss of tax and that he was entitled to make the assessments based on this discovery.

49. There are no other conditions to be satisfied under s 29 Taxes Management Act 1970 before a discovery assessment could be issued for the relevant tax years as Mr Cooper did not submit any self-assessment tax returns for those years.

50. The only issue for us to consider therefore is whether we are satisfied that Mr Cooper has been overcharged by the assessments in accordance with s 50(6) Taxes Management Act 1970.

Burden of proof

51. Both parties agree that it is up to Mr Cooper to satisfy the Tribunal on the balance of probabilities that he has been overcharged by the assessments. The way Mr Birkbeck put this is that if Mr Cooper can show that there is a better explanation for the receipts which HMRC have treated as trading income, the assessments should be reduced.

52. This is however just another way of saying the same thing. The bottom line is that Mr Cooper must be able to show on the balance of probabilities that the amounts which HMRC have assessed as trading profits of his sole trade were not in fact profits of that trade.

53. We will consider each of the relevant tax years in turn.

Tax year ended 5 April 2007

54. Although no submissions were made at the hearing, we note that HMRC's statement of case refers to the time limits for making an assessment.

55. There is no issue in relation to the assessments for the tax years ended 5 April 2008, 5 April 2009 and 5 April 2010 as the assessments were made in December 2013 which is less than six years after the end of the relevant tax year and were therefore permitted by s 36 Taxes Management Act 1970 on the basis that Mr Cooper's conduct was, at the very least, careless.

56. However, the assessment for the tax year ended 5 April 2007 was made more than six years after the end of the tax year and will therefore only be valid if it satisfies one of the conditions in s 36(1A) Taxes Management Act 1970 which allows a 20 year period for making assessments.

57. The conditions which could be relevant in this case are either that the loss of tax was brought about deliberately or that it was attributable to a failure to comply with an obligation under s 7 Taxes Management Act 1970 which requires an individual to notify HMRC of a liability to tax within a certain time period if they have not been given a notice by HMRC requiring them to file a tax return for the relevant tax year.

58. HMRC's statement of case relies on this second condition and notes that under the transitional provisions which are contained in article 7 of Finance Act 2008, Schedule 39 (Appointed Day) Transitional Provisions and Savings Order 2009 (SI 2009/403), HMRC can only rely on this condition if they also establish that the loss of tax is attributable to the taxpayer's negligent conduct. HMRC therefore assert in their statement of case that Mr Cooper's conduct was negligent.

59. However, it is clear that this condition cannot apply in this case as HMRC themselves say that Mr Cooper was issued with a notice requiring him to file a tax return for the relevant tax year. On this basis, he cannot have had an obligation to notify under s 7 Taxes Management Act 1970 and this cannot form the basis of an extended 20 year time limit.

60. The result of this is that the assessment for the tax year ended 5 April 2007 will only have been in time if we are satisfied that any loss of tax was due to Mr Cooper's deliberate conduct. It is of course up to HMRC to satisfy the Tribunal on the balance of probabilities that the loss of tax was brought about deliberately by Mr Cooper and that they therefore had the right to make the assessment.

61. We will consider first the basis of Mr Cooper's appeal against the assessment. If he is unable to establish that the amounts assessed do not represent trading income, we will return to the question as to whether the loss of tax was brought about deliberately.

62. HMRC have identified nine deposits into Mr Cooper's bank accounts which, based on the information provided by Mr Cooper, they say are unexplained. The total of these nine deposits is £47,360. HMRC have allowed various deductions for expenses and capital allowances resulting in a taxable profit for the year of £24,188.

63. Mr Birkbeck submits that, with the exception of one deposit of £25,000, the evidence shows that these deposits all represent interest free loans made by Mr Evans to Mr Cooper.

64. As far as the £25,000 is concerned, Mr Birkbeck submits that this represents the proceeds of a loan taken out by Mr Cooper from a bank.

65. Looking first at the £25,000, Mr Birkbeck took us to various documents which clearly show that, over the years, Mr Cooper had taken out a number of loans from various different financial institutions including NatWest, Santander and Welcome Finance. This showed, he said, that Mr Cooper had a pattern of funding his lifestyle by bank borrowing.

66. Mr Birkbeck also took us to the NatWest bank statement showing the receipt of the £25,000 on 28 December 2006. The reference for the payment is what appears to be a NatWest sort code. Mr Birkbeck suggested that this might indicate that the deposit represented the proceeds of a NatWest loan.

67. Mr Birkbeck also pointed out that, a few days later, there was a payment out of Mr Cooper's bank account of £485.94 to another account with the same sort code. He speculated that the payment out was to the same account as the £25,000 had come from and argued that it was inherently unlikely that, if the £25,000 represented trading income, Mr Cooper would be paying a small amount of that income back to the customer a few days later.

68. Apart from showing us that the £25,000 could not have represented the proceeds of the Welcome Finance loan which was only taken out in 2007, Mr Wilkinson did not make any specific submissions in relation to this £25,000.

69. We are not however satisfied that this £25,000 represents a bank loan.

70. It is clear that the deposit does not represent the NatWest loan which is referred to in the evidence. We have an enforcement letter in relation to the NatWest loan which gives the sort code of the relevant loan account. This is not the sort code which is the reference for the £25,000 payment into Mr Cooper's bank account. In addition, there is a separate credit of £25,000 into Mr Cooper's NatWest bank account in May 2008 which is clearly marked "new loan". The likelihood therefore is that this is the NatWest loan that is referred to in the documents before us and not the £25,000 deposit in December 2006.

71. Mr Birkbeck did not suggest that the £25,000 represented any of the other loans which are mentioned in the documents which have been provided. Whilst it is possible that Mr Cooper may have taken out loans other than those which are mentioned in these documents, we cannot be satisfied without any supporting evidence that this deposit in fact represents such a loan. Had this deposit derived from a bank loan, we would have expected Mr Cooper to be able to provide evidence of that loan.

72. Turning to the other payments, both Mr Cooper and Mr Evans gave evidence that these represented interest free loans made by way of payments of cash from Mr Evans to Mr Cooper. Mr Birkbeck noted that this has consistently been their position, referring us to Mr Cooper's statement of case, the witness statements of Mr Cooper and Mr Evans, a letter sent by Mr Cooper to HMRC in March 2011 and at Mr Cooper's first meeting with HMRC in March 2012.

73. The additional bundle of evidence also contains receipts for cash payments from Mr Evans to Mr Cooper representing interest free loans between March 2004 and October 2007.

74. In addition, Mr Birkbeck says that these loans are apparent from entries in Mr Evans' and Mr Cooper's bank statements. For example, the receipts show a loan by Mr Evans to Mr Cooper in cash of £3,300 on 17 November 2006 and there is a corresponding entry in Mr Cooper's bank account showing a deposit of £3,300 on the same date.

75. Looking at the position from the other end, the receipts show a loan of £5,000 to Mr Cooper on 19 June 2006 and Mr Evans' bank statements show cash withdrawals from his bank account totalling £15,000 on 16 June 2006.

76. Mr Birkbeck makes the point that Mr Wilkinson did not challenge Mr Cooper's and Mr Evans' evidence about the loans during cross-examination. He says there is no contrary evidence and, in particular, no evidence of any trading activities and so he concludes that it is overwhelmingly likely that these payments into Mr Cooper's bank accounts do in fact represent loans from Mr Evans.

77. Mr Wilkinson however says that Mr Cooper's statements about his source of funds have been inconsistent. In particular, he refers to the notes of the first meeting between Mr Woods

and Mr Cooper which clearly record Mr Cooper as saying that he had funded his living expenses by remittances of cash from the assets which he held in Iran. He is recorded in the notes of that meeting as having said that about £600,000 was brought to the UK between 2005 and 2011.

78. In addition, the notes show that Mr Cooper stated at the meeting that Mr Evans owed him £300,000 (being the unpaid consideration for the hovercraft/tug yacht) which Mr Wilkinson found surprising if Mr Evans had in fact been lending money to Mr Cooper.

79. Mr Wilkinson also drew our attention to a note signed by Mr Evans' father in 2005 which confirmed that he would be depositing money into Mr Evans' bank account and that Mr Evans had been instructed by his father to withdraw cash and have it delivered to his father. This note does not mention making loans to Mr Cooper.

80. Based on the evidence we have, it is difficult for us to come to a conclusion (even on the balance of probabilities) as to the source of the eight deposits in question. The result of this is that Mr Cooper has not shown on the balance of probabilities that these deposits were loans from Mr Evans or that they had some other source which does not represent trading income.

81. During cross-examination of Mr Evans, Mr Wilkinson suggested that the handwritten receipts covering a period of more than three years and all in identical form apparently using the same pen had only recently been produced. Mr Evans denied this and explained that the use of the same pen resulted from the fact that he had a pen which he always used and which he had owned since 1999.

82. However, despite this evidence, we think it is more likely than not that the receipts were produced after the event. As Mr Wilkinson has noted, they are all in identical form with the same handwriting and apparently using the same pen. Despite the fact that many of the receipts are over 15 years old, they show no sign of any wear and tear which might perhaps be expected with paper records, particularly small receipt slips as opposed to full size pages. It is also notable that the receipts were only produced on the day of the hearing. Given their importance, it seems very surprising that they would not have been made available at an earlier stage had they existed. We do not therefore give any weight to these receipts.

83. We also note that there is almost no overlap between the bank statements provided for Mr Evans and Mr Cooper. The bank statements for Mr Evans cover the period from September 2004 to August 2006. However, the earliest bank statement we have for Mr Cooper is in March 2006. That bank statement only shows one deposit into Mr Cooper's bank account which ties in with a withdrawal from Mr Evans' bank account which is the payment of £5,000 in June 2006 mentioned in paragraph 75 above. It is impossible for us to verify any of the subsequent payments as we do not have Mr Evans' bank statements covering the relevant period. It is equally impossible to verify any of the earlier payments which are said to have been loans as we do not have Mr Cooper's bank statements for those periods.

84. In addition, it is clear from the evidence that Mr Cooper consistently claimed for a number of years that the deposits into his account related to cash brought from his assets in Iran. As mentioned above, this is referred to in the notes of the first meeting with Mr Woods. It is also referred to in subsequent correspondence sent by Mr Cooper to Mr Woods on 20 October 2014 ("all my expenses throughout my stay in UK up until 2010, apart from £30,000 which came from working as a handyman, has come from my personal estate in Iran") and on 7 August 2015 ("I did mention that I had some earnings as a handyman but the core of my finance over the years was from my own estate in Iran"). There was no mention in those letters of any loans from Mr Evans.

85. Indeed, Mr Birkbeck's skeleton argument suggests that the payments came either from loans provided by Mr Evans or by remittances of cash from Iran. However, it was clear at the

hearing that Mr Cooper's position was now that all of the payments represented loans from Mr Evans rather than remittances from Iran.

86. Mr Cooper has of course said that the minutes of the first meeting with Mr Woods are inaccurate. He says that he provided details of the inaccuracies to Mr Woods in writing. Mr Woods says that he never received these corrections and there is no evidence in the documents and correspondence provided to us that Mr Cooper did in fact make any corrections to the minutes. Mr Woods also made the point that he gave Mr Cooper an opportunity at the second meeting to correct any errors in the notes of the first meeting (given that he had not received any amendments prior to the date of the second meeting). Despite this, no amendments were suggested.

87. Bearing this in mind, we have taken the notes of the meetings at face value and have had to balance this evidence against subsequent contradictory statements made by Mr Evans and Mr Cooper in their witness statements and in their oral evidence.

88. In relation to the source of the deposits in question, given the clear inconsistency between the repeated statements that Mr Cooper has funded himself out of his assets in Iran and the subsequent statements that the funds derived from loans provided by Mr Evans, we are not satisfied on the balance of probabilities that the deposits can be explained by either of these sources. Given that the explanation has changed as the years have gone by, it is perfectly possible that there could be some other explanation for the deposits which has not been revealed.

89. In conclusion, Mr Cooper has not satisfied the burden of proof of showing that, on the balance of probabilities, the deposits into his bank account which HMRC have treated as trading income have some other source.

90. Having reached this conclusion, we now return to the question was to whether the loss of tax was brought about by Mr Cooper deliberately, bearing in mind that the burden of proof is now on HMRC to establish this.

91. It will be apparent that the reasons for our conclusion are based not on the fact that the unidentified deposits which form the basis of HMRC's assessment have been shown to be trading income; rather it is because Mr Cooper has been unable to demonstrate on the balance of probabilities that they represent something other than trading income.

92. It seems to us that, in order for HMRC to establish that the loss of tax was brought about deliberately, it needs to be shown (on the balance of probabilities) that Mr Cooper knew that he had trading income and made a deliberate decision not to declare it.

93. Logically, this requires HMRC to satisfy us that the unidentified deposits do in fact represent trading income. If we cannot be satisfied on this point, we cannot say that Mr Cooper knew that he had undeclared trading income.

94. However, HMRC have not set out to prove (even on the balance of probabilities) that the unidentified deposits represent undeclared trading income. Clearly they suspect that this is the case based on Mr Cooper's known expenditure and the lack of any other credible explanation for the source of the funds and, in the context of the assessment itself, have been content to leave it up to Mr Cooper to try to discharge his burden of proof in showing that the deposits in fact represent some other source of funds. That however is very different to HMRC showing that the deposits are more likely than not to be trading income.

95. We are therefore left in a position where, although Mr Cooper has been unable to produce sufficient evidence to persuade us that the deposits do not represent trading income, there is also insufficient evidence for us to be able to say on the balance of probabilities that the deposits are in fact trading income.

96. In these circumstances, we cannot be satisfied that the loss of tax was brought about deliberately by Mr Cooper. The assessment is therefore out of time and must be cancelled.

Tax year ended 5 April 2008

97. The payments which HMRC have treated as trading profits for this tax year fall into three categories:

(1) unidentified deposits totalling £25,850;

(2) £18,500 received from Mr J Holland in respect of the purchase of a boat; and

(3) £728,994 paid into SOL's bank account representing the deposit for the sale of three barges to Pars Company in Iran.

Unidentified deposits

98. The issues here are the same as for the unidentified deposits in the tax year ended 5 April 2007. Mr Birkbeck submits that these are loans from Mr Evans. For the reasons set out above, we do not accept that Mr Cooper has discharged the burden of proof of showing that these payments are anything other than trading income.

Payments from Mr J Holland

99. Mr Cooper entered into a contract with John Holland on 15 June 2007 to sell him a boat for £98,000, the deposit being £18,500.

100. Mr Holland made a payment of £5,000 in April 2007 and a further payment of £13,500 on 15 June 2007.

101. Mr Birkbeck submits that the contract was never completed and the deposit was returned to Mr Holland. As a result of this, he argues that there was no trading income.

102. The evidence contains a letter from Mr Holland dated 15 November 2007 in which he confirms that the £13,500 was repaid via a £10,000 cheque and £3,500 in cash paid in November 2007. Mr Birkbeck took us to an entry in Mr Cooper's bank statements showing a cheque for £10,000 going through his account on 4 December 2007.

103. As far as the £5,000 is concerned, Mr Cooper's evidence is that the cheque bounced. Again, Mr Birkbeck took us to the relevant entries in Mr Cooper's bank account in relation to this.

104. HMRC accept that the £13,500 was repaid but say that it is not clear whether the cheque for £5,000 did in fact bounce.

105. It is however clear to us from the entries in Mr Cooper's bank statement that the cheque for £5,000 was presented twice to NatWest in April 2007 and that, on both occasions, the cheque bounced. We are therefore satisfied that the whole of the deposit was repaid to Mr Holland and that this £18,500 does not therefore represent Mr Cooper's trading income for the relevant tax year.

Three barges deal

106. There is no dispute that there was a contract to supply three barges to a company in Iran for a total payment of $9 million, nor that a deposit of 15% representing just under £730,000 was paid into the bank account of Ship & Ocean Limited.

107. Mr Birkbeck however puts forward two reasons why this does not represent taxable trading income for Mr Cooper:

(1) The deal was never completed and so the deposit had to be (and was in fact) repaid.

(2) The contract was entered into by SOL and not Mr Cooper trading as SO and so, if the deposit did represent trading income, it is the income of SOL and not Mr Cooper's trading income.

Was the deposit refundable

108. The original contract is in Farsi. The evidence contains a translation of the contract into English by a professional translation company.

109. Mr Birkbeck took us to various provisions of the contract. The first is article 3 which shows the total purchase price of US$9 million of which a deposit of 15% was payable, a further 80% was payable by way of letter of credit when the barges are delivered and the remaining 5% was to be paid 45 days after the barges are delivered.

110. Mr Birkbeck then drew attention to article 7 which provides as follows:

> "Article 7 – guarantee
>
> The seller is obliged to issue real estate collateral or bank collateral with a price 1.10 times more than the price of contract under the name of the buyer. This will be mentioned in purchase contract between the parties.
>
> **Note:** the aforementioned guarantee will be effective after delivering the barges by the seller.
>
> **7.**2 The seller will receive 5% of the price of the contract two months after delivering the barges as good performance, and if the agreed commitments are not demonstrated as planned, once the buyer identifies that the seller has violated the provisions he is allowed to reimburse the aforementioned amount to compensate for the incurred damages.
>
> **7.**3 If the goods are not technically verified according to the technical appendix of the contract, the buyer should provide the reason of mismatch between demanded regulations to the seller, and if the seller does not do any action in appropriate time, the buyer is allowed to do the required actions and reimburse the amounts mentioned in paragraph 7.2."

111. The governing law of the contract is stated in article 9 to be "international laws". Mr Birkbeck submits that in the absence of any specific governing law and in the absence of any evidence as to foreign laws, the contract should, for the purposes of these proceedings, be interpreted under English law.

112. Mr Birkbeck submits that the effect of article 7.2 is that the deposit is refundable if the seller is in breach of the contract. Although clause 7.2 refers to the 5% good performance payment, Mr Birkbeck makes the point that, if the breach is failure to deliver the barges, the good performance payment will not have been made and so the reference to reimbursing the "aforementioned amount" by way of compensation must be a reference to repaying all amounts previously paid under the contract – i.e. the 15% deposit.

113. In support of this, Mr Birkbeck referred to the requirement for collateral to be provided by the seller. Mr Cooper's evidence was that this collateral had been provided using Mr Cooper's real estate assets in Iran which he had inherited from his grandfather.

114. Mr Birkbeck also referred us to correspondence from the purchaser making it clear that the deal never completed.

115. Mr Birkbeck also drew our attention to the fact that Mr Cooper has been consistent since his first meeting with Mr Woods that the deposit had to be repaid as a result of court action taken in Iran, the outcome of which was that he was said to owe $2 million by way of compensation to the purchaser.

116. On this basis, Mr Birkbeck submits that the deposit is refundable and should not therefore be taken into account as Mr Cooper's trading income.

117. Mr Wilkinson on behalf of HMRC makes the point that we have no documentary evidence in relation to any collateral being provided in Iran or the existence of the court case in Iran mentioned by Mr Cooper.

118. As far as the contract is concerned, Mr Wilkinson submits that clause 7.2 only relates to the 5% good performance payment and not to the 15% deposit. On this basis, he says that the deposit is not refundable. Indeed, the view HMRC have taken is that the deposit has been forfeited. Mr Wilkinson argues that this conclusion is supported by the fact that Mr Cooper immediately used almost the entirety of the deposit in making transfers to other bank accounts, paying his former wife and buying a new car.

119. We are in agreement with Mr Wilkinson that the deposit is not refundable.

120. Looking first at the terms of the contract, it is clear to us that on a natural reading article 7.2 is dealing only with the 5% good performance payment and does not relate to the 15% deposit. The reference to "the aforementioned amount" at the end of article 7.2 is the 5% amount which is mentioned at the beginning of article 7.2.

121. This is reinforced by article 7.3 which allows reimbursement of "the amounts mentioned in paragraph 7.2". The only amount which is mentioned in article 7.2 is the 5% good performance payment. It would be odd if article 7.2 allowed reimbursement of all payments whereas article 7.2 only allowed reimbursement of the 5% good performance payment. Had the parties intended that the deposit or the 80% of the purchase price payable on delivery of the barges should be subject to reimbursement, we would have expected article 7.3 (and therefore article 7.2 as well) to cross-refer to article 3.

122. No doubt the purchaser may have a claim against the seller in respect of the failure to deliver the barges but the purchaser would only recover the deposit if it established that there had in fact been a breach of the agreement. Mr Cooper's evidence was that the barges had not been delivered as a result of the purchaser failing to pay the 80% of the purchase price due on delivery of the barges and so it is not clear that the purchaser would succeed in any such action.

123. Mr Cooper has always maintained that there have been court proceedings in Iran as a result of which he is required to pay the purchaser $2 million. However, as Mr Wilkinson has pointed out, there is no documentary evidence of this. Indeed, the only document which Mr Birkbeck referred to in relation to possible proceedings is an email dated 30 November 2009 from the purchaser which states "these are serious issues that we have forwarded to our legal adviser in the UK to pursue". This suggests that, if there were to be any legal proceedings, they would be in the UK and not in Iran.

124. We are also not convinced by the suggestion that Mr Cooper has provided collateral out of his assets in Iran and his oral evidence that the deposit was repaid to the buyer out of this collateral.

125. In his initial meeting with Mr Woods, Mr Cooper said that the approximate value of his inheritance from his grandfather was in the region of £1 million and that £900,000 of this had been brought to the UK by 2011. He told Mr Woods that the result of this and other payments was that Mr Cooper in fact owed his brother-in-law in Iran £400,000.

126. Mr Cooper, in his oral evidence, stated that the value of his inheritance from his grandfather was closer to £3.2 million and that he had only brought £100,000 to the UK. This is directly contrary to what he is reported as having said in the first meeting with Mr Woods and are not figures which have appeared in any of the other documentary evidence which we have seen. Although Mr Cooper says that there are inaccuracies in the notes of the first meeting, we think it is more likely that the figures in those notes are closer to the true position.

127. In any event, the contract requires collateral of 1.1 times the purchase price under the contract. The purchase price is US$9 million which would mean that collateral of US$9.9 million would be required. Even on the basis of Mr Cooper's oral evidence, he did not have assets in Iran totalling US$9.9 million.

128. At the meeting with Mr Woods in March 2012, Mr Cooper said that he still owed £2 million in Iran following the court case (there is inconsistent evidence as to whether the figure is £2 million or US$2 million). This of course indicates that, at that stage, the deposit had not in fact been repaid. Had the deposit been repaid out of the collateral, as stated by Mr Cooper in his oral evidence, we would have expected that the purchaser would have recovered its deposit before March 2012 which was over four years after the contract should have been performed and after Mr Cooper says the court case was concluded.

129. In addition to this, the fact that Mr Cooper immediately used almost all of the deposit for his own purposes indicates to us that he was not expecting that the deposit was refundable.

130. Taking all of this into account, our conclusion is that the deposit was trading income, it was not refundable under the terms of the contract and therefore should be recognised for tax purposes when it was paid. There might be some adjustment if it is shown that, as a result of the failure to complete the contract, the deposit has been repaid but we are not persuaded based on the evidence we have seen and heard, that the deposit has in fact been repaid.

131. We therefore need to go on to consider Mr Birkbeck's second point which is whether the deposit represents trading income of Mr Cooper trading as SO or whether it is trading income of SOL.

Who entered into the three barges contract

132. Mr Birkbeck's starting point is that the contract has been entered into by SOL and not by SO. The contract refers to "Ship & Ocean Co". In the parties section of the agreement this has been reproduced by the translators as Ship & Ocean Limited. However, in the other two places where the seller is referred to by name, the translators have referred to "Ship & Ocean Co".

133. Mr Cooper's evidence was that, in Iran, "Co" effectively means the same as "Limited" in England. Mr Birkbeck therefore submits that it is clear that the agreement is entered into by SOL and not by Mr Cooper trading as SO. He accepts that there could be a mistake in the agreement but referred us to the decision of the House of Lords in *Chartbrook Limited v Persimmon Homes Limited* [2009] 1 AC as authority for the proposition that strong evidence is needed to establish that there is a mistake in a contract. He submits that, in this case, there is no evidence of any mistake in the contract and, in particular, that Pars Company intended to contract with Mr Cooper personally as opposed to his company.

134. Mr Birkbeck acknowledges that Mr Cooper appears to have been confused about whether he was carrying on business as a sole trader or through a limited company but argues that this cannot affect whether the agreement was made by Mr Cooper personally or by his company when it is clear on the face of the contract that the agreement is with the company as this is something which needs to be agreed by both parties and cannot therefore be affected by the understanding of one of the parties.

135. Mr Birkbeck also refers to Mr Woods' witness statement where he says that:

> "I was given to understand that the company, Ship & Ocean Limited had been taken to court in Iran in which case I decided Mr Cooper is not under any legal obligation to pay the debt of the, now struck off, limited company, Ship & Ocean Limited."

136. Mr Birkbeck submits that this shows that HMRC considered the contract to have been made by SOL and not by Mr Cooper trading as SO.

137. In response to HMRC's suggestion that the fact that the deposit was clearly paid into SOL's bank account is of no relevance, Mr Birkbeck argues that this is of course consistent with the contract having been entered into by SOL and that what HMRC are effectively trying to do is to pierce the corporate veil and to treat the deposit as somehow belonging to Mr Cooper rather than SOL.

138. Mr Birkbeck referred us to the decision of the Supreme Court in *Prest v Petrodel Resources Limited* [2013] UKSC 34. After reviewing the authorities, Lord Sumption JSC (with whom the other judges were broadly in agreement) concluded at [35] that:

> "There is a limited principle of English law which applies when a person is under an existing legal obligation or liability or subject to an existing legal restriction which he deliberately evades or whose enforcement he deliberately frustrates by interposing a company under his control. The court may then pierce the corporate veil for the purpose, and only for the purpose, of depriving the company or its controller of the advantage that they would otherwise have obtained by the company's separate legal personality. The principle is properly described as a limited one, because in almost every case where the test is satisfied, the facts will in practice disclose a legal relationship between the company and its controller which will make it unnecessary to pierce the corporate veil."

139. Mr Birkbeck submits that there is no good reason in this case to pierce the corporate veil and that HMRC are not entitled to do so. He observed that, had the money stayed in SOL, no doubt HMRC would have assessed SOL and not Mr Cooper.

140. HMRC's response to this is that Mr Woods was clear, based on what Mr Cooper told him and his own investigations, that the contract had been entered into by Mr Cooper trading as SO and not by SOL.

141. Mr Wilkinson referred to the minutes of the first meeting between Mr Woods and Mr Cooper on 8 March 2012 where Mr Cooper is reported as saying that the deposit had been paid into the bank account of SOL in error and that SOL had never traded, all the trading being carried out by Mr Cooper as SO.

142. Mr Wilkinson made the point that, although Mr Cooper had been told at the beginning of the second meeting on 30 January 2013 that he had suggested making some amendments to the notes of the first meeting, he once again stated that, although the deposit money was paid into SOL's bank account, SOL had never traded and that he was self-employed, trading as SO. Mr Wilkinson reminded the Tribunal that, despite being given the opportunity, Mr Cooper never provided HMRC with any amendments to the meeting notes.

143. Mr Wilkinson submits that the statements made by Mr Cooper were not taken by Mr Woods in isolation but were cross-checked. Mr Woods' evidence is that he checked the position at Companies House which showed that SOL was a dormant company and also checked whether SOL had ever submitted any tax returns, which it had not.

144. In further support of HMRC's position, Mr Wilkinson referred the Tribunal to various letters from Mr Cooper to HMRC in 2014 and 2015 in which he refers in one way or another to the transaction being entered into by him, without mentioning the company. Mr Wilkinson tells us that the first suggestion he can find in the correspondence that the deposit actually belonged to SOL is an email in February 2017.

145. Mr Wilkinson also points out that, in 2010, Mr Cooper applied for VAT registration (backdated to 15 April 2007 – i.e. before the three barges contract) for his sole trade business, SO and not for SOL. He questions why Mr Cooper would apply for VAT registration for his sole trade and not for the company if the company was in fact trading as Mr Cooper now suggests.

146. Finally, Mr Wilkinson submits that the fact that Mr Cooper treated the deposit as his own money is further evidence that he did not consider the transaction to have been entered into by SOL.

147. The more credible explanation, says Mr Wilkinson, is that even if Mr Cooper was trying to make it look as if the transaction was carried out through SOL in order for it to appear more legitimate from the point of view of somebody in Iran, his intention was that, in reality, the transaction was entered into by Mr Cooper himself trading as SO.

148. We are not convinced that the contract for the sale of the three barges was entered into by SOL rather than by SO. The original Farsi version of the contract clearly refers to "Ship & Ocean Co" and not "Ship & Ocean Limited". Whilst Mr Cooper's evidence was that, in Iran, "Co" is the same as "Limited", this is to some extent inconsistent with the fact that the translators have referred to "Ship & Ocean Limited" in one place but to "Ship & Ocean Co" in two other places.

149. Given that the position is not clear from the written terms of the contract itself, it is necessary to look at the surrounding circumstances.

150. Far from Mr Cooper being confused about the difference between SO and SOL, the overwhelming evidence is that Mr Cooper was not only clear about the difference but was also clear that SOL had not traded and that all of his trading activities were in his own name through SO.

151. As Mr Wilkinson has pointed out, this is consistent with the statements he made at both meetings with Mr Woods and is also consistent with the status of SOL at Companies House and in HMRC's records.

152. It is also consistent with the fact that all of the premises were rented by SO, staff were paid by SO and supplies were invoiced to and paid for by SO – i.e. all of the expenses of the business were paid for by SO and not by SOL.

153. In his oral evidence, Mr Cooper said that once SOL was established in 2004, all of the trading activities were carried out by SOL and not by Mr Cooper trading as SO. However, the evidence clearly shows that this is not correct. There is no doubt that the contracts for the sale of the tug yacht, the hovercrafts and the hovercraft plug and the contracts for the purchase of the WIG boat design and the model aircraft were all entered into by SO and not by SOL.

154. Taking all of this into account, we are not satisfied that "Ship & Ocean Co" in the contract for the sale of the barges can be interpreted as meaning "Ship & Ocean Limited".

155. Even if we had been satisfied that the contract was in the name of SOL, Mr Cooper would still need to satisfy us that the income from that contract was not his own trading income rather than the income of SOL.

156. Mr Birkbeck is right that strong evidence is needed to show that there is a mistake in a contract and that there is no evidence here that there has been any such mistake.

157. However, we do not agree with Mr Birkbeck that the absence of any such mistake inevitably means that the only way of SOL's income being treated as Mr Cooper's income is to pierce the corporate veil which, on the basis of the conclusions of the Supreme Court in *Prest v Petrodel* would not be permissible in the circumstances of this case.

158. This ignores the fact that, in coming to their conclusions, the judges of the Supreme Court decided that many of the situations which have arisen in the past which have been thought to involve piercing the corporate veil are in fact situations where there is some other reason why the person in question as opposed to the company has been made liable.

159. Lord Sumption JSC who gave the main judgment drew a distinction between what he referred to as concealment (which does not involve piercing the corporate veil) and evasion (where the corporate veil may be pierced). In relation to concealment, he said at [28] that:

> "The concealment principle is legally banal and does not involve piercing the corporate veil at all. It is that the interposition of a company or perhaps several companies so as to conceal the identity of the real actors will not deter the courts from identifying them, assuming that their identity is legally relevant. In these cases the court is not disregarding the 'façade', but only looking behind it to discover the facts which the corporate structure is concealing."

160. As an illustration of this, Lord Sumption JSC referred at [31] to *Gencor ACP Limited v Dalby* [2000] 2 BCLC 734 observing that:

> "Rymer J held, at para 26, that Mr Dalby was accountable for the money received by Burnstead, on the ground that the latter was "in substance little other than Mr Dolby's offshore bank account held in a nominee name" and "simply … the alter ego through which Mr Dalby enjoyed the profit which he earned in breach of his fiduciary duty to ACP … The correct analysis of the situation was that the court refused to be deterred by the legal personality of the company from finding the true facts about its legal relationship with Mr Dalby."

161. Lord Neuberger of Abbotsbury PSC referred to another well-known case in this area, *Gilford Motor Co Limited v Horne* [1933] Ch 935 saying at [71-72]:

> "71. In any event, it seems to me that the decision in the *Gilford Motor* case that an injunction should be granted against the company was amply justified on the basis that the company was Horne's agent for the purpose of carrying on the business (just as his wife would have been, if he had used her as the 'cloak').
>
> 72. It is by no means inconceivable that the three members of the Court of Appeal in *Gilford Motor* were using the expressions 'cloak or sham' to suggest, as a matter of legal analysis, a principal and agent relationship. Lord Hanworth relied on a passage in a judgment of Lindley LJ in *Smith v Hancock* [1894] 2 Ch 377, 385 (where the expression 'cloak or sham' appears to have originated), and in that passage, it seems to me that the cloak or sham is treated as amounting to the business being 'carried on for the defendant'. This view is supported by something Lord Denning MR said in *Wallersteiner v Moir*

[1974] 1 WLR 991, 1013, namely it was 'quite clear' that the companies in that case:

> 'Were just the puppets of Dr Wallersteiner … transformed into legal language, they were his agents to do as he commanded. He was the principal behind them … at any rate, it was up to him to show that anyone else had a say in their affairs and he never did so: cf *Gilford'*."

162. What is clear from *Prest v Petrodel* is that it is necessary to ascertain the true relationship between the individual in question (in this case Mr Cooper) and the company (SOL). In many cases this will give rise to an answer which means that there is no need to consider piercing the corporate veil. Indeed, in *Prest v Petrodel* itself, it was found on the evidence that the properties which were held in the names of the relevant companies were beneficially owned by the husband.

163. Based on the evidence set out above, our view in this case is that even if the reference to "Ship & Ocean Co" in the three barges contracts is a reference to SOL and that SOL is therefore the contracting party, the surrounding circumstances show, as Mr Wilkinson has submitted, that Mr Cooper's intention was that SOL should do so as his agent.

164. The fact that the purchaser may not have known that SOL was acting as an agent and so would not have known who the principal was does not mean that the principal cannot have rights in relation to the contract (see, for example, *Novasen SA v Alimenta SA* [2011] EWHC 49 (Comm) QBD).

165. Mr Cooper in his evidence told us that one of the reasons for setting up SOL was that a company was needed for the purposes of credibility in relation to his customers as some of them would not trust a sole trader who could easily disappear. This is in our view consistent with the conclusion that SOL was nothing more than a façade and that, to the extent that it did anything, it did so as Mr Cooper's agent. This would explain why Mr Cooper made no real distinction between SOL and his own sole trade and also why he treated the deposit paid into SOL's bank account effectively as his own money without any formality such as SOL recording a loan, declaring a dividend or paying a salary or bonus to Mr Cooper.

166. Our conclusion on this aspect therefore is that Mr Cooper has not satisfied us that the contract was entered into by SOL rather than by himself trading as SO. However, even if the contract were entered into by SOL, we find that, based on the evidence before us, it is more likely than not that SOL did so as Mr Cooper's agent.

167. Had we found that SOL had entered into the contract for the sale of the three barges on its own behalf, we would then have needed to consider whether the fact that almost all of the deposit was used by Mr Cooper for his own purposes gives rise to some separate source of income which was not identified by HMRC at the time they made the assessment. There was no such suggestion in HMRC's statement of case although there was a passing reference in Mr Wilkinson's skeleton argument as to the possibility of income arising to Mr Cooper as a result of SOL writing off a loan to a participator when it was dissolved in 2010.

168. It is for this reason that we asked the parties for written submissions as to the extent to which the Tribunal is at liberty in deciding whether an appellant has been overcharged by an assessment for the purposes of s 50(6) Taxes Management Act 1970 issues which have not been put before the Tribunal by the parties in their grounds of appeal or in their statement of case. Both parties have provided submissions and we are grateful to them for having done so. Given the conclusions we have reached, we do not now need to address this point. However, in case we are wrong in our conclusions, we comment on the submissions made by the parties.

169. Mr Wilkinson's starting point is that in relation to an appeal against a discovery assessment, the Tribunal's primary duty is to determine whether the appellant has been under or overcharged by an assessment to tax. He accepts that this cannot justify a general enquiry into the appellant's affairs but submits that the Tribunal is entitled to look at any tax liability which is of a similar nature to that which forms the basis of the assessment and which falls within the factual matrix associated with the loss of tax which gave rise to the assessment.

170. These submissions are based on the decision of the First-tier Tribunal in *Gareth Clark v HMRC* [2017] UKFTT 0392 where the Tribunal concluded at [39] that:

> "… in common with the closure notice provisions, there is no express requirement in s 29 TMA or elsewhere that the officer must set out or state the reasons for the opinion that has been reached. No such obligation can be implied. Section 31(1)(d) makes no provision for an appeal against the reasons for the assessment. The duty of this Tribunal is not to review or adjudicate upon the officer's reasons, but simply upon the assessment and to determine whether the appellant is either undercharged or overcharged, and to increase or reduce the assessment accordingly (s 50(6) and (7) TMA)."

171. The Tribunal however accepted at [43] that:

> "43. The scope of the assessment, and consequently of the appeal, must therefore have some limitation. We consider that it is consistent with s 29, taken as a whole, for the scope of the assessment to be limited to a charge of the particular nature which is considered to have given rise to the loss of tax for a particular year of assessment, and which arises out of the factual matrix that is found to have been associated with the loss of tax that gave rise to the assessment on the basis of the officer's opinion. That too will be the scope of the appeal. On an appeal, by virtue of s 50(6) and (7), the Tribunal is not confined to the reasons for the opinion of the officer when coming to the opinion that there had been a loss of tax, nor is it confined to examination only of the facts on which that opinion was based, or the legal analysis applied at that time. As Henderson J said, and as equally applicable to a discovery assessment as to a closure notice, the Tribunal, acting fairly, may apply the law to the facts as it finds them, and is not constrained by the arguments put forward by the parties whether before or at any stage in the proceedings. The public interest in taxpayers paying the right amount of tax is as strong as, if not stronger or at least more evident than, it has ever been, and the duty of the Tribunal remains to determine whether the assessment undercharges or overcharges the appellant."

172. Mr Wilkinson notes that the Upper Tribunal in *Gareth Clark v HMRC* [2018] UKUT 0397 (TCC) approved at [53-58] the First-tier Tribunal's conclusions on this issue.

173. In this case, Mr Wilkinson submits that as long as the basis of the assessment is income tax (a charge of a particular nature) and relates to the proceeds of the three barges deal (the factual matrix), it is immaterial how the income tax liability arises.

174. Mr Wilkinson therefore argues that it is open to the Tribunal to reach the conclusion that Mr Cooper has not been overcharged by the assessment for the tax year ended 5 April 2008 if it is satisfied that the income from the three barges deal is Mr Cooper's income whether it reaches that conclusion on the basis that the income constitutes his personal trading income or

for some other reason not suggested by HMRC either at the time the assessment was made or at any later stage.

175. Whilst Mr Birkbeck accepts that s 50(6) and (7) Taxes Management Act 1970 ("TMA") confer wide powers on the Tribunal, he submits that those powers are limited by fundamental principles including in particular, the right to a fair hearing.

176. Mr Birkbeck notes that the decisions of both the First-tier Tribunal and the Upper Tribunal in *Gareth Clark* derive from previous decisions in relation to the scope of an appeal against a closure notice and, in particular, in the First-tier Tribunal, on the decision of Henderson J in the High Court in *Tower MCashback LLP 1 & Another v HMRC* [2008] EWHC 2387 (Ch) who concluded at [114] that:

> "114. A further important principle can in my judgement be deduced from the wording of s 50(6) and (7). Because one of the matters that the commissioners have to consider is whether the taxpayer is *undercharged* to tax by an assessment or self-assessment, or whether any amounts contained in a partnership statement are *insufficient*, it would seem to follow that the commissioners are not confined to an examination of the reasons advanced by HMRC in support of the conclusions set out in a closure notice, and that they are not compelled to treat an amendment to a return under s 28A or 28B as fixing the maximum amount of tax which is recoverable. Provided that they act fairly, and on the basis of evidence that is properly before them, the commissioners may take the initiative and apply the law to the facts in the manner that appears to them to be correct, regardless of the arguments advanced by either side."

177. This, says Mr Birkbeck, makes it clear that, although the Tribunal may take into account any points of fact or law of its own initiative, this must be done fairly as indeed is consistent with the overriding objective in rule 2 of the Tribunal Rules which requires the Tribunal to deal with cases fairly and justly.

178. In further support of his submission, Mr Birkbeck refers to the comments of Lewison LJ In the Court of Appeal in *Prudential Assurance Co Ltd v HMRC* [2016] EWCA Civ 376 in relation to the importance of identifying all of the relevant issues in the pleadings. He observed at [20] that:

> "Our procedural system is and remains an adversarial one. It is for the parties (subject to the control of the court) to define the issues on which the court is invited to adjudicate. This function is the purpose of statements of case. The setting out of a party's case in a statement of case enables the other party to know what points are in issue, what documents to disclose, what evidence to call and how to prepare for trial. It is inimical to a fair hearing that a party should be exposed to issues and arguments of which he has had no fair warning. If a party wishes to raise a new point, he should do so by amending a statement of case."

179. As far as factual issues are concerned, Mr Birkbeck refers to decisions relating to late evidence (*Earthshine* (see paragraph [9] above)) and the importance of cross-examination (*Sait v GMC* [2018] EWHC 3160 (Admin)) in submitting that it would be wrong for the Tribunal to decide that an appellant had been undercharged or overcharged by an assessment for reasons which had not previously been pleaded or argued if its conclusion is based on facts which the

appellant has not had an opportunity to respond to or which have not been put to the witnesses in cross-examination.

180. Finally, Mr Birkbeck refers to the decision of the Northern Ireland Court of Appeal in *Ulster Metal Refiners Limited v HMRC* [2017] NICA 26 which related to VAT fraud. HMRC pleaded and argued the case on the basis that the relevant fraud related to hijacked traders. However, the First-tier Tribunal, after hearing the evidence, found that, although there was fraud involved, the particular fraud was not that identified by HMRC.

181. The Northern Ireland Court of Appeal accepted that a Tribunal could make a finding on a basis which is suggested by the Tribunal but which has not been pleaded (which they described as a "third man theory") but concluded at [43] that:

> "There are a number of steps that it must take to ensure that the defendant is afforded a fair trial. In particular it must inform the parties clearly of the 'third man theory' and then afford the parties sufficient opportunity to respond to the new case and if necessary permit an adjournment to allow the parties time to make decisions about what further investigations they should carry out, what further evidence or disclosure they should seek, what further witnesses they should call and what further submissions they should make. These steps are essential and central to meeting the requirement of a fair hearing as they ensure that the party has an opportunity to know exactly the case he has to meet and an opportunity to meet it."

182. Based on these principles, Mr Birkbeck submits that the Tribunal has no power to take into account points not put in issue and/or pleaded by either party as part of the proceedings, especially where these points involve questions of fact. For example, if the Tribunal were minded to conclude that SOL had made a loan to Mr Cooper or paid a dividend or salary to him, this would, he says, give rise to factual questions which would need to be put to Mr Cooper in order to comply with the fundamental principle that proceedings should be conducted fairly.

183. It is clear from the authorities that the Tribunal does have a wide discretion in relation to s 50(6) and (7) TMA to determine whether a taxpayer has been overcharged or undercharged by an assessment. This includes raising issues on its own initiative which have not been pleaded by either party. The Supreme Court in *HMRC v Tower MCashback LLP 1 & Another* [2011] UKSC 19 specifically approves at [15] the following statement made by Henderson J at [115] in the High Court decision in that case:

> "There is a venerable principle of tax law to the general effect that there is a public interest in taxpayers paying the correct amount of tax, and it is one of the duties of the Commissioners in exercise of their statutory functions to have regard to that public interest. [The judge then considered changes in the tax system and continued] For present purposes, however, it is enough to say that the principle still has at least some residual vitality in the context of section 50, and if the Commissioners are to fulfil their statutory duty under that section they must in my judgment be free in principle to entertain legal arguments which played no part in reaching the conclusions set out in the closure notice. Subject always to the requirements of fairness and proper case management, such fresh arguments may be advanced by either side, or may be introduced by the Commissioners on their own initiative."

184. The Supreme Court also endorsed at [13] the comment of Dr John Avery-Jones CBE in *D'Arcy v HMRC* [2006] STC (SCD) 543 that:

> "It seems to me inherent in the appeals system that the Tribunal must form its own view on the law without being restricted to what the Revenue state in their conclusion or the taxpayer states in the notice of appeal. It follows that either party can (and in practice frequently does) change their legal argument. Clearly any such change or argument must not ambush the taxpayer and it is the job of the Commissioners hearing the appeal to prevent this by case management."

185. The principles established by the Supreme Court and by Henderson J in *Tower MCashback* were approved and summarised by the Court of Appeal in *Fidex Limited v HMRC* [2016] EWCA Civ 385 at [45]:

> "In my judgment the principles to be applied are those set out by Henderson J as approved by and elaborated upon by the Supreme Court. So far as material to this appeal, they may be summarised in the following propositions:
>
> (i) The scope and subject matter of an appeal re defined by the conclusions stated in the closure notice and by the amendments required to give effect to those conclusions.
>
> (ii) What matters are the conclusions set out in the closure notice, not the process of reasoning by which HMRC reached those conclusions.
>
> (iii) The closure notice must be read in context in order properly to understand its meaning.
>
> (iv) Subject always to the requirements of fairness and proper case management, HMRC can advance new arguments before the FTT to support the conclusions set out in the closure notice."

186. Whilst both *Tower MCashback* and *Fidex* dealt with closure notices, the Upper Tribunal confirmed in *Gareth Clark* that the same principles should be applied to appeals against discovery assessments. Indeed, in our view, they would apply to any appeal where the Tribunal must decide in accordance with s 50(6) or (7) TMA whether the taxpayer has been undercharged or overcharged by an assessment.

187. As Mr Birkbeck points out, one common thread in the comments that have been made by the various courts and tribunals is that the process which is followed is a fair one.

188. What is fair will depend on the circumstances of each case. For example, in *Gareth Clark*, the issue was whether there had been an unauthorised pension transfer. There had been a transfer from A to B and then from B to C. HMRC's discovery assessment was on the basis that the payment from B to C was an unauthorised transfer. However, as a result of a submission made by the appellant as to the status of B, the Tribunal upheld the assessment on the basis that the transfer from A to B was an unauthorised transfer. This decision was upheld by the Upper Tribunal on the basis that this finding fell within the factual matrix and the subject matter of the original assessment. There was no suggestion that there had been any procedural unfairness given that it was the appellant themselves who had raised the issue as to the status of B. It should however be noted that this was not a case where the Tribunal raised an issue of its own initiative. The primary question was whether the Tribunal could uphold the assessment on the basis of the transfer from A to B when the assessment was originally made as a result of HMRC's view that the transfer from B to C was not authorised.

189. *Tower MCashback* was in many respects similar. HMRC had disallowed capital allowances. The question was whether HMRC could advance arguments as to why the capital allowances should be disallowed which were different to the taxpayer's understanding as to

the reasons why HMRC had disallowed those capital allowances when they issued closure notices. The Supreme Court decided that they could in the particular circumstances. Although the Supreme Court noted the requirement for procedural fairness, there was no suggestion that the procedure which was followed was in any way unfair.

190. *Ulster Metal* was closer to the current case. As mentioned above, the Tribunal found that fraud was involved but on a different basis to that which had been pleaded by HMRC. The Court of Appeal concluded that there had been procedural unfairness in that the Tribunal judge had not clearly indicated to the taxpayer's counsel that the Tribunal was considering finding for HMRC on a different factual basis to that which HMRC had advanced and that HMRC never indicated that it wished to rely on an alternative factual basis and never applied to amend its pleadings. The taxpayer was therefore taken by surprise and was not given an opportunity to meet the new case which was now being made against it.

191. Based on all of these cases, it is possible to draw out some principles:

(1) The scope of an appeal against an assessment or a closure notice is limited by the conclusions stated in the closure notice and the amendments required to give effect to them or to the nature of the charge which gives rise to the assessment and to the factual matrix giving rise to that conclusion or to the charge (*Gareth Clark*).

(2) Subject to this limitation, it is open to the Tribunal to decide whether a taxpayer has been overcharged or undercharged by an assessment for the purposes of s 50(6) and (7) Taxes Management Act 1970 for reasons other than those put forward by the parties (*Tower MCashback*).

(3) The Tribunal must however follow a fair process. This will normally involve informing the parties of the findings which it is considering making and giving them an opportunity to address any relevant issues including, in relation to any factual issues, producing further evidence or cross-examining witnesses (*Fidex*).

(4) Although it is not a point which has been dealt with in any of the cases we have looked at, we would venture to suggest that where both the law and the findings of fact are clear, it would be open to the Tribunal to make a decision as to whether a taxpayer had been overcharged or undercharged by an assessment based on an application of the law to the facts, even if this resulted in findings which had not been pleaded or argued by either party or put to them by the Tribunal. It is clear from Henderson J's comments at [114] in *Tower MCashback* that the Tribunal may do so and it would not be procedurally unfair for the Tribunal to do so where the relevant facts had been fully explored at the hearing and the legal principles were straightforward. We accept however that the situations in which these circumstances may arise are likely to be few and far between.

192. Turning to the present case, Mr Birkbeck is quite right to point out that, if we are wrong in our conclusion that the three barges deposit was part of Mr Cooper's income from his trade as SO and in fact belonged beneficially to SOL, there is no evidence and no findings of fact which could support a conclusion by the Tribunal that Mr Cooper's use of the money nonetheless resulted in him receiving income of some other nature which has not been taxed.

193. Mr Wilkinson suggests that it is enough to know that the three barges deposit was paid into a bank account of SOL over which Mr Cooper had control and that he in fact used it for his own personal purposes. However, whilst it is perfectly possible that these facts could form the basis for an argument that Mr Cooper had received income in some form other than trading income, there is no evidence as to whether SOL might (for example) have paid a dividend to Mr Cooper, paid a salary to Mr Cooper or made him a loan which was subsequently written off.

194. Although Mr Wilkinson mentioned in his skeleton argument the possibility of SOL having made a loan to Mr Cooper which was subsequently written off when the company was dissolved in 2010, this was neither pleaded in HMRC's statement of case nor was any application made by HMRC to amend their statement of case to include this possibility.

195. As Mr Birkbeck says, in order to conclude that Mr Cooper had received income on any basis other than trading income, the Tribunal would need to explore in further detail the basis on which funds were transferred from SOL to Mr Cooper (or otherwise used for his own purposes) and Mr Cooper would need to be cross-examined about these issues.

196. As this did not happen, it would be procedurally unfair for the Tribunal to conclude that Mr Cooper had received income in some other form which might justify the amount of the assessment made by HMRC for the tax year ended 5 April 2008.

197. Therefore, if we are wrong about the three barges deposit forming part of Mr Cooper's own trading income rather than that of SOL, our conclusion would be that Mr Cooper had been overcharged by the assessment and our decision would be that it should be reduced accordingly.

198. The result of all of this is that Mr Cooper has been overcharged by the assessment. The taxable profit should be reduced by £18,500 representing the deposit paid by Mr John Holland which, we have found, was reimbursed and should not therefore have been treated as forming part of Mr Cooper's trading income for the tax year.

Tax year ended 5 April 2009

199. The income which has been assessed for this year represents 39 payments into Mr Cooper's bank accounts totalling £228,000 and in respect of which HMRC say that Mr Cooper has not provided any credible explanation. This income has therefore been treated by HMRC as trading income. After deduction of estimated expenses and capital allowances, HMRC have arrived at a taxable profit of £90,355.

200. Mr Birkbeck suggested that two payments (totalling £17,000) had been incorrectly included and that these were in fact payments out of Mr Cooper's bank accounts rather than payments into his accounts. However, on looking more closely at HMRC's figures and the payments they have identified, we are satisfied that HMRC have not included these two payments in their total of £228,000.

201. As far as the remaining payments are concerned, the position is different to the deposits in the previous two tax years as Mr Birkbeck does not suggest that these are further loans from Mr Evans but submits that the deposits simply represent Mr Cooper moving money from one account to another to ensure that there is sufficient money in the recipient accounts to meet the expenses which he pays from those accounts. He reminded the Tribunal that, at this point in time, Mr Cooper had access to significant funds following the receipt of the deposit of almost £730,000 in relation to the three barges deal at the end of October 2007.

202. In support of this, Mr Birkbeck took us to some of the entries in Mr Cooper's bank statements relating to the payments in question showing a deposit into Mr Cooper's account made in Epping (i.e. close to SO's workshop) and a second payment being a funds transfer which had no reference. Mr Birkbeck submits that the fact that the funds transfer had no reference is clear evidence that it did not, for example, come from a customer and is therefore consistent with this simply being a transfer from another bank account held by Mr Cooper.

203. As far as the evidence of other bank accounts is concerned, Mr Birkbeck referred in the evidence to details of a number of different bank cards held by Mr Cooper including Bank of America, Citibank and Halifax.

204. Mr Birkbeck again made the point that there is no evidence of any trading transactions being undertaken in this period and so it would be surprising if, all of a sudden, there were

numerous receipts representing trading income. He argues that the fact that all of the deposits are round figures would also support the conclusion that the payments do not represent trading income but instead represent transfers from other accounts. He also suggested that the deposits cease after April 2009 and that this again would suggest that the deposits are not trading income as it would be odd for the trade suddenly to come to an end at that stage with no further payments into the accounts.

205. Mr Birkbeck's conclusion therefore is that the explanation that the deposits represent transfers from other accounts is more plausible than them representing trading income.

206. Mr Wilkinson did not make any specific submissions on behalf of HMRC in relation to the payments in question. He simply asserts that Mr Woods acted reasonably in calculating the trading profits which were the subject of the assessment and that it is up to Mr Cooper to show that the assessment is wrong.

207. In our view, Mr Cooper has not discharged that burden of proof.

208. Mr Cooper's assertion that the payments in question represent transfers from other bank accounts of his is unsupported by any of the documentary evidence. Given that it would have been straightforward for Mr Cooper to provide details of the bank accounts from which the payments were made and copies of the statements for those bank accounts evidencing the payments, we cannot accept what he has told us without any such supporting evidence, particularly as there are suggestions in the evidence which we do hold that what he is saying cannot be correct.

209. Mr Birkbeck reminded us that Mr Cooper had access to the deposits from the three barges deal totalling almost £730,000. However, it is clear from SOL's bank statements (and confirmed by Mr Cooper) that only £150,000 of this was transferred to his own personal accounts. Of the balance, £450,000 was paid to his ex-wife, £64,000 was used to buy a Bentley and the balance of around £56,000 was left in SOL's bank account. It is clear from the bank statements we have that the £150,000 transferred into Mr Cooper's personal accounts and the £56,000 left in SOL's bank account were gradually dissipated by the payment of day to day expenses. There is no evidence in those bank statements of any significant transfers to other bank accounts.

210. In addition, the details of the bank cards referred to by Mr Birkbeck have been annotated by Mr Cooper. The notes show that the Bank of America and Citibank accounts never had any significant funds in them. The Halifax account is stated no longer to be active although it is not clear what date the account ceased to be active. The notes also disclose an account with Santander although no details are provided.

211. Even if we were to accept that the deposits were indeed transfers from other bank accounts of which we (and HMRC) have no details, this does not show that the deposits do not represent trading income as we have no information about where the money in those other bank accounts might have come from. One thing we do know is that the money in those bank accounts does not derive from the three barges deposit as that has been accounted for elsewhere. It is therefore perfectly possible that if Mr Cooper did have other bank accounts which held significant funds, those funds themselves derived from trading activities. Mr Cooper has chosen not to give us any details of the accounts from which he suggests the transfers have been made and he cannot therefore expect us to accept that the funds do not represent trading income.

212. The assessment for the tax year ended 5 April 2009 therefore stands good.

Tax year ended 5 April 2010

213. The income which has been assessed by HMRC represents the purchase price for the four hovercraft and the tug yacht in respect of which invoices were issued on 5 February 2010. The total amount exclusive of VAT is £374,469. Again, HMRC have made allowances for expenses and capital allowances giving rise to a taxable profit of £259,505.

214. Mr Birkbeck's submission in relation to this tax year is very simple. He points out that the only payments received by Mr Cooper during the relevant tax year were the initial payments of £20,000 for the hovercraft and £17,000 for the tug yacht (both inclusive of VAT) and that given that trading profits should be taxed on an accruals basis under generally accepted accounting principles, the balance of the purchase price should not be assessed as trading income for the relevant year as it had not become due and payable.

215. In support of this, Mr Birkbeck referred to the contracts for the construction and supply of the hovercraft and the tug yacht. These make it clear that payments are to be made in stages based on the work completed. There is, he says, no suggestion that any payments other than the initial payments had become due prior to 6 April 2010.

216. The expenses allowed by HMRC total £61,448 net of VAT. HMRC have also allowed capital allowances of £53,516. As Mr Cooper does not take issue with the amount allowed for expenses, Mr Birkbeck submits that if the only income is £37,000 inclusive of VAT (approximately £31,500 net of VAT), there is clearly no taxable profit for this tax year.

217. Mr Wilkinson accepts that the taxable profits should be calculated on the accruals basis and that it is therefore necessary to look at what payments were due during the relevant tax year. He did not suggest that any payments were due other than the payments of £37,000 which were actually made.

218. Mr Wilkinson did however submit that, if most of the work was done after the end of the tax year, HMRC's allowance for expenses should be reduced. He did not however suggest on what basis this should be calculated.

219. We accept Mr Birkbeck's submission that it is only the payments which were actually made during the tax year (or any which were due before the end of the tax year) which should be taken into account in calculating Mr Cooper's trading profits for the relevant tax year. There is no evidence that any payments were due other than the £37,000 actually paid. This means that Mr Cooper's taxable income was approximately £31,500 (exclusive of VAT).

220. At least two items of expenditure for the year are actual expenses paid, representing the rent for the workshop and the office. These total just over £25,000. It is not clear which of the other figures for expenses allowed by HMRC during the year are estimates and which are taken from documents seen from HMRC. However, in the absence of any suggestion from Mr Wilkinson as to how we should adjust the expenses, we would accept on the balance of probabilities that, of the remaining expenses and capital allowances (totalling almost £90,000), a sufficient amount would remain deductible to mean that Mr Cooper would have no taxable profit for the tax year ended 5 April 2010. The assessment for this year is therefore reduced to nil.

SUMMARY OF OUR DECISIONS IN RELATION TO THE INCOME TAX DISCOVERY ASSESSMENTS

221. The assessment for the tax year ended 5 April 2007 is cancelled as it is out of time.

222. The assessment for the tax year ended 5 April 2008 is reduced to reflect the fact that the £18,500 deposit paid by Mr John Holland was refunded and so does not form part of Mr Cooper's trading profits for the year.

223. The assessment for the tax year ended 5 April 2009 is upheld as Mr Cooper has not discharged the burden of showing, on the balance of probabilities, that he has been overcharged by the assessment.

224. The assessment for the tax year ended 5 April 2010 is reduced to nil.

225. We turn now to deal with Mr Cooper's appeal against the two VAT assessments for the 06/10 and 09/10 periods of account. We deal with the question of penalties both in relation to VAT and income tax at the end of our decision.

THE VAT ASSESSMENTS

VAT period 06/09

226. As mentioned above, Mr Cooper applied to be registered for VAT in respect of his sole trade carried on through SO in April 2010. He asked for registration to be back dated to April 2007. After some correspondence, HMRC agreed to register SO with effect from April 2007. The first VAT return which was due was therefore in respect of the period from April 2007 to June 2010.

227. Mr Cooper submitted a VAT return for the 06/10 period. This showed a repayment due of £10,316.

228. Following HMRC's investigation, their conclusion is that Mr Cooper in fact had a VAT liability of £69,671. Unfortunately, we do not have a breakdown as to how this figure was calculated. However, although it takes into account inputs and outputs throughout the whole of the period of account, the most significant element relates to the VAT on the sale of the four hovercraft and tug yacht which were both invoiced on 15 February 2010 and in respect of which VAT of £65,531.92 in total was charged.

229. Mr Cooper's explanation for omitting the full amount of these sales from his VAT return was that he thought he only needed to include the payments he had received. He did not believe that he needed to include the entire amount of the invoices when the full amount had not been paid.

230. Mr Birkbeck accepts that the tax point is the date of the invoice and so the full amount of the invoices should have been included as outputs during this VAT period. He does however point out that, as the contracts were never completed, Mr Cooper would have been able to claim relief from VAT in respect of the unpaid amounts but accepts that any such claim would now be out of time.

231. Based on this there can be no doubt that the assessment for the 06/10 VAT period of account should be upheld.

VAT period 09/10

232. Mr Cooper claimed a VAT repayment of £78,032 for the 09/10 VAT period. This is attributable entirely to the VAT on the purchase by Mr Cooper of the WIG boat design and the model aircraft, the invoices for both of which are dated 5 September 2010. The VAT in respect of the WIG boat design was £56,000 and the VAT in respect of the model aircraft was £22,032.50 making a total of £78,032.50.

233. HMRC's decision in relation to this VAT period is to allow a credit of £12,707.50, a reduction of £65,325.

234. Again, we do not have a breakdown as to exactly how these figures are calculated. However, it is clear from the documents provided by HMRC that they have allowed credit for the input tax on the purchase of the model aircraft of £22,032.50 but that they have refused any credit for the input tax on the purchase of the WIG boat design of £56,000. Although Mr

Birkbeck dealt with both of these contracts in his submissions, it is therefore only the contract for the purchase of the WIG boat design which is relevant.

235. There was some uncertainty as to whether Mr Cooper was in fact appealing against the refusal to allow credit for the VAT in respect of the purchase of the WIG boat design as he had previously said to HMRC that he no longer wished to pursue this claim. However, Mr Cooper confirmed at the hearing that this did form part of his appeal.

236. In order to understand the position put forward by the parties, it is necessary to examine the transaction in a little more detail.

237. Mr Cooper and Mr Evans say that SDS agreed to sell a WIG boat design to SO which Mr Evans, using his engineering background and his research at Cranfield University, had developed. We were told that a WIG boat is a boat which can fly at very low altitudes above water making it much faster and more fuel efficient than a normal boat.

238. Mr Cooper and Mr Evans say that the plan was for Mr Cooper to pay Mr Evans in Iran. The intention was then that Mr Evans, as a British national, would be able to bring the funds to the UK and to use them to pay SO for the four hovercraft and the tug yacht.

239. However, the evidence from Mr Evans and Mr Cooper is that, due to the UN sanctions in relation to Iran, Mr Evans was not able to bring the money out of Iran and that the contract was therefore cancelled and the money returned to Mr Cooper's representatives in Iran some time in 2011.

240. Mr Birkbeck's position is that the only reason HMRC have put forward for denying the input tax credit is that they do not believe that the transaction took place. This is based on Mr Woods' conclusion that it is commercially unlikely that Mr Cooper would agree to pay the purchase price to Mr Evans in Iran at a time when SDS owed SO somewhere between £300,000 - £400,000 for the hovercraft and the tug yacht. Mr Woods' evidence was that he would expect the payments under the various contracts to be set off against each other rather than Mr Cooper paying SDS in Iran, the money being brought to the UK and SDS then paying Mr Cooper.

241. Mr Birkbeck submits that HMRC cannot ignore a transaction simply because of a view that a particular officer has taken as to the commerciality of the transaction. In any event, Mr Birkbeck argues that Mr Woods' views ignore the fact that implementing the transaction in the way described by Mr Evans and Mr Cooper would have allowed Mr Cooper's funds in Iran to be brought to the UK and to end up in his hands in the UK by way of payment for the hovercraft and the tug yacht.

242. One final point made by Mr Birkbeck is that HMRC do not appear to have questioned whether or not the sale of the WIG boat design was genuine when looking at the VAT position of SDS. That company was required to account for the output tax. However, it was unable to pay the VAT due to the inability to extract funds from Iran and the company was ultimately struck off.

243. Given that the transaction was never completed, Mr Birkbeck accepts that there could no doubt be some adjustment to the VAT position but, as with the tug yacht and hovercraft contracts, suggests that the time limit for any adjustment would now have expired.

244. On this basis, Mr Birkbeck submitted that in order to ensure consistency between the two VAT periods, there were two ways of dealing with the position:

> (1) Look at both periods in retrospect and assess them on the basis of the end result. The effect of this would be that in relation to the 06/10 VAT period, the only outputs would relate to the £37,000 (inclusive of VAT) actually paid by SDS. As far as the 09/10 VAT period is concerned, there would be no input tax credit as no supply in fact took place following the cancellation of the contract.

(2) The alternative would be to accept that there was a supply in the 06/10 VAT period but also that there was a supply in the 09/10 VAT period, thus allowing the input tax credit. It would be accepted that it was now too late to adjust the position for either of those two VAT periods as a result of the cancellation of the contracts.

245. Mr Wilkinson did not have any additional submissions to make on behalf of HMRC. He confirmed that the basis of HMRC's case is that it is not credible for Mr Cooper to have agreed to make a payment in Iran when he was owed a substantial amount of money by SDS in the UK.

246. In order to succeed, Mr Cooper has to satisfy us on the balance of probabilities that SDS did in fact make a taxable supply of the WIG boat design. Based on the evidence we have, we are not satisfied that such a supply took place.

247. Although SDS issued an invoice for the sale, we have not been provided with any detailed documentation relating to the design, the intellectual property rights involved or any evidence of any protection of any intellectual property rights.

248. The only agreement we have been provided with is what purports to be a non-disclosure agreement but which states in the background section that:

> "The Assignor owns the Assigned Rights, and has agreed to assign the Assigned Rights to the Assignee on the terms of this assignment."

249. There is however no definition of the Assigned Rights, the Assignor or the Assignee. The main body of the agreement does not effect the assignment of anything but is instead a fairly standard form agreement for one party to disclose information to another party and for the other party to keep that information confidential. The non-disclosure agreement (not surprisingly) does not mention any amount which might be payable by Mr Cooper to SDS.

250. It is apparent from Mr Woods' evidence that there are some more detailed documents in existence in relation to the design itself as the notes of the second meeting between Mr Woods and Mr Cooper refer to a document which is apparently over 100 pages long. It does however appear from what is reported to have been said at that meeting that some of this was generic research carried out by someone other than Mr Evans although other parts of the document were prepared by Mr Evans.

251. In his witness statement, Mr Cooper suggests that the non-disclosure agreement would enable Mr Cooper to develop and manufacture the WIG boat. However, it is not at all clear from this agreement how that would be the case. We also have no evidence as to how Mr Cooper thought that SO would be able to finance the development and manufacture of the WIG boat. If what Mr Cooper is reported as having said to Mr Woods at their first meeting is to be believed, he had significant debts and no assets other than the £300,000 which SDS owed him for the hovercraft and tug yacht.

252. The evidence from Mr Cooper and Mr Evans was that one of the purposes of structuring the transaction in the way that it was, was to enable Mr Cooper's money to be brought out of Iran to the UK. This however conflicts with what Mr Cooper told Mr Woods at their first meeting where he said that the money to pay for the WIG design had been borrowed from his brother-in-law in Iran as he had by then exhausted all of the funds which he had inherited from his grandfather.

253. Even if Mr Cooper did have funds in Iran which he wanted to repatriate, this does not shed any light on whether SDS genuinely supplied the WIG boat design to Mr Cooper. Given the lack of evidence of what was in fact supplied (for example a proper contract), the lack of evidence that any design was viable and the lack of any evidence that Mr Cooper was in a

position to exploit any design, we are not persuaded on the balance of probabilities that SDS did in fact supply a WIG boat design to Mr Cooper trading as SO.

254. Our conclusion therefore is that HMRC were right not to allow credit for the VAT in respect of this transaction.

PENALTIES

Civil evasion penalty – VAT period 06/10

255. In relation to the 06/10 VAT period, where it is accepted that Mr Cooper failed to include the sales of the four hovercraft and the tug yacht as outputs in his VAT return, HMRC have charged a civil evasion penalty under s 60 Value Added Tax Act 1994. They are only able to do this where the conduct of the individual is dishonest. Mr Wilkinson accepts that HMRC bears the burden of showing, on the balance of probabilities, that Mr Cooper's actions (or omissions) were dishonest.

256. In relation to this VAT period, Mr Wilkinson submits that Mr Cooper was aware that he was receiving trading income and that he should have known that this income had to be disclosed for VAT purposes. Mr Woods gave evidence that the return which Mr Cooper submitted showed £33,000 of outputs which, says Mr Wilkinson, supports the proposition that Mr Cooper was aware that trading income needed to be disclosed on his VAT return.

257. Mr Birkbeck accepts that if Mr Cooper was lying about his trading income, this would constitute dishonesty for the purposes of s 60 Value Added Tax Act 1994. However, he submits that HMRC cannot succeed as they have not pleaded dishonesty in sufficient detail in their statement of case and Mr Wilkinson did not put any allegations of dishonesty to Mr Cooper in cross-examination.

258. In relation to the first point, Mr Birkbeck referred to the decision of the Northern Ireland Court of Appeal in *Ulster Metal Refiners Limited v HMRC* [2017] NICA 26. Although this was a Northern Ireland case, Mr Birkbeck submits that it should be followed as the relevant part of it is based on a decision of the House of Lords. As far as pleadings are concerned, the Northern Ireland Court of Appeal said the following at [36]:

> "It is well established that in ordinary civil litigation involving allegations of fraud, the obligations in respect of pleadings are heightened. The fraud must be 'distinctly alleged' and it must be sufficiently particularised. As Lord Millet said in *Three Rivers District Council v Governor & Co of the Bank of England (No. 3)* [2003] 2 AC 1 at para [186]:
>
> > 'This is only partly a matter of pleading. It is also a matter of substance. As I have said, the defendant is entitled to know the case he has to meet. But since dishonesty is usually a matter of inference from primary facts, this involves knowing not only that he is alleged to have acted dishonestly, but also the primary facts which will be relied upon at trial to justify the inference. At trial the court will not normally allow proof of primary facts which have not been pleaded, and will not do so on a case of fraud. It is not open to the court to infer dishonesty from facts which have not been pleaded, or from facts which have been pleaded but are consistent with honesty. There must be some fact which tilts the balance and justifies an inference of dishonesty, and this fact must be both pleaded and proved.'."

259. As far as cross-examination is concerned, Mr Birkbeck took us to the decision of the High Court in *Mohammed Suhaib Sait v The General Medical Council* [2018] EWHC 3160 (Admin). After reviewing previous cases, the judge had this to say at [51-54] about the importance of cross-examination in ensuring that the court's findings are fair:

> "51. These iconic voices from the past seem to me to express exactly why 'testing the evidence in the crucible of cross-examination' is the best way of gaining 'the true and clear discovery of the truth'; it is the best method of trial for 'sifting out the truth'.
>
> 52. That was certainly the view of Carr J in *Williams* where a solicitor had been accused of serious dishonesty. At [94] – [95] she stated:
>
> > '94. I fully accept that Mr Williams was on notice that he had a case to answer on the £3.9m representation (even if only as part of the build-up to an overarching case of deceitful misrepresentation as to value), and that he had, and took, the opportunity to deal with it in his witness statement. But he was not cross-examined at all on it. The question is whether that goes far enough in terms of fairness in all the circumstances. This is not in my view a question of the strict application of the rule in *Browne v Dunn* (supra). The situation is more nuanced, in the context of fairness overall.
> >
> > 95. On careful consideration, I have concluded that it did not. This was the most serious of allegations against a practising solicitor. The case involved multiple allegations, in what was a complex case. This was not a 'single issue' case, where it was obvious that the issue would, or might, end up as a central finding (and the only finding of dishonesty) in the case. There was ambiguity in the pleaded case. In all the circumstances, it was necessary for Mr Williams to be challenged directly on the point so that his evidence could be tested properly before a finding of dishonesty could be made. The Tribunal could not fairly find him to be dishonest without the most careful consideration of what he said in his defence (as it was put by Lewison LJ, in *Clydesdale Bank* (supra) at [52]). He should have had the opportunity to respond to the SRA's allegations against him orally in the witness box, and to be judged on that evidence. I do not accept that the court should speculate in this case that such evidence would have been an 'empty technicality'. Moreover, Mr Williams could have been re-examined on the point.'
>
> 53. I do not read these paragraphs to suggest that cross-examination is not generally necessary where the allegation is either simple or single-issue. If the allegation is serious (and an allegation of sexually motivated misconduct against a doctor is about as serious as it gets) then in my judgment the allegation must be fully and squarely put in cross-examination to the accused doctor. The content of the doctor's replies is, as well as his demeanour, will equip the Tribunal to decide whether the allegation is, or is not, true.

> 54. *Chen v Ng* fully supports my view. It was not a particularly complex case and the grounds on which the judge disbelieved Mr Ng were rational and plausible. Yet on the facts of that case it was unfair for judgment to be thus rendered without those grounds having been squarely put to him in cross-examination."

260. Even before the start of these proceedings, it was clear from HMRC's penalty assessment that Mr Cooper was being accused of dishonesty. The letter states as follows:

> "… we found that you had not declared the right amount of tax. This was because the level of sales were deliberately suppressed.
>
> We consider that these actions were dishonest."

261. In relation to this penalty, HMRC's statement of case contains the following at paragraph 115:

> "Prior to 1 April 2008, a penalty was chargeable under s 60 VAT Act 1994 where a taxpayer does any act or omits to take any action, and the conduct involves dishonesty. The Respondent submits that on the balance of probabilities in this case, the Appellant knew that he had breached the VAT registration threshold in 2008/09. The Respondent therefore submits that the Appellant acted dishonestly."

262. We accept that HMRC's statement of case is not clear about the facts giving rise to the dishonesty as it refers to the unidentified deposits resulting in a breach of the VAT registration threshold in 2008/09 whereas the main omission in respect of the 06/10 VAT period is the failure to declare the full amount of the invoices for the four hovercraft and the tug yacht as outputs for that VAT period.

263. Mr Cooper's explanation for the failure was that he thought he only had to include the amounts which had actually been paid during the relevant VAT period (i.e. £37,000 including VAT) and not the full amount of the invoices. Clearly, if he held this as a genuine belief, this does not constitute dishonesty. Mr Wilkinson did not challenge Mr Cooper on this during cross-examination. The only point he put to Mr Cooper on this issue was to suggest that he did not declare the outputs in relation to the hovercraft and the tug yacht when he issued the invoices but did not probe any further in relation to the reasons why there might have been an under declaration. Mr Cooper's response was that he did disclose these transactions but this is still consistent with him declaring the amounts actually paid rather than the full amount of the invoices.

264. HMRC accept that Mr Cooper declared outputs of £33,000 in the 06/10 VAT period. We do not have any evidence as to whether this included the deposits for the hovercrafts and the tug yacht (approximately £31,500 net of VAT) but it is certainly possible that it could have done.

265. In the circumstances, we are not satisfied that Mr Cooper acted dishonestly in relation to the VAT return for this period. As a result, HMRC were not entitled to charge a penalty under s 60 Value Added Tax Act 1994. They may have been entitled to charge a penalty under s 63 Value Added Tax Act 1994 (where the penalty is for a mis-declaration or for neglect) but HMRC have not charged a penalty under that section and we cannot impose one.

266. Mr Cooper's appeal on this point therefore succeeds and the penalty assessment is cancelled.

Inaccuracy penalty – VAT period 09/10

267. The penalty for the 09/10 VAT period has been charged under schedule 24 Finance Act 2007 which had by then replaced the penalty provisions in Value Added Tax Act 1994 in respect of inaccurate VAT returns.

268. The penalty charged by HMRC is £30,866 being 47.25% of the tax at stake. The penalty has been calculated on the basis that the inaccuracy was deliberate and that the disclosure was prompted by HMRC's enquiry.

269. Again, Mr Wilkinson accepts that HMRC have the burden of showing that the inaccuracy was deliberate. Mr Wilkinson referred to the decision of the First-tier Tribunal in *Auxilium Project Management v HMRC* [2016] UKFTT 249 (TC) where the Tribunal stated at [63] that:

> "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."

270. Both parties agree that, for practical purposes, there is no difference between this test and the test for dishonesty.

271. The inaccuracy alleged by HMRC is Mr Cooper's inclusion of the input tax in relation to the WIG boat design. Mr Wilkinson submits that the inaccuracy was deliberate as the claim for the credit was included despite the fact that there was in fact no supply of the WIG boat design.

272. Mr Birkbeck raises the same criticisms about pleading and cross-examination as he did in relation to the penalty for the 06/10 period.

273. In this case, the copy of the penalty assessment which we have merely refers to the fact that there has been an inaccuracy. It does not say whether that inaccuracy was deliberate or careless. HMRC's statement of case makes it clear that they are alleging that the inaccuracy was deliberate although nothing is said in the statement of case as to the basis on which HMRC have reached this conclusion.

274. On the other hand, Mr Wilkinson did clearly put the point about whether this was a genuine transaction to Mr Cooper in cross-examination.

275. Despite the deficiencies in HMRC's statement of case, it is clear to us from the voluminous correspondence that Mr Cooper was well aware that HMRC held the view that the WIG boat transaction did not really happen. It is equally clear that HMRC had thought (based on clear statements made by Mr Cooper) that the claim for credit for VAT in respect of the WIG boat transaction had been withdrawn. It is therefore understandable that HMRC did not deal with this in any detail in their statement of case.

276. We do not therefore believe that there is any procedural irregularity or unfairness in the way that this point has been dealt with by HMRC.

277. The question therefore is whether we are satisfied on the balance of probabilities that the WIG boat transaction did not involve a genuine supply and that Mr Cooper knew this.

278. It follows from our conclusion in respect of the VAT assessment itself that Mr Cooper has not satisfied us on the balance of probabilities that there was a genuine supply. However, in relation to that issue, the burden of proof was on him. The fact that he has been unable to persuade us on the balance of probabilities that there was a genuine supply does not automatically mean that we should be satisfied, when the burden of proof is on HMRC, that there was no genuine supply. However, it is a strong pointer in that direction.

279. The reasons why we are not satisfied that a supply of the WIG boat design took place are set out in paragraphs [218-224] above. Based upon the evidence discussed in those paragraphs, we think it is more likely than not that SDS did not in fact supply a WIG boat design to Mr Cooper trading as SO.

280. Given this finding of fact, it is difficult to escape the conclusion that Mr Cooper must have been aware that no supply had in fact taken place and that he was not therefore entitled to claim any input tax on his VAT return for the 09/10 VAT period.

281. Our conclusion therefore is that the inaccuracy in Mr Cooper's VAT return was deliberate within the meaning of schedule 24 Finance Act 2007 meaning that HMRC's starting point of imposing a penalty of a minimum of 35% and a maximum of 70% of the unpaid tax was correct.

282. We accept that the allowance for disclosure made by HMRC (a reduction of 65% within the penalty range) is appropriate.

283. Taking into account all the circumstances, we do not think that there are any special circumstances which would justify a further reduction in the amount of the penalty.

284. The penalty relating to the 09/10 VAT period is therefore upheld.

Income tax penalties

285. HMRC have charged penalties under s 93 Taxes Management Act 1970 in respect of Mr Cooper's failure to file self-assessment tax returns for the relevant tax years.

286. Section 93(5) Taxes Management Act 1970 allows HMRC to charge a penalty not exceeding the amount of tax at stake but they have complete discretion under s 100 Taxes Management Act 1970 as to the amount of the penalty subject to this limit. Similarly, the Tribunal has discretion to reduce or increase the penalty to such amount as it considers appropriate (s 100B Taxes Management Act 1970).

287. Mr Birkbeck accepts that if the Tribunal upholds the assessments, penalties will be payable. He does not seek to argue that there was any reasonable excuse for the failure to file the returns. His only submission is that, to the extent that the level of the penalties reflects HMRC's view that Mr Cooper acted dishonestly, there should be a greater reduction in the amount of the penalties should the Tribunal conclude that Mr Cooper's actions were not dishonest.

288. In response to this, Mr Wilkinson submits that the 50% reduction allowed by HMRC is reasonable in the circumstances.

289. Unlike the VAT penalties, there is no requirement for HMRC to show that Mr Cooper was dishonest or that his failure to file returns was a deliberate attempt to evade the payment of tax. No doubt this is a relevant factor in setting the level of the penalty but it is no more than that.

290. We have been unable to accept Mr Cooper's explanation for the unidentified deposits which have formed the basis of the assessments for the tax years ended 5 April 2007 and 5 April 2009 and part of the assessment for the tax year ended 5 April 2008. We have also not accepted Mr Cooper's assertion that the deposit for the three barges transaction which forms the vast majority of the basis for the assessment for the year ended 5 April 2008 is refundable and was in fact refunded.

291. We also take into account the fact that Mr Cooper's explanation for the deposits into his bank accounts has changed significantly between the first meeting with Mr Woods and the hearing before the Tribunal as well as the fact that it would have been quite easy for him to have provided further evidence in relation to many of those deposits had he chosen to do so

(for example, the payments in the tax year ended 5 April 2009 which he says are transfers between bank accounts).

292. Taking all of this into account, our view is that the 50% reduction allowed by HMRC is reasonable and we do not think that the penalties should either be increased or reduced on this basis.

293. We have of course decided that the assessment for the tax year ended 5 April 2007 must be cancelled as it was issued outside the statutory time limit allowed to HMRC. It does not however follow that no penalty is due. The relevant parts of s 93 Taxes Management Act 1970 provide as follows:

> "93. **Failure to make return for income tax and capital gains tax**
>
> (1) This section applies where -
>
> (a) any person (the taxpayer) has been required by a notice served under or for the purposes of section 8 or 8A of this Act (or either of those sections as extended by section 12 of this Act) to deliver any return, and
>
> (b) he fails to comply with the notice.
>
> …
>
> (5) Without prejudice to any penalties under sub-sections (2) to (4) above, if –
>
> (a) the failure by the taxpayer to comply with the notice continues after the anniversary of the filing date, and
>
> (b) there would have been a liability to tax shown in the return,
>
> the taxpayer shall be liable to a penalty of an amount not exceeding the liability to tax which would have been so shown.
>
> …
>
> (7) If the taxpayer proves that the liability to tax shown in the return would not have exceeded a particular amount, the penalty under sub-section (2) above, together with any penalty under sub-section (4) above, shall not exceed that amount."

294. It is clear that liability to a penalty under s 93 Taxes Management Act 1970 depends on whether the return would have revealed a liability to tax and not on whether HMRC have successfully issued a discovery assessment.

295. Although s 90(7) relates specifically to the fixed penalties which are payable under s 90(2) and (4), it confirms the conventional position in relation to any challenge by a taxpayer to an assessment to tax that it is up to the taxpayer to show that any liability to tax would not exceed a particular amount.

296. Mr Cooper has failed to show that the amount assessed by HMRC is not due. Therefore, even though the assessment must be cancelled as it was issued out of time, the penalty is still based on the amount of the tax which HMRC say is due.

297. Although the time limit for assessing penalties was not raised by either of the parties, we should mention this briefly given our conclusion that the assessment for the tax year ended 5 April 2007 was out of time.

298. Section 103 Taxes Management Act 1970 gave HMRC six years from the date the penalty was incurred to issue a penalty determination. As mentioned above, the penalty was incurred in accordance with s 93(5) Taxes Management Act 1970 as a result of a tax return not having been filed by the anniversary of the filing date. In this case, the filing date was 31 January 2008 and so the penalty was incurred on 1 February 2009. As the penalty was assessed in December 2013, this was well within the six year time limit.

299. The penalties for the tax years ended 5 April 2007 and 5 April 2009 are therefore confirmed. The penalty for the tax year ended 5 April 2008 is reduced to reflect the reduced amount of tax payable as a result of the exclusion of the £18,500 received from John Holland but is otherwise confirmed. The penalty for the tax year ended 5 April 2010 is reduced to nil given that, based on our conclusions above, there is no tax to pay for that year.

SUMMARY OF DECISION

300. The income tax discovery assessments for the year ended 5 April 2007 is cancelled as it was out of time.

301. The income tax discovery assessment for the year ended 5 April 2008 is reduced by excluding income of £18,500, being the deposit paid by Mr John Holland which was refunded.

302. The income tax discovery assessment for the year ended 5 April 2009 is upheld and should stand good.

303. The income tax discovery assessment for the year ended 5 April 2010 is cancelled as no tax is due.

304. The penalties charged under s 93 Taxes Management Act 1970 for the tax years ended 5 April 2007 and 5 April 2009 are upheld.

305. The penalty charged under s 93 Taxes Management Act 1970 for the tax year ended 5 April 2008 is reduced to reflect the reduced amount of tax payable as a result of the exclusion of the £18,500 received from John Holland but is otherwise confirmed.

306. The penalty charged under s 93 Taxes Management Act 1970 for the tax year ended 5 April 2010 is reduced to nil.

307. The VAT assessment for the 06/10 period of account is confirmed.

308. The VAT decision in relation to the 09/10 period of account is also confirmed.

309. The civil evasion penalty relating to the 06/10 VAT period is cancelled as we are not satisfied that Mr Cooper's conduct was dishonest.

310. The penalty for the inaccuracy in Mr Cooper's VAT return for the 09/10 period of account is upheld.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

311. 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.

ROBIN VOS
TRIBUNAL JUDGE

RELEASE DATE: 02 DECEMBER 2019