



TC04805

Appeal number: TC/2014/4906

Income Tax. Development of a tree surgery and woodmanship trade from a domestic concern- income in kind- when did trade start? Losses arising – quantification on the evidence; set off of losses against other income – was trade commercial: s 66 ITA

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

KEVIN JOHNSON MBE

Appellant

- and -

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

**TRIBUNAL: JUDGE CHARLES HELLIER
 WILLIAM HAARER**

Sitting in public in Plymouth on 21 September 2015

The Appellant in person

Mr C J Brown, for the Respondents

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DECISION

Introduction

5 1. This appeal raises three issues:

(i) when did Mr Johnson start trading? HMRC accept that today Mr Johnson carries on trade whose activities encompass tree surgery; Mr Johnson says that his activities were such that he should be viewed as having started a trade in November 2010;

10 (ii) when Mr Johnson was carrying on a trade, was it commercial? HMRC say that it was not commercial until the year 2012/13 and that, as a result, losses which Mr Johnson claims he made in 2010/11 and 2011/12 may not be relieved against other income of those years; and

15 (iii) if Mr Johnson was trading, then what were the amounts of his trading profits or losses in 2010/11 and 2011/12.

The evidence and our findings of fact.

2. We heard oral evidence from Mr Johnson. We also had a bundle of copy correspondence between the parties. After the hearing and at our direction Mr Johnson also provided copies of invoices supporting some of the expenses for which
20 he claimed deduction in the computation of his results.

3. We found Mr Johnson to be a credible and honest witness. In what follows when we relate what he told us we mean that we accept that evidence.

Mr Johnson's naval career.

4. Until March 2012 Mr Johnson was a naval officer. In the Spring of 2010 he
25 returned from a tour in Afghanistan. On his return he had an extended period of leave and did not resume a full-time role in the Navy until January 2011. After his return from Afghanistan in the Spring of 2010 he resolved that in due course he would resign his commission, but at about that time he heard rumours that redundancies might be made in the forces and that some compensation might be payable to those
30 who accepted redundancy. He therefore decided to delay his decision as to whether to resign. Sometime after his return to a full-time post in January 2011 the redundancy rumour proved well founded, and Mr Johnson made an application to be considered for redundancy. In September 2011 he was notified of the success of his application.

5. Following his selection for redundancy in September 2011 Mr Johnson remained
35 an officer for a further six months, that is to say until about the beginning of March 2012. In those six months he participated in resettlement training offered by the Navy and attended a number of courses.

6. Mr Johnson's first child was born in October 2011 and he had a period of parental leave. Overall he told us that as a result of resettlement training and the

parental leave he was in the office for only about two weeks of the final six months of his service between September 2011 and March 2012.

Obtaining wood and chainsaw work

5 7. In November 2006 Mr Johnson and his wife (also a naval officer) had moved into a house in Cornwall. Initially it was cold and damp and draughty. They opened up the fireplaces and brought four wood burning stoves into operation. Mr Johnson and his wife found themselves burning a considerable amount of wood. Mr Johnson found himself abstracting firewood not wanted by his friends and neighbours, and in November 2009 went on his first chainsaw course.

10 8. Between the Spring of 2010 and January 2011, when Mr Johnson was on his period of extended leave after Afghanistan, he found it useful to keep himself busy and spent time logging for wood to use in his house, cutting and collecting wood and doing tree jobs for friends and neighbours. He would remove the wood and stack the logs for later heating of his house.

15 9. It was at this time that Mr Johnson began to consider what he would do on leaving the Navy. He found that his logging expertise was in some demand. He saw an opportunity for an activity of providing gardening and tree surgery services.

10. In November 2010 he obtained from Vista Print some business cards. These described his business as

20 "Empire Tree & Gardening Services.

Specialist in rope access pruning

Kevin Johnson MBE

Liskeard

Cornwall

25 [tel no]

[email address]"

11. These business cards reflected his initial thinking of an amalgam of gardening and tree surgery services. He told us that he distributed his cards when he could.¹

30 12. In November 2010 Mr Johnson spoke to someone at HMRC about his activities and discussed whether he should register with HMRC as self-employed. Following a conversation he registered as such with HMRC in November 2010.

1. ¹. We note that later cards described in more detail Mr Johnson's qualifications and his expertise in matters such as tree planning applications.

13. Between January 2011 and September 2011, when Mr Johnson was back in full time work for the Navy, he sought work which he could do at weekends and during annual leave (of about 52 days per annum).

5 14. Mr Johnson described himself as fortunate in the period before he left the Navy in that, because he was receiving a full naval salary he did not have to depend financially on his wood or gardening activity, but could profit from the firewood he obtained. After he left the Navy he received a pension which would also have taken the edge off his financial concerns.

Courses

10 15. When Mr Johnson's redundancy application was successful in September 2011 he chose, from the resettlement activity menu offered by the Navy, courses and activities which would enable him to continue and extend his woodmanship activity and assist him in running a business.

15 16. In late 2011 Mr Johnson attended a course run by the Royal British Legion about self-employment and business mentoring. He told us that he recalled discussing business ideas then - the sustainability, development and profitability of the business he had in mind: he recognised then that in the future his tree climbing days might be limited and that he would have to develop other aspects of the activity (but he was keen to ensure that he did the physical tasks before moving on to further stages).

20 17. Courses (including those leading to City & Guilds qualifications) on woodmanship and chainsaw use tended to be cumulative: before attending a course on using a chainsaw for felling medium trees one had to attend the chainsaw maintenance course; attendance on a course on using a chainsaw with rope and harness was a pre-requisite for a course on arboricultural dismantling. Very often the
25 course qualifications did not come into effect until after the period of practice and further assessment. It was thus not possible to become completely trained in all aspects of the work in a short time, but there was work which could be done having competed only early parts of the training. Mr Johnson is still attending further courses. As he does, so the nature of his activities have changed and developed.

30 18. Mr Johnson attended at least two courses in 2010, four in 2011, 15 in 2012 and obtained further qualifications in 2014.

The Work Done

19. Mr Johnson gave examples of the jobs he had done for other people from late 2010 onwards:

35 (i) 2010

In this year Mr Johnson did about 12 jobs. One example was a job done in November 2010 for a Malcolm Oliver. Mr Johnson had been asked to access the crown of a large oak tree overhanging a bungalow and stable and to remove the

dead wood. Having done the job he took away (for use at home) several trailer loads of wood.

Another example was taking down a tree overhanging a garage. Mr Johnson used a chipper to deal with a small wood. He bought the chipper and a trailer in November 2010.

In addition Mr Johnson said he had done a number of half day minor jobs in the year. We saw an e-mail of 20 July 2010 to an unnamed home owner offering Mr Johnson's tree services, and an e-mail on the same date to a Mrs Barbara Mason about the removal of ivy.

(ii) 2011.

In this year Mr Johnson had done 20 to 30 jobs. He also gave an example of an unsuccessful quote for stump grinding (he purchased a stump grinder in April 2011).

We saw an e-mail of December 2011 from a career consultant of the Navy's career transition management function providing links to useful self-employment websites. The e-mail thanked Mr Johnson for his advice on tree management and spoke of obtaining a quotation from him at some time in the future.

(iii) 2012

Mr Johnson was not able to recall the amount of work he had done in this year. His daughter, Clara, had been born in October 2011 and he spent more time at home with her. It was likely he had done about 12 jobs. An example was the clearance of the site for Mr Oliver's grandson who was a developer; that work required the help of some six subcontractors whom he had paid.

We saw copies of e-mail correspondence, quotations and business bank statements showing a number of transactions from the period May 2012 onwards. It appeared from the copy correspondence that Mr Johnson opened a business bank account in May 2012 when he received his first payment for work done.

(iv) Later Years

Mr Johnson said that he would be available for work about three days a week but he did not say that he worked for each of those days. Mr Johnson's recent work has included tree assessment and estate management advice.

Mr Johnson's expenditure

20. With a letter of 13 January 2015 to HMRC Mr Johnson enclosed two schedules of expenditure, one (at page 135 of the bundle) of which covered 2010 and the other (at pages 133 and 134) for 2011 and part of 2012. The 2010 schedule showed details of the suppliers, the items purchased and date; the detail in the 2011/12 schedule was limited to a generic description of the item, a price and the date.

21. The 2010 schedule starts with the purchase of a Stihl brushcutter on 1 May 2010. The schedule also showed that:

5 in November 2010 Mr Johnson had purchased the business cards referred to earlier and promotional mugs and postcards from Vista Print.. He told us that the mugs (of which he had purchased about two dozen for about £40 in all), carried his name and phone number on one side, and on the other the legend "Can't see the view for the Trees".

10 by the end 2010 Mr Johnson had acquired a brushcutter, a pole saw, a 15 inch chainsaw bar, a brushwood chipper, a trailer, a bungee strap and lighting equipment. He already had a chainsaw.

22. The 2011/12 schedule shows that in 2011 Mr Johnson purchased further materials from Vista Print. These were further business cards and also, for about £20, about 10 lawn signs - corrugated plastic signs - which he told us he put up at premises where he was working, and also at a garden centre (where he had thinned some trees).
15 In 2011/12 Mr Johnson also purchased a LandRover 110 Utility Vehicle; he used this only for his arboricultural work , keeping a separate car for domestic use.

23. We shall return later to the question of the deductibility of expenses shown on these schedules.

24. *Summary*

20 (i) Spring 2010 to January 2011: Period of extended leave; thinking about leaving the navy; attended a couple of chainsaw courses; doing more chainsaw work for others (taking away the logs) increasingly on a formal basis; obtained business cards bought chipper, trailer, and brushcutter.

25 (ii) February 2011 to September 2011: Full time work in the navy. Attended two further courses. Pursued work in woodmanship (taking away the logs) and heavy gardening which was done at weekends and in periods of annual leave.

30 (iii) September 2011 to March 2012: Period of resettlement training. Attended at least half a dozen courses related to woodmanship and some to running a business. Daughter born October 2011. Only two weeks in the office. Did tree work for others (taking away the logs).

(iv) 31 March 2012 onwards: No longer in the navy. Drawing naval pension. Attended 12 courses in the remainder of 2012. First job paid in cash May 2012.

Mr Johnson's tax returns, the closure notice and the assessment.

35 25. 2010/11. In Mr Johnson's tax return for 2010/11 he declared himself as being self employed (together with his full-time naval commission). He said in the further information section (the "White Space"):

40 "The Empire Tree & Garden Services company has been in the process of being established (predominantly professional training, collecting necessary equipment, preparing the workspace and establishing a client base) in order to facilitate a se[a]mless transition to self-employment from 31 Mar 2012 when

my Royal Navy redundancy becomes effective. I expect the company to commence generating income from March 2012."

26. For the period 1 November 2010 to 31 March 2011 Mr Johnson declared a turnover of nil, and allowable expenses of £2,604. A deduction was claimed for £9,705 of Annual Investment Allowance. This took his net loss for the period to £12,309.

27. 2011/12. In Mr Johnson's tax return for 2011/12 he again declared himself as having a self-employment business and included similar language in the White Space as in the 2010/11 return. He again declared no turnover for the year, and declared allowable expenses of £11,099. An Annual Investment Allowance claim of £26,078 brought the total loss for the year to 31 March 2012 to £37,177.

28. These returns gave rise to tax computations in which each loss was set against other income and showed tax repayable.

29. HMRC opened an enquiry into Mr Johnson's 2011/12 tax return in September 2013.

30. Following correspondence in which:

(i) a breakdown of the £11,099 expenses was sought;

(ii) HMRC expressed the view that £19,800 of the claimed Annual Investment Allowance was not available because it represented expenditure on a Land Rover station wagon (or 110 Utility Wagon) which the officer considered to be a car and so not eligible for the allowance (Mr Johnson now accepts this conclusion), and

(iii) questions were raised as to whether Mr Johnson conducted his business on a commercial basis,

a closure notice was issued on 4 December 2013 in which the officer concluded that the business was not shown to have been carried on on a commercial basis and that, as a result, the claimed loss could not be used. Mr Johnson's 2011/12 tax return was amended accordingly.

31. The closure letter also speaks of disallowing the £11,099 expenses because no breakdown had been produced. Mr Johnson responds to this in a letter of 14 March 2014 in which he says that the information was provided orally in a telephone call on 6 November 2012 when he understood that the officer was satisfied. It also appears that in an earlier telephone call of 10 September 2013 an officer had said to Mr Johnson that £1,433 of the expenses would be disallowed as a capital cost of training.

32. Two days later, on 6 December 2013, HMRC issued a discovery assessment in relation to 2010/11. This assessment was made on the basis of disallowing the claimed 2010/11 trading loss.

33. Mr Johnson appeals against the closure notice and the 2010/11 assessment.

The relevant law.

34. By section 5 Income Tax Trade and Other Income Act 2005 ("ITTOIA") income tax is charged on the profits of trade. By section 25 profits must be calculated in accordance with generally accepted accounting practice ("GAAP") but subject to particular provisions of law, and by section 26 losses must be calculated in the same way as profits. The computation of profits in accordance with GAAP is made subject to restrictions in sections 32 to 55; these restrictions relevantly include:

- (i) the provisions of section 33 which deny a deduction for capital expenditure; and
- (ii) the provisions of section 34 which deny a deduction for an expense unless the expense is incurred wholly and exclusively for the purposes of the trade.

35. The Capital Allowances Act 2001 permits deductions for the capital expense of plant and machinery for use in a trade. In the case of a small trader an Annual Investment Allowance is permitted for such expenditure of the whole of its cost. Plant and machinery expenditure does not, however, include expenditure on buildings (see section 21).

36. Section 64 Income Tax Act 2007 ("ITA") permits a person who makes a loss in a trade to set that loss against his general income of the relevant tax year. But section 66 provides that this relief is "not available unless the trade is commercial". Section 66(2) provides that a trade is commercial only if it is carried on both (i) on a commercial basis and (ii) with a view to the realisation of profits. If the trade affords a reasonable expectation of profit it is to be treated as carried on with a view to the realisation of profits.

37. These statutory provisions give rise to the issues before us in each of the years 2010/11 and 2011/12, namely:

- (i) were Mr Johnson's activities trade?
- (ii) if so what were the profits or losses of that trade? and
- (iii) if they were a trade, and if there were losses, whether the trade was commercial.

Discussion.

1. Were Mr Johnson's activities a trade?

38. No definition of 'trade' is provided by the Acts although section 989 ITA provides that trade includes any venture in the nature of trade. In *Ransom v Higgs* [1974] 3 All ER 949 Lord Wilberforce said:

"Trade has for centuries been, and still is, part of the national way of life; everyone is supposed to know what "trade" means; so Parliament which wrote it into the income tax in 1799 has wisely abstained from defining it and has left it to the courts to say what it does or does not include..."

5 “Trade cannot be precisely defined, but certain characteristics can be identified which trade normally has. Equally some indicia can be found which prevent a profit from being regarded as the profit of a trade. Sometimes the question whether an activity is to be found to be trade becomes a matter of degree, frequency, of organisation, even intention, and in such cases it is for the fact-finding body to decide on the evidence whether a line is passed. ...

10 "Trade involves, normally, the exchange of goods, or of services, for reward, not of all services since some qualify as a profession, or employment or vocation, but there must be something which the trade offers to provide by way of business. Trade, moreover, presupposes a customer (to this too there may be exceptions but such is the norm), or, as it may be expressed, trade must be bilateral - you must trade with someone. And the ‘mutuality’ cases are based in part on this principle, and it was the existence of it that made *Sharkey v Wernher* an interesting problem: could Lady Zia trade with herself?"

15 39. In our judgement "trade" is not limited to an activity in which money is received. Cases such as *Gold Coast Selection Trust Ltd v Humphrey* 1948 AC 459 show that if a trade is conducted nonmonetary receipts are part of the income of the trade and thus indicate that trading activities are not limited to those which give rise to a monetary receipt (so long perhaps as the monetary value of what is received can be
20 ascertained). An activity of bartering is no less capable of being a trade than one in which the barter is replaced by exchanges of money.

25 40. In providing his services in return for the wood arisings Mr Johnson was providing to a third party his labour in return for a benefit. Thus we conclude that Mr Johnson's activities in the period before May 2012 (when he first received a cash payment for his labours) and in which he supplied his services in return for the wood arisings are not prevented from being *capable* of being trade because no money was received.

30 41. But the fact that a particular piece of work was capable of being a trading activity does not mean that it was a trade. It may for example be something done once and for personal reasons. A person who kept a chain saw and did an occasional job for a neighbour in return for the wood would not without more be a trader.

35 42. In some cases the "badges of some trade" have been found to be useful aids in the consideration of whether or not an activity is a trade, although they have particular relevance to transactions which consist in the dealing with some asset. They were described in *Marson v Morton* [1986] STC 463 at 470-471):

- (1) Repetition. Repetition of an activity is indicative of trade,
- (2) An existing trade. If an activity is part of or similar to an existing trade it is more likely to be a trade;
- (3) The subject matter. It is for example more likely that the sale of 100 tons of
40 carbon steel is trading than the sale of an old baby's high chair

(4) The way the transaction was carried through. Whether there was a degree of organisation, or businesslike behaviour.

(5) The source of finance. If an activity is financed by borrowing that may indicate trading.

5 (6) The work done on an object. If an object is acquired and modified or enhanced before being sold, that is indicative of trade.

(7) If assets are acquired and broken down into lots for sale that is indicative of trading.

10 (8) If the purchaser intended to sell at the time of purchase, that is indicative of trading.

(9) Where an asset is acquired and then sold, if the asset provided income pending resale (as might shares) it is less likely that the activity is a trade

43. With these indicia in mind it seems to us that an activity which consists of the repeated provision of woodmanship of a kind for which the recipient might otherwise expect to pay a full time professional, but in return for the log arisings, which was conducted in an organised manner and advertised to third parties, and both involved the financial risk of the acquisition of plant and equipment and the expense of training in excess of that which might be incurred by a hobbyist, is a trade.

44. We accept therefore that at some time before May 2012 Mr Johnson was trading. The next question is when did that trade commence. In *Mansell v HMRC* [2006] STC (SCD) 605 the Special Commissioner (who was one of the members of this tribunal) considered when a trade "commenced" for the purposes of provisions whose effect was determined by when trade was "set up and commenced". In that case the Special Commissioner said:

25 88. ... I conclude that trade cannot commence until it has been set up (to the extent it needs to be set up), and that acts of setting up are not commencing or carrying on trade. Setting up trade will include setting up a business structure to undertake essential preliminaries, getting ready to face your customers, purchasing plant, and organising the decision-making structures, the management and the financing. Depending on the trade more or less than this may be required before it is set up.

89. ... the cases cited to me ... suggest ... the following principles. First before its trade can be said to commence there must be as fairly specific concept of the type of activity to be carried on.

35 90. Second: an activity which consists merely of a review of the possibilities in the expectation or hope that information will be obtained to justify going into the business of some kind is not the carrying on of the trade.

91. Third: it is not always necessary that a sale is made or service supplied before trade can be said to have commenced...

5 93 It seems to me that trade commences when the taxpayer, having a specific
idea in mind of his intended profit-making activities, and having set up his
business, begins operational activities - and by operational activities I mean
dealings with third parties immediately and directly related to the supplies to be
made which it is hoped will give rise to the expected profits, and which involves
the trader putting money at risk: the acquisition of the goods to sell or turn into
items to be sold, the provision of services, or the entering into a contract to
provide goods and services: the kind of activities which contribute to the gross
(rather than the net) profit of the enterprise. The restaurant which has bought
10 food and which is in its kitchen and opens its doors, the speculator who
contracts to sell what he has not bought, the service provider who has started to
provide services under an agreement to do so, have all engaged in operational
activities in which they have incurred a financial risk and I would say that they
that all started to trade."

15 45. In so far as the criteria set out in that case are relevant to Mr Johnson's
activities, it seems to us that by November 2010 Mr Johnson had set up his trade: he
had purchased tools and readied himself to face and find customers.

20 46. Mr Johnson explained that, as his business card showed, initially he saw his
activity as comprising both heavy-duty gardening and chainsaw work, but that as time
went by, his focus became woodmanship only. It seems to us that by November 2010
Mr Johnson had a specific activity in mind, although the activity he conducted
changed somewhat in due course.

25 47. Before November 2010 it was fairly clear that Mr Johnson was still in the
process of considering what to do and hoping that he could find a business. He was
trying out the possibilities. Such work as he did was we believe mainly for the
domestic purpose of obtaining firewood rather than the provision of service for
reward. But to our minds the acquisition and distribution of business cards in
November 2010 marked a change. He had begun to seek work in which he would be
rewarded, if only in the acquisition of logs. He may not have been able to offer his
30 services on all working days because of his domestic and Navy commitments but he
was offering and thereafter did supply his services for reward. He had dealt with third
parties and put money at risk in acquiring advertising materials and tools, and had
begun to provide his services with a degree of organisation.

48. We conclude that Mr Johnson started to trade in November 2010.

35 2. What were the profits and losses of the trade in the period to 31 March 2010 and
the period to 31 March 2012?

49. Two issues arise: (i) what income arose, and (ii) what expenses were allowable.

(i) *What income arose?*

40 50. If a trader engages in barter the question arises as to how his profits should be
calculated. The principal in the *Gold Coast* case is that the receipts should be valued
at realisable value at the time of the receipt.

51. A similar question arises when a trader appropriates to himself an asset of his trade - and of course in a trade consisting wholly of barter transactions that would be the only way in which the trader could enjoy the fruits of his activities. In *Sharkey v Wernher* 1931 16 TC 595 the House of Lords held that on such an appropriation the market value of the assets at the date of their appropriation should be brought into account as a receipt of the trade².

52. Thus Mr Johnson must bring into his income computations the realisable value of the logs received in return for the work done, and must then treat the appropriation of those logs to himself as a sale of the logs again at market value. The end result is that the market value of the logs received and thereafter appropriated comes into account as his turnover in each relevant period.

53. Mr Johnson told us that his activities yielded 10 to 15 tons³ of firewood in a year, he said that seasoned logs delivered by Mole Valley Farmers cost about £200 per cubic metre (which would be somewhat less than a ton), air dried oak logs could be £120 a ton, the value of timber at roadside for converting into logs was £60-£40 per ton, and he estimated that logs which had been seasoned for 12 months for provision to a firewood processor would sell at £90-£100 a ton.

54. The logs which Mr Johnson brought back from the sites at which he had been working would not generally have been seasoned. At some stage he would stack logs to let them dry. The lists of expenditure Mr Johnson produced to HMRC (see below) indicate expenditure on the provision of cover for the logs.

55. Allowing for some discount for the value of drying the logs, we conclude that in each of the periods of 5 months ending on 31 March 2011 and the 12 months ending 31 March 2012 Mr Johnson received in return for the work he did logs of market value no less than £1,500 and £2,500 respectively.

56. Mr Johnson also suggested in a later written submission that he had received value from access to a landowner's trees because the work enabled him to gain the necessary practical experience for progression through the training courses. We do not regard this as something he received in return for his work, it was a benefit which accrued as a result of his work which did not have a realisable value.

(ii) What expense was allowable?

2010/11

2. ² Although these cases were decided before the enactment of the predecessor to section 25 ITTOIA which requires the profits to be calculated under GAAP subject to any provisions of law, we are aware of no aspect of GAAP which would dictate a contrary approach even if the principle of the cases were not treated as an overriding provision of law.

³ A ton is for present purposes almost the same as a metric tonne

57. We have related that in his tax return for this period Mr Johnson claimed expenditure of £2,604 and £9,705 for Annual Investment Allowance. The 2010/11 analysis referred to above (Folio 135) however showed expenditure of only £7,061.51 including VAT. Given no evidence of any other expenditure we conclude that the maximum allowable is £7,061.51.

58. We asked Mr Johnson to provide invoices backing up certain of the elements of expenditure in the 2011/12 analysis sheets schedules. The information he provided confirmed the amounts of the expenditure although the quality of the reproduction was not always sufficient for us to ascertain from the copies provided to us the nature of expenditure. However Mr Johnson provided details of expenditure. We accept his descriptions. We concluded that the analysis in the 2010/11 schedule correctly described the nature of the relevant items.

59. Looking at that schedule the expenditure appeared to us to divide into the following items:

- 15 (i) building materials: £1393.47
- (ii) revenue expenditure for the trade: £400.43
- (iii) expenditure on plant and machinery for the trade: £5,267.61.

60. The expenditure on building materials appears to have been related to workshops and wood storage at Mr Johnson's home. It does not seem to us that it was shown that this was revenue rather than capital expenditure wholly for the purposes of his trade. The expenditure on log sheds was expenditure incurred for the purpose of drying out the logs he had obtained from the trade. It was capital expenditure and not expenditure for the purposes of the trade. It is not allowable as an expense.

61. Nor is it allowable for Annual Investment Allowance since expenditure on buildings is excluded from that allowance.

62. We conclude that the allowable expense of this period was £400.43 and the Annual Investment Allowance amount £5,267.61.

2011/12.

63. Save in relation to the acquisition of the Land Rover, and as was the case for 2010/11, the only evidence of expenditure before us was in the schedules. We conclude that (save as related to the Land Rover) the maximum allowable expenditure is that shown in those schedules.

64. The description of the relevant items in the analysis in the 2011/12 schedules was less helpful. It describes the expenditure mainly as either "tools" or consumables" without specifying the exact nature. As we have said Mr Johnson supplied at our direction copies the invoices and give a description of nine items of expenditure. From that information we accept that the listed expenditure was incurred by Mr Johnson, and we accept his description of what was provided. The relevant descriptions are as follows:

Date	Description on Schedule	Mr Johnson's description	Amount £	On building work	Of revenue nature, for the trade
7 May 11	Consumables	Protective seat covers	38.10		38.10
7 May 11	Consumables	MDF boards for workshop	43.12	43.12	
7 May 11	Consumables	MDF boards for workshop	28.75	28.75	
2 Dec 11	Consumables	Armoured cable for workshop	105.00	105.00	
2 Dec 11	Consumables	Armoured cable for workshop	105.00	105.00	
12 Mar 12	Consumables	Materials for log shelter	272.12	272.12	
1 June 11	Protective Clothing	Protective eye glasses	74.99		74.99
3 Mar 12	Tools	Consumable climbing felling items	206.74		206.74
14 Oct 11	Tools	Timber treatment/preservative	63.77	63.77	
Totals			937.59	617.76	319.83

65. The items which relate to the building work are in our view capital and not allowable expenses, nor is expenditure which relates to buildings eligible for Annual Investment Allowance. We conclude that 66% of the claimed expenses were not allowable as income expenses or for Annual Investment Allowance. On that basis we concluded only 34% of the expenses listed on the 2010/11 schedules as consumables, tools and protective clothing were allowable.

66. Mr Johnson's analysis in the 2012/11 schedules details, on one schedule, £2,091 of expenditure divided into those classes and a second schedule details £1,559.29 of separately described administrative expenditure and £8,009 of capital equipment.

67. We conclude that 34% of the £2,091 is allowable. Ie £710.

68. Of the £1,559.39 of administrative expenditure, £1437 relates to training courses. In our view those courses are capital expenditure being undertaken to produce an enduring benefit for the purposes of trade. As such they are not allowable. We conclude that £122 is allowable.

5 69. Thus we conclude that $£710 + £122 = £832$ is allowable revenue expenditure for 2011/12.

70. So far as concerns the six items of capital expenditure on equipment totalling £8,009.50, we conclude that this amount was allowable for Annual Investment Allowance.

10 *Net taxable profits/loss.*

71. As a result we conclude that in each of the relevant years Mr Johnson's net profit/loss for each period was:

	2010/11	2011/12
Income	1,500	2,500
Allowable expenditure	(400)	(832)
Ann Inv Allowance	(5,267)	(8009)
Net (Loss)	(4,167)	(6,341)

15 From the net loss a further deduction needs to be made for capital allowances on the Land Rover.

3. Was the trade carried on on a commercial basis?

(i) 2010/11

20 72. We did not get the impression that in 2010/11 one could have had a reasonable expectation that either (1) in the short term the value of the wood arising from Mr Johnson's activities would exceed his expenditure, or (2) in the longer term (as viewed from any time in 2010/11) the value of the wood arising plus any cash receipts would exceed that expenditure.

25 73. In this year Mr Johnson's spare time activity had become more serious: what could perhaps be described as a hobby was beginning to deliver benefits, and a flow of work was starting. But he was still contemplating gardening and as well as tree work, and the tree work produced wood for his own use of limited value. At this stage Mr Johnson had done some of the necessary training but not all of it. His later success could not be relied upon. This was also a time of relative economic uncertainty and, as Mr Johnson says in one of his letters to HMRC, it was a "marked achievement to

have managed to establish a business" in an area with persistent weak economic performance competing against established traders. The fact that Mr Johnson actually succeeded does not mean that it was objectively reasonable to suppose that he would succeed.

5 74. If the trade was not carried out with a reasonable expectation of profit we cannot find that it was commercial.

75. We conclude that the trade was not commercial in this period, and accordingly that the loss in the trade cannot be set against other income.

(ii) 2011/12.

10 76. In this year Mr Johnson expended some £8,000 on machinery together with £19,800 on the Land Rover. That level of expenditure on machinery which would only have significant uses otherwise than solely in his own garden, taken with the reduced level of his income from the Navy, indicated that Mr Johnson had confidence that he would reap some income from his activities.

15 77. However there is a difference between an individual's hope of income and an objectively reasonable expectation of profit; and, as he said to us, the income Mr Johnson received from the Navy and would receive from his pension provided a cushion.

20 78. Nevertheless in this year Mr Johnson appeared to have gone about his activities in an organised and businesslike manner. He continued his training, obtained assignments and reaped logs in return. He sought jobs for which he would be paid. That seems to us to be a commercial basis.

25 79. It seems to us that the trade of a tree surgeon can reasonably be expected to be capable of being carried on so as to afford a reasonable expectation of profit, and that by 2001/12 Mr Johnson had the equipment to carry on such a trade and, by reason of experience and further training now had a reasonable expectation of carrying on such a trade.

30 80. Mr Johnson acknowledged that he would not carry on the trade every day of the week. That does not seem to us to point away from the trade being carried on on a commercial basis for there is no reason why a service provider should be always available, but it does affect the question of profitability, for less would be earned in that case, and if the business had fixed costs the expectation of profit would be dented. But Mr Johnson's fixed costs were limited to the depreciation of his equipment, which would arise mainly from its use, although there would be some decay with age. Overall we consider that it was reasonable to expect Mr Johnson to
35 make profits in later years and overall to expect the aggregate income over a period of say three to five years from the beginning of 2011/12 to exceed the expenses.

40 81. We conclude that in 2011/12 the trade was commercial for the purposes of section 66 ITA, so that that section does not preclude the setting off of the losses in that year.

Conclusions.

82. We dismiss the appeal against the 2010/11 assessment. The 2010/11 trading losses cannot be set against other income.

5 83. We allow in part the appeal against the 2011/12 closure notice. The trading losses may be set against other income in this year, but the amount which may be so offset is limited to the losses which we have found arose.

Rights of Appeal

10 84. 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.

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CHARLES HELLIER

TRIBUNAL JUDGE

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