



TC01505

Appeal number TC/2010/07167

Rent-a-room relief – main residence – question of fact – appeal dismissed

FIRST-TIER TRIBUNAL

TAX

MICHELINA WOODS

Appellant

- and -

**THE COMMISSIONERS FOR HER MAJESTY'S
REVENUE AND CUSTOMS (INCOME TAX)**

Respondents

**TRIBUNAL: ANDREW LONG (TRIBUNAL JUDGE)
TERENCE BAYLISS**

Sitting in public at Temple Court Birmingham B4 6EQ on Friday 15 April 2011

The Appellant in person

Suzanne Whitley, Presenting Officer, for the Respondents

DECISION

1. The Appellant, Mrs Michelina Woods, appeals against assessments to income tax issued on 12 February 2010 for the three tax years ended 5 April 2007 under section 28A (1) and (2) Taxes Management Act 1970 ('TMA') and against discovery assessments for the four tax years ended 5 April 2004 under s 29 TMA. Penalties were issued on 17th March 2010 for incorrect returns for the seven tax years ended 5 April 2007 under section 95 TMA. The assessments and penalties followed an enquiry into Mrs Woods tax returns which had been opened because of disallowable expenditure being claimed for a Mercedes vehicle, and a claim within the rent a room scheme for rental income received.
2. HMRC contend that the Appellant fraudulently or negligently submitted incorrect returns for the seven years ended 5 April 2007. The Appellant disputes this.
3. There were three principal issues for the Tribunal to determine. First, whether certain property let by the Appellant was her main residence during the relevant tax years and thus whether rental income falls within the Rent a Room scheme. Secondly, whether certain business expenses were allowable as deductions. Thirdly, the amount (if any) of penalties to be imposed.
4. The evidence. We heard evidence from Mr Molloy, Inspector of Taxes. He had supplied a full detailed witness statement, which included references to the discussions with the Appellant about the issues relevant to the appeal. We also heard oral evidence from the Appellant; she had not supplied a formal statement but orally confirmed the written material which she had sent to the Tribunal. There were also five bundles of documents. This included notes of meetings between Mr Molloy and Mrs Woods, including a record of her responses to issues raised by Mr Molloy. Many of the issues previously between the parties had been narrowed or agreed by the time of the hearing. Bundle 5 contained an updated summary of the position as at the hearing date.
5. The background law. There was no substantive dispute on the law. On the onus of proof, this is on the Appellant to demonstrate that the normal time-limit assessments for the three years ending 5 April 2007 are, as she asserts, excessive. For the discovery assessments the onus of proof rests with HMRC to show that the conditions for discovery are met. Once those conditions are met, the onus of proof moves to the Appellant to show that the assessments are, as she asserts, excessive.
6. On penalty, the onus of proof is on HMRC to establish fraudulent or negligent conduct and for the Tribunal to determine the penalty (if any).
7. Section 12 TMA requires the person who has to submit tax returns under s 8 TMA to retain all records relating to the completion of the return to the fifth anniversary of the 31 January next following year of assessment.

8. By s34 Income Tax (Taxation of Income) Act 2005 ("ITToI") in calculating the profits of a trade, no deduction is allowed for expenses unless incurred wholly and exclusively for the purposes of the trade

5 9. *Issue One. Rent-a-room.* The law concerning rent-a-room relief is principally contained in s784-789 ITToI. By s784 (1) (Overview) relief is provided "on income from the use of furnished accommodation in an individual's only or main residence". By s786(1)(c) an individual has rent-a-room receipts for a tax year only if "for some or all of that period the residence is the individual's only or main residence"

10 10. The background facts were not in dispute. Mrs Woods is a self employed mortgage adviser. She has been married since September 1996. She has two children, the younger born in 2004. Mrs Woods confirmed that she had owned four properties during the relevant period covered by the enquiry. The relevant properties were 13 Willington Street, Nuneaton of which she was the sole owner, which had been purchased in January 1986. Secondly, 21 Manor Court Road, Nuneaton of which she
15 was the sole owner, purchased in 1991. Thirdly, 345 Queen Elizabeth Road, Nuneaton, owned from 2003 to 2009. Fourthly, 27 Fife Street, Nuneaton purchased jointly with her husband in June 2005.

20 11. During the enquiry Mrs Woods told Mr Molloy that Tracey Knight moved into 13 Willington Street in October 2000 and moved out in August 2005. Refurbishment works were done from August 2005 to February 2006. Mr Miles and Mrs Miles were then resident from May 2006 to March 2007 and then Miss S Davidson moved in during July 2007.

25 12. Mrs Woods also said that the property at 345 Queen Elizabeth Road was purchased in February 2003 and vacant until Mrs T Towers moved in. She did not pay rent at first but signed a contract to pay rent of £80 per week from 21 August 2005. After Mrs Towers left a Tracey Phillips moved in during May 2006.

30 13. Mrs Woods received rental income from 13 Willington Street. She contended that income received was covered by rent-a-room relief as this property was her main residence. Mrs Woods had not kept rental income records for 13 Willington Street. She has also said that for some times she had occupied it, as had members of her family, although she did not provide details of which member of her family or when.

35 14. Mrs Woods told Mr Molloy that her husband and family lived at 21 Manor Court Road and that she lived at 13 Willington Street except when it was being repaired. Mrs Woods said that this was her main residence up to June 2007. Mrs Woods said that she moved into 345 Queen Elizabeth Road on 22 May 2006 but, according to Mr Molloy, subsequently changed this to November 2006 and June 2007. The rent-a-room claim was transferred to 345 Queen Elizabeth Road. 345 Queen Elizabeth Road was sold on 22 May 2009 for £60,000.

40 15. 21 Manor Court Road is an extended semi-detached house occupied by Mrs Woods' husband and children. 13 Willington Street is a two bed-roomed terraced property not far from Manor Court Road. Mrs Woods had 21 Manor Court Road as

her address for many purposes (looked at during the period in issue). She is registered on the electoral roll there. She is registered there for council tax purposes. Her credit cards are registered there. Receipts and documentation for car purchase and repairs show her address there. Her vehicle licence application shows her address there. Her car is garaged overnight there, which is the basis on which her car is insured. Documents from the local authority relating to 13 Willington Street have been sent to Mrs Woods at 21 Manor Court Road. Her bank account shows 21 Manor Court Road as her address. A statutory notice from the local authority in relation to tenanted property shows this as her address. Her business is registered as carried out there.

16. There are also indications from the documents that 13 Willington Street might not have been Mrs Woods' main residence. These indications include the lack of records to that effect (but see below). The tenancy agreement produced (in relation to 345 Queen Elizabeth Road) does not have any reference to any rights of Mrs Woods to stay at the property. On its face it is an assured shorthold tenancy, which, as a matter of law, would give the tenants exclusive right to occupy. By a return of information dated 12 May 2004 furnished under s 16 of the Local Government (Miscellaneous Provisions) Act 1976 relating to 13 Willington Street, Mrs Woods described her interest in the land as "property owner", the tenants as Tracey Knight and Stuart Knight and made no reference whatsoever to her own occupation thereof. She also gives her address as care of 21 Manor Court Road.

17. 13 Willington Street would also have been an uncomfortable location for Mrs Woods. The local authority took enforcement action in relation to 13 Willington Street because of disrepair. In May 2004 Mrs Woods stated that there was damage to the property which needed to be repaired. The list of items that needed repair (according to a schedule attached to a notice from the local authority dated 28 April 2004) included "bare electrical wires protruding from the walls" in the front room, a "leaking bath" in the bathroom and kitchen units and kitchen ceiling "damaged by water leak". In a written statement dated 15 May 2004 Mrs Woods stated that "since they (Mr and Mrs Knight) have been residing in the property the damage which needs to be repaired has been done by them the tenants" and "urgent electrical repairs to be done work commencing 17 May 2004 provided access to the property can be obtained" and "no work can be done while tenants are not there because of Rottweiler guard dog...". Mrs Woods has also stated that workmen were frightened by the guard dog such that the workmen were not willing or able to carry out work in the absence of the tenants.

18. In her document for the Tribunal Mrs Woods confirmed that her car was kept and registered at 21 Manor Court Road. This was because the property had a garage and drive for safekeeping, which made it sensible to keep the car there as it is safest. She stated secondly that one has a choice as to where to have one's voters right registered. Thirdly there is also a clear choice as to where post can be sent and that she is entitled to have post sent to wherever she chooses without that, in itself, determining the location to be her residence. In that document she also pointed to periods when 13 Willington Street was empty for renovation and periods when rent was not received from the tenant of 345 Queen Elizabeth Road, resulting in court action for recovery of the monies due.

19. Mr Molloy's statement records what Mrs Woods said about 13 Willington Street when he had a meeting with her in April 2007 during the course of the enquiry. This is recorded in paragraphs 27–30 of Mr Molloy's statement. Mrs Woods said that she bought 13 Willington Street on 30th January 1996 when she was living at her parents' house. The property was purchased in cash and was in a state of disrepair. Following renovation work she moved into 13 Willington Street. Various relatives have lived at 13 Willington Street but Mrs Wood would not give any names. Mrs Woods also stated that she had problems with Mr and Mrs Knight, the previous tenants who changed the locks and she had to have them evicted. They had left the property in a bad state and it was not fit to live in for approximately 12 months. A lot of work needed to be done on it as the house was falling apart. She said action was taken to evict Tracey and Stuart Knight. Mrs Woods had included with her appeal an undated letter from Tracey Knight. Mr Molloy records asking why Mrs Woods had not taken action to prevent the damage if, as she maintained, she was living there. Mrs Woods is recorded as responding by stating that she lived there, as and when she wanted, and the tenants then changed the locks.

20. Mrs Woods' April 2007 description of the previous domestic arrangements at 13 Willington Street is contained in paragraph 30 of Mr Molloy's statement. At 13 Willington Street there was a communal kitchen, a big bathroom, sitting room and separate dining room. There were two bedrooms with one partitioned for the children. She stayed there as and when she wanted to. Some clothes were kept there. Some items of furniture were kept there. Mrs Woods slept there "as and when". Mrs Woods children's slept there "as and when". The tenants and their two children slept in the two rooms upstairs. Mrs Woods slept on a put up bed downstairs but that sometimes if the tenants or their children were away she would use one of the bedrooms. Mrs Woods "mostly ate out". Mrs Woods family ate anywhere "at the house, cafe, or parents' home".

21. Mrs Woods told us, in oral evidence, when being questioned, that she had stayed at 13 Willington Street "most nights". When asked about where she was residing when her second child was born in 2004 she said "at various addresses".

22. In her document to the Tribunal Mrs Woods relied extensively on three specific documents. First, the letter dated 8 May 2003 from the Inland Revenue, Special Compliance Office. In that letter the Inland Revenue (as it then was), having not finalised arrangements for a hearing before the General Commissioners, discontinued proceedings in relation to Mrs Woods' tax returns for the years 1992/1993 to 1999/2000 with Mrs Woods' returns submitted being accepted. Mrs Woods states that "assessments were raised on the same issue regarding my main residence property being 13 Willington Street"

23. Secondly, insurance documentation. A document dated 12 October 2005 from her insurers showed the "insured" as "Mrs Woods" and the address as 13 Willington Street. Perhaps more importantly the buildings insurance statement dated 21 April 2005 was shown to Mrs Woods. That statement had insurance cover to take effect from 5 May 2005 - a period when the property was occupied by tenants. Mrs Woods had been asked to indicate on the form whether she was either the owner occupier or

the landlord. The "owner occupier" box had been ticked and the 'landlord' box left blank. In cross-examination Mrs Woods accepted that she should have informed the insurers of the fact that there were tenants in the property.

24. Thirdly, but most importantly, there was a copy document purportedly signed by Mrs Tracey Knight. The full contents of the document are as follows. Firstly it has the address "13 Willington Street Nuneaton Warwickshire" at the top. There is then a single sentence which reads "Mrs Tracey Knight can confirm that Mrs Woods resided permanently at this address during my time I resided at this address with my husband Mr Stuart Knight". It then contains (in copy form) Mrs Knight's signature.

25. Our assessment of the evidence. We found Mr Molloy to be a straightforward, competent and credible witness. His evidence was in fact not subject to substantive challenge. Mrs Woods principally disagreed with the inferences that he had drawn from the material he had obtained during the enquiry. We had no difficulty whatsoever in accepting Mr Molloy's evidence; moreover his conduct of this enquiry had appeared to us to be diligent, fair and appropriate.

26. The main document for us to consider was that of Mrs Tracey Knight. We find this document unsatisfactory and unhelpful in a number of respects.

27. The issue that it purports to deal with goes to the heart of the case and is fully contested on the facts. Mrs Knight was however not called to give evidence. On that basis alone only limited weight could be given to her evidence. There would be a number of documents and lines of cross-examination which HMRC would have wanted to put to Mrs Knight, if she had given evidence in support of Mrs Woods. Secondly no address is given for Mrs Knight. Apparently Mrs Woods did not have contact details for Mrs Knight, so that HMRC could neither themselves call Mrs Knight to give evidence nor check with her the substance of what she would have said. Thirdly, the document is undated. Mrs Woods stated that the document was signed in 2005. When it was put to Mrs Woods that it would be surprising to produce a document at that date when Mrs Woods' residence was not being disputed for tax purposes, Mrs Woods responded that past experience had made her be cautious over this. Fourthly the purpose for which the document was to be used was not made clear in the document. There was no reference to the possibility of legal, court, tribunal or commissioners hearings. There was no statement of truth attached which would have clearly set out the confirmation of truth. Fifthly, it would have been important to know what Mrs Knight meant by "resided permanently at this address" and what the practical arrangements were. Sixthly there are other matters of interpretation of what Mrs Knight has said; for example the statement about Mrs Woods' residence is limited to the period when Mrs Tracey Knight herself resided at the address with her husband Mr Stuart Knight. Other evidence was that Mrs Knight had first moved in alone; there are also been issues about entitlements to housing benefit dependent on the number of occupiers. Accordingly the period covered by the statement was unclear.

28. For the reasons given in the preceding paragraph, we attach no substantive weight to the document purportedly signed by Mrs Knight.

29. Our assessment of Mrs Woods was that she was an unreliable witness. Documents and material that she had supplied were likely to be subject to error. Overall, we did not believe her evidence as explained below.

5 30. The issue for determination is whether Mrs Woods is entitled to rent a room relief, itself dependent upon 13 Willington Street (and subsequently 345 Queen Elizabeth Road) being her "only or main residence". We were not referred to any case law as to the meaning of this phrase. We think that we should apply the ordinary English meaning of the words. In applying this test no one indicator (such as where an individual is on the electoral roll) is decisive. It is necessary to look at all the relevant
10 facts and circumstances and make a judgement on the basis of those.

31. We come to the conclusion and find as a fact that Mrs Woods' main residence was 21 Manor Court Road. We do so for the following reasons. First, the proposition that a two bed-roomed terraced house occupied by tenants was a main residence rather than a semi detached family home where her husband and children lived is, in
15 our view, inherently unlikely. Mrs Woods advanced no substantive reason for her (apparently surprising) choice of main residence. Secondly, there is considerable documentary evidence of the use in various respects of 21 Manor Court Road by Mrs Woods. Thirdly, the evidence of Mrs Woods residing at 13 Willington Street is limited. There is her own oral evidence (see below). The insurance documentation
20 that she referred to was (on her own admission) inaccurate. The outcome of the enquiry by HMRC (which was an abandonment, not a finding) is not determinative. Fourth, the particular circumstances of the two bed-roomed terraced house at 13 Willington Street make it even more unlikely that Mrs Woods would choose to use it as her main residence. These included her pregnancy and giving birth in 2004; a
25 frightening Rottweiler guard dog at the property, the state of disrepair of the property, the fact that the tenants were in the course of damaging the property and the requirement to sleep on a put up bed downstairs.

32. We recognise that in making this finding we are rejecting Mrs Woods' evidence. We did not believe her evidence as to the extent of her residence at 13 Willington
30 Street. We find as a fact that any use by her of 13 Willington Street as a residence was comparatively minimal. We find as a fact that the majority of her time was spent residing at 21 Manor Court Road. We find that any time that she did spend at 13 Willington Street was at best occasional and far closer to her 2007 description of "as and when", rather than her evidence to us that she spent "most nights" at 13
35 Willington Street. We conclude that she has significantly exaggerated, whether consciously or subconsciously, the extent of her residence at 13 Willington Street.

33. We reject Mrs Woods' evidence because we did not find it credible; we did not believe her. Her evidence was against the weight of the other evidence. Her evidence was largely unsupported. She did not keep records that would have assisted her in an
40 issue which is already previously been the subject of a dispute. She said that the statement from Mrs Knight was obtained because of the history of dispute; but then failed to keep any other basic record or evidence which would have supported her version. She had made other errors; the document that she supplied relating to

insurance was, as she accepted in cross-examination, not consistent with her evidence to us. The s16 document failed to mention her residence at 13 Willington Street.

5 34. HMRC ask us to go further and conclude that the purported statement from Mrs Knight had, in effect, been forged by Mrs Woods. The HMRC contention is that the signature of Mrs Knight was transferred (i.e. copied, probably by a photocopy method) from another document. HMRC also pointed us to the suspicious circumstances surrounding the production of that statement, which included the absence of Mrs Knight, the absence of any contact details and the construction of the statement at a time when there was not a dispute about Mrs Woods residence.

10 35. HMRC asked us to compare the notice signed by Mrs Tracey Knight on 15 May 2004 with her purported statement. HMRC contend that the analysis of where the signature breaks the dotted line supports their thesis/proves that the signature is copied over. There are a total of 70 dots on both signature lines. HMRC say that the signature breaks the line after respectively 12, a further five dots and then a further
15 seven dots on both signatures. HMRC contend that this would not happen by accident or coincidence.

20 36. We do not make such a finding. To find that Mrs Woods has effectively forged Mrs Knight's signature through such a process would be a (very) serious conclusion. It would require strong evidence. We did not have any forensic evidence. In the absence of forensic or handwriting evidence from an expert, we do not think that the evidence is anything like strong enough to make such a finding.

25 37. *Issue two – business expenses.* Mrs Woods made extensive claims for expenses in the relevant tax returns. In general, these were unsupported by proper records. During the enquiry HMRC proposed alternative figures, which were the subject of debate and negotiation between Mr Molloy and Mrs Woods. Fortunately by the day of the hearing most issues had been resolved; of those remaining outstanding, Mrs Woods accepted the position in relation to capital allowances on the day of the hearing

30 38. The issues remaining outstanding for the Tribunal were those set out in Appendix 1 of Bundle 5 for the day at the hearing. HMRC proposed general administration expense figures of £880 and £1084 and motor expenses of £1515 and £1910 for the two years 2002–3 and 2003–4 respectively. Mrs Woods had been unable to support her (much higher) figures with records; Mr Molloy's figures were based on the limited records available. He explained the calculation to us. We were satisfied that Mr Molloy's figures were fair and reasonable. They are the best estimate in all the
35 circumstances.

40 39. *Issue three – Penalty.* By section 95 TMA a penalty is payable where incorrect returns or accounts have been fraudulently or negligently submitted to HMRC. The amount of penalty is 100% of the tax that would otherwise have been lost, but the penalty may be mitigated dependent on the extent of disclosure, cooperation and the size and gravity of the failure.

40. Mrs Woods accepts that she was negligent in submitting the capital allowance claim. We conclude that Mrs Woods was negligent in other aspects in two principal ways. Firstly she failed to keep proper records and secondly failed to follow the guidance within the notes that accompany the tax returns. As a result she wrongly
5 claimed business expenses, understated business income and claimed for rent-a-room relief that she was not entitled to. The failings of Mrs Woods were more fully set out in the letters of 12 February 2010 and 17 March 2010.

41. Mr Molloy decided to mitigate the penalty from 100% down to 30% of the lost tax. He explained his reasoning and calculation in paragraph 86 of his statement.
10 Mitigation of 10% of disclosure, 30% for cooperation and 30% for size and gravity was given for the reasons set out in paragraph 86. Whilst the penalty is initially set by HMRC, the Tribunal has the power to set aside, increase or decrease or confirm the penalty. Our view is that the assessment made by Mr Molloy was right for the reasons he gives in paragraph 86 of his statement.

15 42. At the hearing HMRC asked us to increase the penalty from 30% to 70%. The basis for doing so was Mrs Woods' conduct and, in particular, the allegation that she had forged Mrs Knight's statement. As can be seen above, we have not found that Mrs Woods forged Mrs Knight's statement. We have however carefully considered the conduct of Mrs Woods. On balance, we conclude that the mitigation proposed by Mr
20 Molloy should be confirmed. We have taken into account the fact that Mrs Woods has persisted in the claim for rent-a-room relief at the Tribunal; however, we also take into account the fact that many of the other aspects of the claim have been resolved by agreement, thereby narrowing the issues for the hearing.

43. Discovery assessments. The onus is on HMRC to establish the conditions
25 enabling HMRC to make discovery assessments. Section 29 TMA enables HMRC, where insufficient assessment is found, subject to one or other of two conditions, to make an assessment in the amount or further amount necessary to make good the lost tax. The first condition ("culpable mistake") is fraud or negligence on the taxpayer in failing properly to assess liability to tax or in claiming relief. The second condition
30 ("innocent mistake") applies when an officer of HMRC is out of time to make an enquiry under TMA 1970 into the tax payers return but that HMRC "could not have been reasonably expected, on the basis of information made available to him before that time, to be aware of" such failure or excessive claim for relief. The information made available to HMRC includes the information in the return and accompanying
35 documents.

44. We are satisfied that the Inspector has made a discovery. Mr Molloy discovered that rental income had been omitted from each of the returns seven tax years ended April 2007, income had been omitted from the return for year ended 5 April 2007 and that business expenses had been claimed on each of the returns for the six years ended
40 April 2007 and expenses have been claimed that were not wholly and exclusively for business purposes. We are also satisfied that the conditions for discovery have both been made out; the omission of income and wrongful claims for expenses were caused by the failings of the Appellant, which could easily have been avoided by her taking proper care.

45. Conclusion. The appeal will be dismissed. The claim for rent-a-room relief fails. The business expenses and general administration expenses are determined in the amount set out by Mr Molloy. The penalties are confirmed at 30%. The Appellant has failed to establish that the assessments for 2005 – 2007 should be amended. HMRC
5 have satisfied the conditions for discovery for the years ending April 2001-2004. The actual figures resulting were not before the Tribunal, on the basis that amendments and agreements were being made at the last moment.

46. 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
10 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.

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20 **TRIBUNAL JUDGE**
RELEASE DATE: 12 OCTOBER 2011