[2016] UKFTT 0576 (TC)

TC05325

Appeal number: TC/2015/04364

Income tax - incorrect returns - HMRC amendments to self-assessment return in respect of profits of self-employment - whether HMRC had incorrectly disallowed expenditure - on the facts, no - whether assessment correctly calculated - yes - whether penalties correctly assessed - yes - appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

KUJTIM GJOCI **Appellant**

- and -

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

TRIBUNAL: JUDGE: MICHAEL CONNELL
MEMBER: CAROLINE DE ALBUQUERQUE

Sitting in public at Fox Court, Brooke Street, London on 14 April 2016

Mr Lanford Holmes, Accountant for the Appellant

Mr John Corbett, Officer of HM Revenue and Customs, for the Respondents

DECISION

The Appeal

1. This is an appeal by Kujtim Gjoci ("the Appellant") against HMRC's closure notices and amendments to his self-assessment return in respect of the profits of his self-employment for the 2012-13 and 2013-14 tax years, pursuant to s 28A(1) and (2) Taxes Management Act 1970 ("TMA"), and discovery assessments raised pursuant to s 29 TMA 1970 in respect of the 2009-10, 2010-11 and 2011-12 tax years.

2. The Appellant also appeals against the penalty assessments imposed for the submission of incorrect returns for the tax years 2009-10 to 2013-14. The penalties were raised under Schedule 24 Finance Act 2007.

3. The points at issue are:

(1) Whether the Appellant understated his profits from his self-employment profits from Leo Gjoci Building Contractors for the tax years in question and in particular, firstly whether HMRC were right to treat unexplained bank lodgements as additional sales, secondly to disallow un-vouched expenses and thirdly to restrict CIS tax credits claimed to the amounts returned by the contractors he worked for in the year.

(2) Whether HMRC are correct to impose penalties on the Appellant for making incorrect income tax returns for the tax years in question and, if so, in what amount.

Background

4. Throughout the period covered by the decisions under appeal, the Appellant was a self-employed plumber/fitter who commenced self-employment on 10 August 2004. The Appellant's 2013 self-assessment tax return was received on 4 September 2013 showing turnover of £44,598, business expenditure of £46,292, and capital allowances of £3,220, leaving a net business profit of £314, with a claim to Construction Industry Scheme tax deducted of £8,720. The return also included incapacity benefit of £761. HMRC noted that the Appellant's expenditure was very high in relation to his turnover.

5. On 10 March 2014, HMRC opened an enquiry into the Appellant's self-assessment return for the year ended 5 April 2013 and requested copies of his business books and records for the year in question, including:

i. *Trading income* – copy bank statements for the account into which business income was paid. When provided the statements showed that although the Appellant's turnover was shown on his return as being £44,598, the amount paid into his bank account during the year was £85,582.

The Appellant's agent, Mr Holmes, explained that the Appellant had used money from his own personal account to pay for materials and other expenses; the extra monies paid into his bank account were reimbursements by

contractors he had worked for. HMRC pointed out that round sum cash deposits totalling £13,180 had been paid into the Appellant's business account into the bank and requested evidence from the contractors in support and copies of the Appellant's personal bank statements. No such evidence was provided. On the basis that the Appellant was unable to provide any receipts or invoices to support the expenses figure of £13,180 and contractors appeared to make direct credits to the account, HMRC took the view that it was unlikely contractors would pay the Appellant in cash. In the absence of evidence as to the source of those receipts HMRC treated them as additional non-returned income, raising the Appellant's turnover to £57,778.

ii. *Cost of Goods* - invoices and receipts to support a business expenditure figure of £14,800. The Appellant provided a large number of invoices totalling £19,112.30, but most appeared to relate to household expenses, which were not allowable. The Appellant's agent identified a number of items as business expenses but the Appellant was unable to provide any copy invoices or other verification of the expenditure. HMRC said that they would be prepared to accept 10% of the expenditure as business related in order to settle that aspect of matters.

iii. *Car, Van and travel expenses* - invoices and receipts to support a claimed figure of £6,750. The Appellant provided fuel receipts totalling £2,310.84 and two invoices for tyres totalling £213.52. HMRC agreed to allow £2,311 but not the cost of the tyres.

iv. *Wages* – to support a claimed figure of £4,500 which the Appellant said related to bookkeeping costs - the names and National Insurance Numbers of staff to whom wages were paid, together with evidence of the payments, such as payslips or bank statements. The Appellant was unable to provide any supporting evidence and therefore HMRC disallowed the claim.

v. *Rent, Rates, Power and Insurance* - invoices and receipts to support a claimed figure of £6,859. The Appellant was informed that he would only be able to claim such proportion of those costs as were referable to business expenditure. No evidence was provided and therefore HMRC proposed an allowance of 10% of the amount claimed.

vi. *Interest and financial charges* - invoices and receipts to support a claimed figure of £3,418. No evidence was provided.

vii. *Other sundry business expenses* - all invoices and receipts to support a claimed figure of £3,750. No evidence was provided.

viii. *CIS deductions* - all payment and deduction statements in support of the amount claimed. HMRC's records showed that only £500 was deducted by CIS contractors from payments made to the Appellant as opposed to £8,720 claimed in his self-assessment tax return. HMRC advised that in the absence

of deduction statements to evidence the amounts claimed, HMRC would restrict the relief to the tax deducted of £500.

The Appellant produced a certificate from APM Maintenance Limited showing that £8,152.85 had been deducted for the year to 5 April 2014, but no certificates for any earlier periods. This amount and other deductions recorded on HMRC's systems were allowed. Similarly in the earlier years the amounts recorded on HMRC's system were allowed.

6. Following further communication with the Appellant's agent, HMRC allowed the cost of goods figure which was supported by records and proposed to allow 10% of other (unverified) expenses as a concession.

7. Amendments were made to the Appellant's 2013 return, and on 5 November 2014 HMRC wrote to the Appellant and his agent who were each issued with factsheets detailing penalties for inaccurate returns.

8. In view of the inaccuracies found in the 2013 return, on 21 January 2015 HMRC issued compliance checks for 2010, 2011 and 2012.

9. On 3 February 2015 after further correspondence with the Appellant's agent, HMRC agreed by concession to allow 20 % of the unverified expenses claimed in respect of the 2013 return.

10. HMRC then examined the earlier years for which self-assessment tax returns had been submitted and again noted the high level of expenses in comparison to turnover. The Appellant was advised that HMRC proposed to amend his returns in line with the amendments to his 2013 return and that if he did not agree the figures he should provide copies of his records for 2010, 2011 and 2012 to support his returns

11. The Appellant did not provide any further documentation and therefore HMRC served a notice on the Appellant under paragraph 1 of Schedule 36 to the Finance Act 2008 requiring him to produce the same information as had previously been requested for his 2013 return.

12. As nothing further was provided, HMRC concluded that as there appeared to be no change to the way the business had operated, there had not been any great variation in the expenditure claimed, and as no copy records, copy invoices and receipts had been provided, the Appellant's expenses would be regarded as having been over-claimed in 2010, 2011 and 2012 in the same way as in the 2013 return. HMRC therefore reduced the expenses claimed by the percentages used in 2013 and also restricted the CIS tax deducted to that shown on HMRC's system.

13. Further, HMRC concluded that additional income in the Appellant's business bank account which did not appear to have been included in his returned turnover for years 2010, 2011 and 2012 had resulted in the turnover from the business being understated.

14. Closure notices for 2013 and 2014 and assessments for 2010, 2011 and 2012 were issued on 24 April 2015.

15. HMRC then similarly amended the Appellant's 2014 return.

16. In view of the inaccuracies in the returns HMRC determined that a penalty should apply under Schedule 24 Finance Act 2007 and on 24 April 2014 notified the Appellant of the penalty to be imposed. Reasons were given for applying the penalty, including the reductions for quality of disclosure. HMRC advised that they proposed to suspend the penalty subject to the Appellant in future:

- meeting all his notification and filing obligations
- keeping and preserving records of all monies received and expenses incurred in the course of his business in order to make complete and correct returns
- ensuring that expenses claimed are business related and are in line with HMRC guidance

17. Summary of assessments penalties, and additional tax due

Date	Year	Type	Source	Amount	Additional Tax
22/04/2015	2009-10	Assessment	Profits	£7,806	£2,757.48
22/04/2015	2010-11	Assessment	Profits	£12,459	£9,238.52
22/04/2015	2011-12	Assessment	Profits	£19,405	£3,482.20
24/04/2015	2012-13	Closure Notice	Profits	£45,551	£19,530.10
24/04/2015	2013-14	Closure Notice	Profits	£33,231	£8,649.33
24/04/2015	2009-10 to 2013-14	Penalty Assessment	Penalty	Suspended	£6,548.62

18. The Appellant appealed HMRC's decisions on 29 April 2014.

19. HMRC undertook a review of their decision on 26 June 2015, but upheld the decision of 24 April 2015.

20. The Appellant lodged an appeal with the Tribunal on 10 July 2015.

Legislation

21. Section 29(1) TMA 1970 provides that if an Officer of the Board or the Board discovers, as regards any person and a year of assessment, that any income which ought to have been assessed to income tax, or chargeable gains which ought to have been assessed to capital gains tax, have not been assessed, or that any assessment to tax is or has become insufficient, or that any relief which has been given is or has become excessive, the Officer, or as the case may be the Board, may subject to

subsections (2) and (3) make an assessment in the amount, or the further amount, which ought in his or their opinion to be charged in order to make good to the Crown the loss of tax.

22. Under s 34 TMA 1970, the ordinary time limit for raising an assessment is four years after the end of the tax year. The assessments were issued after 5 April 2015 and accordingly years prior to 6 April 2011 are not covered by this provision.

23. Section 36 TMA 1970 provides that where the loss of tax has been brought about carelessly, a time limit of six years applies.

24. Section 34(1) IT (Trading & Other Income) Act 2005 provides that in calculating the profits of a trade no deduction is allowed for expenses not incurred wholly and exclusively for the purposes of the trade. Under subsection (2) only any identifiable proportion of the expenses are allowable.

25. The relevant legislation with regard to penalties for the submission of an incorrect return for income tax or capital gains tax is contained in s 95 TMA 1970, which states:

> "95
>
> (1) Where a person fraudulently or negligently –
>
> (a) delivers any incorrect return of a kind mentioned in [section 8 or 8A of this Act (or either of those sections] as extended by section 12 of this Act …), or
>
> (b) makes any incorrect return, statement or declaration in connection with any claim for any allowance, deduction or relief in respect of income tax or capital gains tax, or
>
> (c) submits to an Inspector or the Board or any Commissioners any incorrect accounts in connection with the ascertainment of his liability to income tax or capital gains tax,
>
> he shall be liable to a penalty not exceeding [the amount of the difference specified in subsection (2) below.]
>
> (2) The difference is that between -
>
> (a) the amount of income tax and capital gains tax payable for the relevant years of assessment by the said person (including any amount of income tax deducted at source and not repayable), and
>
> (b) the amount which would have been the amount so payable if the return, statement, declaration or accounts as made or submitted by him had been correct.
>
> (3) The relevant years of assessment for the purposes of this section are, in relation to anything delivered, made or submitted in any year of assessment, that, the next following, and any preceding year of assessment; …"

26. Section 100 TMA 1970 allows an authorised Officer of the Board in making a penalty determination to set it at such an amount as in his opinion is correct or appropriate.

The Appellant's case

27. In his Notice of Appeal, the Appellant's agent says:

> "HMRC amended the accounts in their favour, adding items on bank statements to turnover which were clearly marked [as the Appellant's] monthly expenditure. Therefore increasing the turnover and tax due. They have also not taken into account the Contractor's deduction which is not on their system although statement from contractors had been put on the forms. They have also disallowed many of [the Appellant's] expenses saying they are too much."

28. At the hearing Mr Holmes appearing for the Appellant disputed HMRC's assessments and the penalties. He reiterated the broad grounds of appeal contained in the Notice of Appeal but said that he was not able to supply any further evidence in support. He disputed HMRC's methodology, saying that further detailed examination of the Appellant's bank statements by HMRC would show that the expenditure claimed was generally closer to the figures returned than as determined by HMRC. Similarly he said that the Appellant's turnover was much less than as assessed. He said that unfortunately the Appellant's records had all been shredded. He did not identify any specific deposits paid in the Appellant's bank account as not being business receipts and similarly did not identify any items of expenditure as valid business overheads or business costs. Nothing was offered in the form of a schedule of added back income or expenses which genuinely represented materials or other business costs.

HMRC's submissions

29. Where an amendment is made to a return following an enquiry, the burden of proof is on the Appellant to show that the amendment is wrong and the amount by which it is wrong.

30. However, HMRC is under an obligation to determine the profits on a fair and reasonable basis. From the outset of the enquiry HMRC had asked for information and evidence in order to arrive at a revised profit figure.

31. Mr Corbett for HMRC said that purchases made from the Appellant's business account had to be verified by primary evidence, of which there was none.

32. With regard to income, customers and CIS contractors do not reimburse expenses. They pay for both labour and expenses charged by the Appellant. The Appellant now concedes that he has no personal bank account which goes to credibility. The difference between the amount banked and the amount available to bank based on the return was £42,929. There were cash deposits of £13,180 into the Appellant's bank which HMRC could not accept as reimbursements for materials and other expenses without documentary proof. That amount therefore had to be added back to the Appellant's returned turnover figure.

33. With regard to expenses, the Appellant works from home. No invoices had been supplied. Under s 34 IT (Trading & Other Income) Act 2005 (2) only any identifiable proportion of the expenses are allowable. HMRC had allowed 68% of the cost of goods figure as supported by records. With regard to unverified costs HMRC initially suggested 10% but subsequently accepted the agent's proposal of 20%.

34. No records of bookkeeping costs have been submitted. The name, address and national insurance number of the bookkeeper has not been supplied. In these circumstances the claim has been disallowed in full.

35. Car, van and travel expenses had to be revised in accordance with invoices supplied, and reduced to £2,311 which reflected the amount spent on fuel.

36. In the 2013 enquiry year the Appellant claimed for tax deducted by contractors under the Construction Industry Scheme. Under the CIS, contractors deduct money from a subcontractor's payments and pass it to HM Revenue and Customs ("HMRC"). The deductions count as advance payments towards the subcontractor's tax and National Insurance. Contractors are required to tell HMRC each month about payments they have made to subcontractors through their monthly return. This includes details of the tax which they have deducted and these details are linked to the record held for the subcontractor on HMRC's CIS system. In the Appellant's case HMRC's records show that only £500 was deducted from payments made to him as opposed to the £8,720 claimed.

37. No evidence of any further deductions has been supplied by the Appellant. For plumbing and heating the scheme only applies to the installation of new systems with the maintenance and repair falling outside the scope of the scheme. As the Appellant appears to have worked mainly for property maintenance companies rather than builders it is likely that most of the work was outside the scheme.

38. HMRC assert that in the absence of any evidence to show otherwise, they were right to treat part of the excess deposits as additional sales and to revise the expenses claims as excessive. The 20% concession in the absence of documentary proof of expenditure was reasonable.

39. The Appellant failed to keep any or adequate records. The legislation covering the records to be kept for the purposes of returns is contained in s 12B Taxes Management Act 1970. Section 12B (1) Taxes Management Act 1970 requires that any person who may be required by a notice under Section 8 of the Act to make and deliver a return for a year of assessment or other period, shall keep all such records as may be requisite for the purpose of enabling him to make and deliver a correct and complete return for the year or period end.

40. The records required to be kept and preserved include records of all amounts received and expended in the course of the trade, profession or business and the matters in respect of which the receipts and expenditure take place, and in the case of a trade involving dealing in goods, all sales and purchases of goods made in the course of the trade.

41. There is also guidance leaflet THFS 1 – *Keeping records for business – what you need to know*. A person engaged in a trade business or profession must maintain: "a record of all sales and takings including cash receipts e.g. till rolls, sales invoices, bank statements, paying in slips and accounting records and a record of all purchases and expenses, including cash purchases e.g. receipts, purchase invoices, bank and credit card statements, chequebook stubs, motoring expenses and mileage records, and accounting records."

42. In *Bookey v Edwards Estates Ltd* 55 TC 486 Mr Justice Walton states:

> "there is no doubt, pursuant to Section 50 (6) of Taxes Management Act 1970, that the onus is very much upon an appellant to convince the Commissioners of Income Tax as to the accuracy of his case."

43. The same judge in *Jonas v Bamford* 51 TC 1 states:

> "but he is once again forgetting that the onus falls upon the taxpayer to show that the Revenue's figure was wrong — an onus which is not discharged merely by showing there may have been an explanation for the accretion in Mr Jonas's wealth, not that there in fact was."

44. In *Nicholson v Morris* 51 TC 95 Walton J states on page 110:

> "The Taxes Management Act throws upon the taxpayer the onus of showing that the assessments are wrong. It is the taxpayer who knows and the taxpayer who is in a position (or, if not in a position, who certainly should be in a position) to provide the right answer, and chapter and verse for the right answer, and it is idle for any taxpayer to say to the Revenue, "Hidden somewhere in your vaults are the right answers: go thou and dig them out of the vaults". That is not a duty on the Revenue. If it were, it would be a very onerous, very costly and very expensive operation, the costs of which would of course fall entirely on the taxpayers as a body. It is the duty of every individual taxpayer to make his own return and, if challenged, to support the return he has made, or, if that return cannot be supported, to come completely clean, and if he gives no evidence whatsoever he cannot be surprised if he is finally lumbered with more than he has in fact received. It is his own fault that he is so lumbered."

45. It is clear that the Appellant did not retain a record of his income and expenditure to support the returned figures of turnover and expenditure in his self-assessment. Under s 12B TMA 1970(5) any person who fails to comply with subsection (1) [or (2A)] in relation to a year of assessment or accounting period shall be liable to a penalty not exceeding £3,000. On this occasion HMRC have not charged a penalty.

46. Penalties are however chargeable for deliberately making an incorrect income tax return. It is for HMRC to show incorrect returns were submitted negligently, and to show that the inaccuracies in the returns were a result of careless behaviour. If this is established the onus of proof reverts to the Appellant to show the quantum of the penalty is wrong. The statutory onus of proof is on the Appellant (s 50(6) Taxes Management Act 1970). HMRC assert that the Appellant had not discharged that onus.

47. From 2009 onwards penalties are chargeable under Schedule 24 Finance Act and the legislation sets a level of penalties of 35% minimum to 70% maximum for deliberate behaviour and a prompted disclosure, which means knowingly providing an inaccurate document to HMRC. As the Appellant failed to take action in respect of his records to ensure that his return was accurate, a penalty was chargeable on that basis.

48. Following reductions to reflect disclosure and cooperation the penalties represented 15% of the additional tax due and in any event had been conditionally suspended.

Conclusion

49. The onus is on the Appellant to show that he has been overcharged by the amendments to his self-assessments. In our view he has not discharged that burden. The Appellant has not produced any documentary evidence to displace the figures in HMRC's closure notices and assessments. No meaningful evidence has been adduced by the Appellant to show that HMRC's assessments are incorrect.

50. The Appellant failed to take reasonable care in both maintaining records and submission of his tax returns.

51. Deposits paid into the Appellant's bank account were from his business and had been omitted from the sales turnover in his accounts and returns. The Appellant said that some of the deposits were reimbursements for materials paid for out of another personal account, which he later admitted was incorrect. Most unidentified deposits were round figures and the Appellant has been unable to identify the source of those funds and show that they did not arise from his business. We accordingly find that HMRC's assessment of the Appellant's turnover for all the years under appeal are correct

52. With regard to 'cost of goods' claims we concur entirely with HMRC that a 20% allowance for unverified claims is reasonable.

53. With regard to vehicle and wages claims, for the reasons explained by HMRC we agree that these should be disallowed where not supported by primary evidence.

54. Similarly amounts claimed for rent, rates, insurance, interest financial charges and other sundry unidentified expense claims cannot be allowed without supporting evidence.

55. The CIS tax deducted at source has been correctly identified for each year under appeal and allowed by HMRC.

56. The amendments to the Appellants self-assessment for the 2012-13 and 2013-14 tax years, and the discovery assessments raised in respect of the 2009-10, 2010-11 and 2011-12 tax years are accordingly confirmed.

57. We also concur with HMRC that the penalties imposed have been correctly applied. The penalties imposed are reasonable and the Appellant has not discharged

the onus upon him to demonstrate that they are excessive or have been calculated incorrectly. They are therefore also confirmed.

58. The appeal is dismissed.

59. 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.

MICHAEL CONNELL
TRIBUNAL JUDGE

RELEASE DATE: 16 AUGUST 2016