[2016] UKFTT 0593 (TC)

TC05329

Appeal number: TC/2014/00749
TC/2014/00984

INCOME TAX, NATIONAL INSURANCE CONTRIBUTIONS – computation of profits of accounting business and property business – whether flat conversion allowances validly claimed – whether various expenses deductible – whether late payment penalties and surcharges due – appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

OLAYINKA AYENI **Appellant**

- and -

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

TRIBUNAL: JUDGE JONATHAN RICHARDS
G. NOEL BARRETT LLB

Sitting in public at Fox Court, Brooke Street, London on 1 August 2016

The Appellant in person

Gill Cawardine, Officer of HM Revenue & Customs, for the Respondents

DECISION

1. Mr Ayeni carries on a business as a chartered certified accountant. He also owns properties (both in his own name and jointly with his wife) that have been let to tenants. He is appealing against various adjustments that HMRC have made to his income tax and national insurance position in respect of both the accountancy business and the property letting business and also against some late payment penalties and surcharges.

Procedural background

2. Mr Ayeni's Notice of Appeal to the Tribunal was submitted in February 2014 and was distinctly lacking in particulars. In that Notice of Appeal he stated that he was appealing against "various" decisions issued on "various dates". This resulted in a lengthy process of seeking to discern precisely what he was appealing against and precisely which of those appeals were in time. It might well have been open to HMRC to apply to the Tribunal for a direction that, unless Mr Ayeni provided adequate particulars, the entire appeal should be struck out. However, to their credit, HMRC did not do this and instead prepared (with little, if any, assistance from Mr Ayeni) a schedule of all decisions that they had made in relation to Mr Ayeni's tax affairs for the tax years in question and considered whether Mr Ayeni could be taken as appealing against all or any of those decisions.

3. An interim Tribunal hearing took place on 5 October 2015 at which the Tribunal considered the extent to which Mr Ayeni could be taken as making valid, in time, appeals against the decisions that HMRC had identified. Where Mr Ayeni appeared either to have made his appeal to HMRC out of time, or to have notified that appeal to the Tribunal out of time, the Tribunal considered whether permission should be given to make, or notify, a late appeal. Mr Ayeni did not attend that hearing (and he informed us that this was because he was not aware of it).

4. Following that hearing, on 20 October 2015, the Tribunal released a decision that set out those aspects of Mr Ayeni's appeal that could proceed. In addition, on 25 January 2016, the Tribunal (having considered written representations from both parties) struck out that part of Mr Ayeni's appeal that related to the 2004-05 and 2005-06 tax years which had been determined at a hearing before the General Commissioners in 2009. Mr Ayeni confirmed to us that he had received both Tribunal decisions. He has not to date applied for permission to appeal against either decision (or requested the Tribunal to consider setting aside the decision of 20 October 2015 on the grounds that he did not attend the relevant hearing).

5. Mr Ayeni expressed dissatisfaction to us that certain aspects of his appeal (in particular those relating to a number of late payment penalties and penalties for failure to produce documents) would not be considered. If Mr Ayeni considers that the Tribunal's decisions of 20 October 2015 or 25 January 2016 were wrong, he should seek permission to appeal against the relevant Tribunal decisions (and make an

application for the Tribunal to consider that application late). At this hearing, we considered appeals in relation to the matters set out in the table below.

Tax Year	Nature of decision	Date of decision	Amount
2006-07	Closure notice	14 March 2010	£17,095.37 (reduced to £13,671.05 on 21 September 2010)
	Late payment surcharge	11 May 2010	£129.03
2007-08	Closure notice	16 March 2010	£12,623.56 (reduced to £8,905.28 on 30 October 2010)
	Late payment surcharge	18 June 2010	£224.43
2008-09	Closure notice	13 September 2011	£36,626.42 (reduced to £18,160.39 on 15 January 2016)
2009-10	Closure notice	18 September 2012	£9,574.88 (reduced to £8,812.16 on 30 October 2012)
2010-11	Late payment penalty	10 April 2012	£466

Evidence

6. We were provided with a bundle of documentary evidence. Mr Ayeni also gave oral evidence at the hearing. We found him to be an honest witness. However, his evidence was often quite vague and this was not helped by the fact that in many cases there was an insufficiency of documentary evidence to support his oral evidence. HMRC did not rely on any witness evidence.

Matters in dispute

7. Mr Ayeni did not dispute that HMRC validly opened enquiries into his tax returns for each of 2006-07, 2007-08, 2008-09 and 2009-10. The hearing bundles contained notices of enquiry into these tax returns which were, in all cases, issued within the applicable time limits. It follows that HMRC were entitled to issue the closure notices for those tax years that they did issue and in the remainder of this decision we will consider whether the closure notices correctly state the amounts of tax and national insurance contributions that were due. We will consider whether HMRC were entitled to issue the penalty and surcharge notices in the section of this decision that deals with Mr Ayeni's appeal against those penalties and surcharges.

8. The following table summarises (at a very high level) the particular matters that were in dispute for the tax years in question.

Matter in dispute	Mr Ayeni's position	HMRC's position
Deductibility of certain property related expenses in 2006-07	The expenses were deductible as costs of putting a property into a condition where it could be let to tenants.	There was insufficient evidence to demonstrate the costs were deductible.
Deductibility of life assurance premiums in 2006-07 and 2007-08	The life assurance was a condition of obtaining loans used for business purposes and should be deductible in the same way as interest.	Mr Ayeni had not demonstrated obtaining the life assurance was a condition of obtaining the loan. The connection with the business was too remote.

Whether loan interest of £2,020 should be disallowed in 2007-08	This interest was no different from other interest.	There was insufficient evidence to demonstrate this was deductible as loan interest certificates had not been provided.
Deductibility of expenses totalling £2,073 and £14,857 in 2007-08	The expenses were deductible.	Insufficient evidence of deductibility.
Whether Mr Ayeni was subject to tax on £12,519 relating to rent received in 2008-09	Mr Ayeni had validly notified HMRC that only his wife was to be taxed on this income. In any event the £12,519 ignored associated expenses.	The election was of no effect and Mr Ayeni remained subject to tax on that income.
Whether Mr Ayeni was entitled to a deduction for £17,064 of property related expenses in 2008-09	If Mr Ayeni was subject to tax on the income of £12,519, he should obtain relief for these expenses.	Insufficient evidence of deductibility.
Whether Mr Ayeni was entitled to Flat Conversion Allowances in 2007-08 and 2008-09	A valid claim for allowances was made by letter dated 20 December 2012.	No valid claim had been made. There was no evidence that the conditions for FCAs were satisfied.
Late payment penalties and surcharges	These should not have been issued until Mr Ayeni had agreed the underlying tax liabilities.	Mr Ayeni's agreement of the underlying tax liabilities was not necessary for a penalty or surcharge to be payable.

9. During the hearing, certain points that were in dispute were resolved and are not, therefore, reflected in the above table. In particular:

(1) HMRC abandoned their assertion that capital allowances on a motor vehicle should be reduced by £599 to reflect private use in return for Mr Ayeni agreeing, in the future, to prepare, and to produce on request, a record of private mileage of any vehicle that is used for both business and personal purposes.

(2) Mr Ayeni abandoned an argument that he should be entitled to a deduction in relation to a notional payment of £55,000 to himself in respect of the office used for his accountancy practice.

10. We consider that Mr Ayeni has the burden of proving matters relating to the correct quantification of his taxable income for the years in question. Therefore, where Mr Ayeni is arguing that he should benefit from a deduction in computing his income, or that a particular type of income is not taxable, he has the burden of proving that matter. HMRC, however, have the burden of proving that the conditions necessary to impose the penalties or surcharges have been met.

General findings of fact

11. We will deal with each of the items in dispute (as set out in the table at [8] above) in a separate section and will make separate findings of fact where necessary to resolve those items. However, we have also made the following general findings of fact that are relevant to a number of aspects of Mr Ayeni's appeal.

12. Mr Ayeni conducts his accountancy business under the trading name of "O.A. George & Co – Chartered Certified Accountants & Registered Auditors". His office is located in New Cross in London.

13. Mr Ayeni owns the building in which his office is located in his sole name. (It is not relevant to this decision whether he has a freehold or leasehold interest.) That building also contains other offices which are used by other businesses.

14. Before Mr Ayeni acquired the office in New Cross, it was used as a DIY shop. Above that shop were two units that were designed for occupation as self-contained flats. The DIY business used those units to store stock so, when Mr Ayeni acquired the building, they were not used as flats. Mr Ayeni subsequently incurred expenditure on those units for the purposes of bringing them back into use as residential flats and, at some point, the flats were let to residential tenants.

15. Mr Ayeni and his wife also own a residential property situated in Monson Road, London. Although Mr Ayeni did not produce any legal documentation that explained their ownership interests in that property, he said in evidence that he and his wife owned the property "jointly". Mrs Cawardine did not challenge that evidence. Mr Ayeni is not a lawyer and probably was not seeking to make any distinction between whether the property was owned as joint tenants or as tenants in common. It is not necessary for the purposes of this decision to make a finding on that specific issue. In view of Mr Ayeni's unchallenged evidence we have concluded that, at the material times, Mr Ayeni and his wife had equal shares in the property in Monson Road (either by virtue of holding that property as joint tenants, or by virtue of holding it as tenants in common in equal shares).

Deductibility of property related expenses in 2006-07

Findings of fact

16. In computing profits from his property letting business in 2006-07, Mr Ayeni claimed a deduction for insurance premiums of £158, rates of £862 and the cost of repairs totalling £4,040.

17. In his oral evidence, Mr Ayeni gave evidence as to the nature of these expenses. He said that, in the 2006-07 tax year, he and his wife moved out of the property at Monson Road as they had decided to let it to tenants. However, before they could let the property to tenants they had to spend money to make it suitable for letting. During that period, they remained liable for the payment of rates to the local council.

18. Mr Ayeni explained that he spent £3,470 having the roof fixed (as it was leaking and tiles on it needed to be replaced). He spent £570 on fixing a plumbing problem. The £158 related to buildings insurance. Mrs Cawardine did not challenge Mr Ayeni's evidence that he had spent the sums above and we have therefore accepted that he did. We have also concluded that the sums above were the total amount spent (not a half share of the total expenses attributable to Mr Ayeni's half share in Monson Road). We have reached that conclusion because Mr Ayeni showed us documentation relating to

the repair works from third party contractors (who would be expected to present a total bill for their work and not separate bills for Mr Ayeni and his wife). Moreover, Mr Ayeni showed us spreadsheets evidencing payment of the amounts in question and did not suggest that the figures on these spreadsheets were 50% of a larger amount.

19. Mrs Cawardine did not challenge Mr Ayeni's description of the purpose for spending those sums. There were, perhaps, points that could have been put to Mr Ayeni in cross-examination. For example, while Mr Ayeni had described the work on the roof in the terms outlined at [18], the estimate prepared by the building contractor described the work as:

> Supply and fix new Eternite Slate Roof to main up and over roof
>
> Supply and fix Lead Work as required to party wall
>
> Clear all slates and rubbish from site.

That, perhaps, suggests that there was more to the work than simply replacing a few slates and that the works might in fact have involved the complete replacement of the roof. However, since there was no challenge to Mr Ayeni's description of the roof works, we have accepted it.

Legal principles

20. Section 272 of the Income Tax (Trading and Other Income) Act 2005 ("ITTOIA") provides for certain principles governing computation of taxable trading income to apply for the purposes of calculating the taxable income of a property business. In particular, in determining whether expenditure is deductible in computing the profits of a property business, the provisions of s33 of ITTOIA and s34 of ITTOIA are applied. Those sections provide as follows:

> **33 Capital expenditure**
>
> In calculating the profits of a trade, no deduction is allowed for items of a capital nature.
>
> **34 Expenses not wholly and exclusively for trade and unconnected losses**
>
> (1) In calculating the profits of a trade, no deduction is allowed for—
>
> (a) expenses not incurred wholly and exclusively for the purposes of the trade, or
>
> (b) losses not connected with or arising out of the trade.
>
> (2) If an expense is incurred for more than one purpose, this section does not prohibit a deduction for any identifiable part or identifiable proportion of the expense which is incurred wholly and exclusively for the purposes of the trade.

21. It therefore follows that, in order for the items in question to be deductible, they must be of a revenue nature and incurred wholly and exclusively for the purposes of

the property business. That requires an examination of how much has been incurred and the nature of the expenditure, including why it has been incurred.

22. Although neither party referred to it in their submissions, s272 of ITTOIA also provides for the provisions dealing with "pre-trading expenditure" (in s57 of ITTOIA) to apply for the purposes of calculating profits of a property business. Section 57 provides as follows:

> **57 Pre-trading expenses**
>
> (1) This section applies if a person incurs expenses for the purposes of a trade before (but not more than 7 years before) the date on which the person starts to carry on the trade ("the start date").
>
> (2) If, in calculating the profits of the trade—
>
> (a) no deduction would otherwise be allowed for the expenses, but
>
> (b) a deduction would be allowed for them if they were incurred on the start date,
>
> the expenses are treated as if they were incurred on the start date (and therefore a deduction is allowed for them).

Discussion

23. There is a question as to whether the expenditure on the roof was of a revenue or capital nature. Central to that issue is the question of whether Mr Ayeni was incurring expenditure on a completely new roof (which might be capital in nature) or whether he was incurring expenditure on repair of the existing roof (which would be more likely to be revenue). However, if Mrs Cawardine wished to argue that the expenditure was capital, she would have needed both to challenge Mr Ayeni's description of the roof works and made at least some submissions as to why it was capital. Since she did not, we have concluded that the expenditure on the roof was of a revenue nature. We were satisfied that the other disputed expenses (the insurance, the rates and the costs of plumbing repairs) were also of a revenue nature.

24. There is, to our mind, a real question as to whether the expenses were incurred wholly and exclusively for the purposes of the property business. For example, it might be assumed that the roof at Monson Road became dilapidated as a result of events taking place while it was used as a private residence. One can speculate that the only reason that Mr Ayeni and his wife were obliged to continue to pay rates of £862 was because the property had not yet been let and that, if the property had been let, the rates would have been the responsibility of the tenant. If that were the case then expenditure on rates would be the very opposite of expenditure incurred for the purposes of a letting business. However, we had no evidence on matters such as this, and Mr Ayeni's evidence, that the expenditure was incurred in order to enable Monson Road to be let, was not challenged. In those circumstances, we have concluded that the expenses set out at [16] were included wholly and exclusively for the purposes of the property business or, to the extent they were not because the

property business had not commenced when the expenses were incurred, they were pre-trading expenditure that was deductible under s57 of ITTOIA.

25. There is then the question of how much of a deduction Mr Ayeni should obtain in respect of these expenses. We have found at [18] that the expenses for which Mr Ayeni claimed a deduction were the total amount of those expenses. For the tax year in question the effect of s282 of the Income and Corporation Taxes Act 1988 ("ICTA"), the predecessor to s282 of the Income Tax Act 2007 which we deal with in detail later in this decision, was that, since Mr Ayeni and his wife owned Monson Road in equal shares each was subject to tax on 50% of the income derived from that property[1]. Since the measure of taxable income is calculated by subtracting expenses incurred from income received, we consider that a similar principle applies for the purposes of allocating expenses. It follows that Mr Ayeni should be treated as incurring deductible expenditure equal to 50% of the sums set out at [16] (i.e. £2,545). We do not know if Mrs Ayeni has claimed a deduction for her 50% share of those sums. If she has not, then Mr and Mrs Ayeni will not, between them, have claimed the full deduction to which they are entitled. However, that cannot alter our conclusion which is that Mr Ayeni is entitled to a deduction for only 50% of the expenses claimed.

Life assurance premiums

Findings of fact

26. Mr Ayeni has borrowed money for the purposes of his accountancy practice. We were not shown the precise amount of those borrowings or a breakdown of the interest expense that he has incurred on various loans. However, it was common ground that at very least a proportion, and perhaps a substantial proportion, of the interest expense that he incurred in the tax years 2006-07 and 2007-08 was a deductible expense of his accountancy profession.

27. We were satisfied that Mr Ayeni paid life assurance premiums of £4,603 in the tax year 2006-07 and of £3,126 in the tax year 2007-08. He did not show us evidence of payment of life assurance premiums in any other tax year at issue for the purposes of this appeal. Mr Ayeni gave oral evidence to the effect that he did not choose to, or wish to, take out the underlying life assurance policies. However, he said that it was a condition of the loans that he take out the policies. He showed us two business loan facility letters dated 12 March 1997 and 21 January 1998 from Barclays Bank plc which required Mr Ayeni to provide security for those loans in the form of a fixed charge over a life policy approved by the bank. His evidence was not challenged in cross-examination and we have accepted it and have concluded that Mr Ayeni could not have obtained the loans had he not also taken out the life assurance policies. Mrs Cawardine did, however, submit that HMRC had asked Mr Ayeni on a number of

[1] There was no suggestion that any election under s282B of ICTA had been made for the tax year 2006-07 although, as discussed later in this decision, Mr Ayeni did appear to argue that such an election had effect in later tax years.

occasions to provide evidence that it was a contractual requirement of the loans that he obtain the life assurance policies but Mr Ayeni had failed to do so.

Legal principles

28. We have already referred to s34 of ITTOIA 2005 which permits, subject to statutory exceptions, a deduction for expenditure that is incurred wholly and exclusively for the purposes of a trade or profession.

29. Section 58 of ITTOIA also provides a deduction for the incidental costs of obtaining loan finance. As in force for the tax years in question, it provided as follows:

> **58 Incidental costs of obtaining finance**
>
> (1) In calculating the profits of a trade, a deduction is allowed for incidental costs of obtaining finance by means of—
>
> (a) a loan, or
>
> (b) the issue of loan stock,
>
> if the interest on the loan or stock is deductible in calculating the profits of the trade.
>
> (2) "Incidental costs of obtaining finance" means expenses—
>
> (a) which are incurred on fees, commissions, advertising, printing and other incidental matters, and
>
> (b) which are incurred wholly and exclusively for the purpose of obtaining the finance, providing security for it or repaying it.
>
> …
>
> (4) But the following are not incidental costs of obtaining finance—
>
> (a) sums paid because of losses resulting from movements in the rate of exchange between different currencies,
>
> (b) sums paid for the purpose of protecting against such losses,
>
> (c) the cost of repaying a loan or loan stock so far as attributable to its being repayable at a premium or having been obtained or issued at a discount, and
>
> (d) stamp duty.
>
> …

Discussion

30. After she saw the evidence of the contractual link between the loans and the life assurance policies that Mr Ayeni presented at the hearing, Mrs Cawardine said that she did not wish to make any submissions to the effect that the life assurance premiums were not deductible although she did not formally concede the point and asked the Tribunal to make a determination of it.

31. Given our findings at [27], we have concluded that the requirements of s58 of ITTOIA are met. Since we are not sure what proportion of Mr Ayeni's total interest expense is deductible in computing the profits of his accountancy profession, we will not specify the precise amount of deduction to which he is entitled in relation to the life assurance premiums. Rather we will simply decide that Mr Ayeni should, in 2006-07 and 2007-08 be entitled to a deduction for a proportion of the premiums of £4,603 and £3,126. The proportion of those premiums that is deductible should be the same as the proportion of the total interest expense that he claimed in the computation of his accountancy profits for those years that is deductible for tax purposes.

Loan interest of £2,020 in 2007-08

32. In the property income section of his amended tax return for 2007-08, Mr Ayeni claimed relief for an interest expense of £12,122. A letter from HMRC dated 12 September 2012 indicated that HMRC considered that this represented an increase of £2,020 on a previous claim for £10,102 and that, since no satisfactory explanation had been given of the increase, that part of the claim would be disallowed. However, neither Mr Ayeni nor Mrs Cawardine was able to show us the original claim of £10,102 and we could not ourselves find it in the bundle of tax returns provided.

33. Mr Ayeni was not able to explain why HMRC had given him insufficient relief for loan interest. He showed us some copies of loan agreements and mortgage statements that were in the bundle and his evidence in this respect was not challenged. However, that evidence did not come close to supporting his evident view that the amount of deduction for interest expense to which he was entitled was greater than HMRC had allowed. We have therefore dismissed this aspect of his appeal.

Deductibility of property related expenses, and other expenses of £14,857, in 2007-08

34. In his tax return for 2007-08, Mr Ayeni claimed a deduction for some £2,073. Even at the hearing, it was not clear what the expenses in question were. However, contemporaneous documentation suggested that some £808 related to rates in respect of the flats above Mr Ayeni's office and £1,165 related to the costs of installing heating. At the hearing, Mr Ayeni was unable to offer any evidence as to precisely what the £1,165 expense involved and why it had been incurred. We were not sure whether this expense related to the flats above the office, Monson Road or even Mr Ayeni's private residence. However, there was no challenge to his evidence that he incurred £808 of deductible expenditure on rates for the flats above the office.

35. Mr Ayeni had also, in his 2007-08 tax return claimed a tax deduction for £14,857 of other expenses. (For reasons that no-one was able to explain to us, this figure was 82% of a larger figure of £18,086.) Mr Ayeni was not able to provide any evidence at all of what those expenses related to (or even a general description of the kind of expenses involved). However, he said that this information had previously been provided to HMRC and we have accepted that this is the case as there was a letter in the hearing bundle from HMRC to Mr Ayeni dated 8 October 2010 which thanked him for "the detailed schedule in respect of Repair Costs of £18,086". Mr

Ayeni said that he had full documentation at home which he was confident would establish that the full figure of £14,857 was deductible.

36. In view of the fact that Mr Ayeni had evidently previously provided HMRC details on the £14,857 figure, Mrs Cawardine indicated that she would be prepared to "split the difference" and consider accepting that half of this amount was deductible. However, Mr Ayeni was not prepared to accept this offer and asked for an adjournment to permit him to provide HMRC with details on the £14,857 figure (with a view to establishing that it was all deductible) and fuller details on the other costs referred to at [34].

37. Mrs Cawardine did not object to the idea of an adjournment. However, we decided not to adjourn the hearing to permit further evidence to be given on these issues. We noted that the appeals had been made some time ago. The process of determining what decisions Mr Ayeni was appealing against and why has already taken up a significant amount of HMRC's time and Tribunal resources and, as we have noted at [2] to [4] above, Mr Ayeni did not contribute to the process of resolving those issues. Both parties have received Tribunal directions requiring them to share documentary evidence with each other and Mr Ayeni, as a professional man, should have understood that he needed to marshal his evidence in advance of the hearing. In short, we concluded that both parties had been given an adequate opportunity to gather their evidence together and that it was not in the interests of other Tribunal users that we adjourn this appeal, which would result in it taking up still more time and Tribunal resources. We explained this decision to the parties during the hearing itself and suggested that Mr Ayeni might wish to reconsider his approach to Mrs Cawardine's offer in the light of it.

38. By the time the hearing finished, Mr Ayeni and Mrs Cawardine had not reached an agreement on the deductibility of these expenses. We therefore make a decision on this issue in case no agreement has been reached subsequent to the hearing. In other tax years we have accepted that Mr Ayeni is entitled to a tax deduction in computing the profits of his property business for expenditure on rates. We will therefore allow a deduction for £808 of rates (the full amount claimed since this amount relates to the flats which were owned by Mr Ayeni alone and not jointly with his wife). Since Mr Ayeni was not able to explain precisely what the remaining expenses were, or the purpose for incurring them, he did not satisfy his burden of proving that they were deductible.

Rent of £12,519 received in the tax year 2008-09

Findings of fact

39. In his amended tax return for the tax year 2008-09 (which Mr Ayeni filed on 5 October 2011), Mr Ayeni included an amount of £12,519 in relation to "other business income". He maintained, however, in that return that this amount was not subject to tax.

40. HMRC asked Mr Ayeni to explain why the £12,519 was not taxable income. However, they did not receive an answer that satisfied them and accordingly proceeded, in calculating the amount of tax that they considered Mr Ayeni to owe, on the basis that this sum was taxable.

41. Mr Ayeni wrote a letter to HMRC dated 17 October 2012 that included the following paragraphs:

> Please be informed that the rental property on Monson Road being a jointly held property has (in agreement with my wife) been decided will be her responsibility from 2006/7, consequently, I have adjusted my accounts for all years with the effect of the changes for your attention. As regards the flats above the offices, I will continue to be responsible for them.
>
> In view of the fact that I had been responsible for the Monson Road property, my wife will have to declare them on her Returns. However, before she submits them, I should be grateful to receive your acceptance of the revised Returns for the years 2006/07 to 2009/10 enclosed.

42. HMRC replied to this letter on 30 October 2012 and their letter included the following paragraph:

> I have noted your request for the rental income from Monson Road to be assessed in full on your wife and enclose a form 17 to make declaration of beneficial interests in the joint property and income. Please supply papers to confirm that this property is held in joint name but note that an election can only be effective from the date of signature of the form which must be submitted within 60 days of signature.

(That letter also recorded HMRC's view that they had still not been provided with a satisfactory explanation of the nature of the £12,519 "other business income" referred to at [39].)

43. In Grounds of Appeal that Mr Ayeni submitted to the Tribunal in February 2014, Mr Ayeni included the following paragraphs:

> I have not made any declaration on the flats and have informed the Inspector to that effect, but he kept raising assessments on the flats. In order to separate the two operations, I decided with my wife to let her bear the responsibility for the flats. I therefore do not agree to the non-business income of £12,519 being added to my income as this was rent received on the flats between May 2007 and April 2008 and was excluded from my income in the tax computations.

44. The extract of the Grounds of Appeal referred to at [43] appears to be inconsistent with the letter that Mr Ayeni wrote to HMRC on 17 October 2012 referred to at [41]. In his letter, Mr Ayeni purported to transfer responsibility for tax on rent on Monson Road, but to retain responsibility for tax on rent generated by the flats. However, the Grounds of Appeal suggest that he considered he had made an

election as regards income on the flats (and says nothing about income received on Monson Road).

45. In his oral evidence, Mr Ayeni contradicted the statement in his Grounds of Appeal in some respects. He said that the £12,519 represented the total gross rent received on Monson Road (which, as we have noted was owned jointly by him and his wife) and not the gross rent on the flats (which he owned himself). Specifically, Mr Ayeni said that the figure was not a half share in that gross rent; it was the total amount of the rent paid. None of that evidence was challenged and we have accepted it.

Legal principles

46. For the tax years 2008-09 and subsequently, s836 and s837 of the Income Tax Act 2007 ("ITA 2007") deal with property owned by husband and wife. Those provisions provide, so far as material, as follows:

> **836 Jointly held property**
>
> (1) This section applies if income arises from property held in the names of individuals—
>
> (a) who are married to, or are civil partners of, each other, and
>
> (b) who live together.
>
> (2) The individuals are treated for income tax purposes as beneficially entitled to the income in equal shares.
>
> (3) But this treatment does not apply in relation to any income within any of the following exceptions.
>
> *Exception A* Income to which neither of the individuals is beneficially entitled.
>
> *Exception B* Income in relation to which a declaration by the individuals under section 837 has effect (unequal beneficial interests).
>
> …
>
> **837 Jointly held property: declarations of unequal beneficial interests**
>
> (1) The individuals may make a joint declaration under this section if—
>
> (a) one of them is beneficially entitled to the income to the exclusion of the other, or
>
> (b) they are beneficially entitled to the income in unequal shares,
>
> and their beneficial interests in the income correspond to their beneficial interests in the property from which it arises.
>
> (2) The declaration must state the beneficial interests of the individuals in—

(a) the income to which the declaration relates, and

(b) the property from which that income arises.

(3) The declaration has effect only if notice of it is given to an officer of Revenue and Customs—

(a) in such form and manner as the Commissioners for Her Majesty's Revenue and Customs may prescribe, and

(b) within the period of 60 days beginning with the date of the declaration.

(4) The declaration has effect in relation to income arising on or after the date of the declaration.

…

47. The general rule is that set out in s836 of ITA 2007. Income derived from property held in the names of a husband and wife who live together is to be treated as received by them in equal shares. The husband and wife can vary that general rule by an election under s837. However, before they can make an election, one of the conditions set out in s837(1) must be satisfied. If, as a matter of general law, the husband and wife are beneficially entitled to income arising from the jointly held property in equal shares, they cannot make an election under s837 of ITA 2007 so as to result in only one of them being subject to tax on that income. Any declaration that is made must be a joint declaration and, as is made clear by s837(4), takes effect in relation to income arising after the date of the declaration. A declaration cannot, therefore, be made in relation to income that has already arisen.

Discussion

48. Mr Ayeni's evidence that the £12,519 was rent received on the Monson Road property was not challenged although it appears at first sight not to be consistent with what he said in his Grounds of Appeal referred to at [43]. We have therefore accepted this evidence which is important because, since we have found that Mr Ayeni and his wife jointly owned Monson Road (see paragraph [15] above), the starting position under s836 of ITA 2007 is that Mr Ayeni is subject to tax on only half of the figure of £12,519. We asked Mrs Cawardine whether, given that Mr Ayeni had included the full amount of £12,519 in his amended tax return for 2007-08, she wished to submit that he could not now argue that he is subject to tax on only half that figure. Mrs Cawardine said that she did not wish to make any submissions to this effect. We have therefore concluded that applying the general rule under s836, Mr Ayeni received taxable income of £6,259 (prior to deduction of expenses which we will consider further below).

49. The letter of 17 October 2012 referred to at [41] was not a valid election under s837 of ITA 2007 and does not, therefore, alter the position set out at [48]. Firstly, since we have concluded that Mr Ayeni and his wife owned Monson Road in equal shares, the conditions necessary to make an election under s837 were not satisfied. Mr Ayeni has not demonstrated that, as a matter of general law, his wife owned the rent arising on Monson Road to the exclusion of him. Secondly, even if the conditions were satisfied, the letter was not a "joint" election of both Mr Ayeni and his wife but

was signed only by Mr Ayeni. Finally, the letter of 17 October 2012 was sent after the rental income arose in the 2008-09 tax year and could not, therefore, have any effect on the tax liability of Mr Ayeni or his wife on that income.

Expenses of £17,064 in 2008-09

50. In box 16 of an amended tax return for 2008-09 (which Mr Ayeni submitted on 5 October 2011) Mr Ayeni included an amount of £17,064 as representing allowable expenses falling within the section headed "other UK income not included on supplementary pages". On 24 October 2011, HMRC requested information on the nature of these expenses. On 12 September 2012, HMRC wrote to Mr Ayeni to explain that, in the absence of any information on those expenses, no relief had been given for them. In January 2016, as part of the process of seeking to agree which matters were in dispute for the purposes of the proceedings before the Tribunal, HMRC wrote to Mr Ayeni saying that they had not received any details on the £17,064 figure but that if Mr Ayeni provided some information, HMRC would consider it.

51. Having not previously advanced an explanation of the £17,064 figure, Mr Ayeni gave an explanation in his oral evidence to the Tribunal and said that it related to expenses associated with the Monson Road property (such as mortgage interest, insurance and council tax payments). He was not able to give a much fuller account of the figure than this (although he said that he thought the expenses were similar in amount to those incurred in 2008-09) and did not show us any invoices or evidence of payment which could have cast further light on matters. He said, however, that he could arrange for evidence to be faxed to the Tribunal and asked for a short adjournment to deal with this. We refused this request for reasons similar to those outlined at [37]. We doubted whether it would be practicable to get the new evidence by fax in the time remaining for the hearing. We were also concerned that, in circumstances where HMRC had evidently been seeking information on the £17,064 figure for well over four years, it would not be fair to allow Mr Ayeni to admit new evidence during the hearing and require HMRC to respond to it immediately.

52. Mr Ayeni was able, however, to show us a mortgage statement relating to a loan (in the joint names of Mr Ayeni and his wife) which he said had been taken out to purchase the Monson Road property. That statement showed that between 18 January 2006 and 17 January 2007, interest of £10,581.40 was payable on that loan. He said that the amount of interest payable on that loan would have been about the same in the 2008-09 tax year and that, in that tax year, Mr Ayeni and his wife therefore incurred a similar level of interest expense for the purpose of the property business. Mrs Cawardine did not challenge this evidence at all in cross-examination; nor did she suggest that relief had already been given for mortgage interest. We have, therefore, accepted Mr Ayeni's evidence and concluded that in 2008-09, he was entitled to relief of £5,290 (half of the annual interest expense shown on the statement).

Flat conversion allowances in 2007-08 and 2008-09

Findings of fact

53. In 2007-08 and 2008-09, Mr Ayeni incurred expenditure associated with putting the units above his office in a condition where they could again be used as residential flats. We will not make findings as to the precise amount he spent for these purposes, as we do not need to. However, we accept that the amount he spent was more than £50,000 in the two tax years. Mr Ayeni accepted that in his tax returns for those tax years, he made no claim for flat conversion allowances under what was then Part 4A of the Capital Allowances Act 2001. That accords with our own review of Mr Ayeni's returns (as amended) for those years. Mr Ayeni did, however, seek to claim the costs of the conversions as revenue deductions and provided HMRC with some evidence as to the nature of the expenditure in question. HMRC objected to this claim on the basis that the expenses were capital in nature.

54. On 20 December 2012, which was after HMRC had issued closure notices relating to his 2007-08 and 2008-09 tax returns on 16 March 2010 and 13 September 2011, Mr Ayeni sent a letter to HMRC which included the following paragraphs:

> **Flats Over the Shop (FOTS) Claim**
>
> Please be informed that I intend to claim the above allowances on the expenditure that I incurred in converting the two flats above the office.
>
> In addition to the repairs and other costs which the Inspector has hitherto disallowed, the cost of the conversion of £52,247 is now being claimed. The effect of this is to cancel all the liabilities and charges the Inspector has raised against me.

55. The parties were agreed that the reference to "Flats Over the Shop" was a reference to flat conversion allowances contained in what was then Part 4A of the Capital Allowances Act 2001 (which has since been repealed). However, in cross-examination, Mrs Cawardine suggested to Mr Ayeni that the letter above evidenced an intention to make a claim for flat conversion allowances in the future and was not itself an actual claim for flat conversion allowances. We have accepted Mr Ayeni's evidence that he was seeking to make an actual claim for capital allowances. It is clear from the letter itself that Mr Ayeni considered his letter had an actual effect (of eliminating his tax liability). If he intended his letter simply to set out his intention to make a claim in the future, he would not have considered that his letter had this effect. Moreover, later correspondence suggested that Mr Ayeni thought he had made a valid claim for flat conversion allowances.

56. Beyond Mr Ayeni's unchallenged oral evidence as to the amount of the expenditure (which he said was £65,821 in 2007-08 and £1,665 in 2008-09) we had little, if any, evidence as to what exactly the expenditure consisted of. Mr Ayeni gave unchallenged evidence as to the nature of the flats and the building in which they were located which has led us to make the findings of fact set out at [13] and [14] above. However, Mr Ayeni did not give oral evidence, nor was there detailed documentary evidence, as to the nature of the flats or the building in which they were

situated. Nor did we have any evidence as to the amount of rent that Mr Ayeni charged on the flats or the tenants to whom they were let.

Legal principles

57. Flat conversion allowances are a type of capital allowance. Subject to certain exceptions that are not relevant in this appeal, s3 of the Capital Allowances Act 2001 ("CAA 2001") provides relevantly as follows:

> **3 Claims for capital allowances**
>
> (1) No allowance is to be made under this Act unless a claim for it is made.
>
> (2) The claim must be included in a tax return.

58. Section 9ZA of the Taxes Management Act 1970 ("TMA 1970") permits individual taxpayers to amend tax returns. However, s9ZA(2) of TMA 1970 provides that an amendment cannot be made more than twelve months after the "filing date". Therefore, Mr Ayeni had until 31 January 2010 to amend his 2007-08 return and until 31 January 2011 to amend his 2008-09 tax return under s9ZA.

59. At the relevant times, s9B of TMA 1970 provided as follows:

> **9B Amendment of return by taxpayer during enquiry**
>
> (1) This section applies if a return is amended under section 9ZA of this Act (amendment of personal or trustee return by taxpayer) at a time when an enquiry is in progress into the return.
>
> (2) The amendment does not restrict the scope of the enquiry but may be taken into account (together with any matters arising) in the enquiry
>
> (3) So far as the amendment affects the amount stated in the self-assessment included in the return as the amount of tax payable, it does not take effect while the enquiry is in progress and—
>
> (a) if the officer states in the closure notice that he has taken the amendment into account and that—
>
> (i) the amendment has been taken into account in formulating the amendments contained in the notice, or
>
> (ii) his conclusion is that the amendment is incorrect,
>
> the amendment shall not take effect;
>
> (b) otherwise, the amendment takes effect when the closure notice is issued.
>
> (4) For the purposes of this section the period during which an enquiry is in progress is the whole of the period—
>
> (a) beginning with the day on which notice of enquiry is given, and
>
> (b) ending with the day on which the enquiry is completed.

60. Certain textbooks suggest that s9B gives taxpayers a free-standing right to amend their returns while an enquiry is current (although any amendment may not take effect until the enquiry is concluded). It is not entirely clear how s9B (which is expressed to apply to amendments under s9ZA) interacts with the time limit set out in s9ZA(2) and whether s9B therefore applies only to amendments to a tax return that are made by the deadline set out in s9ZA(2). However, it is clear from s9B(1) and s9B(4) that the section does not apply to any purported amendments made after an enquiry is completed.

61. Section 393A of CAA 2001 provided for flat conversion allowances to be available on capital expenditure on, or in connection with the conversion of part of a "qualifying building" into a "qualifying flat", or the renovation of a flat in a "qualifying building" if the flat is, or will be, a "qualifying flat".

62. Section 393C of CAA 2001 contained the definition of "qualifying building" as follows:

> **393C Meaning of "qualifying building"**
>
> (1) In this Part "qualifying building" means a building in respect of which the following requirements are met—
>
> (a) all or most of the ground floor of the building must be authorised for business use,
>
> (b) it must appear that, when the building was constructed, the storeys above the ground floor were for use primarily as one or more dwellings,
>
> (c) the building must not have more than 4 storeys above the ground floor, and
>
> (d) the construction of the building must have been completed before 1st January 1980

63. Section 393C of CAA 2001 contained the definition of "qualifying flat" as follows:

> **393D Meaning of "qualifying flat"**
>
> (1) In this Part "qualifying flat" means a flat in respect of which the following requirements are met—
>
> (a) the flat must be in a qualifying building,
>
> (b) the flat must be suitable for letting as a dwelling,
>
> (c) the flat must be held for the purpose of short-term letting,
>
> (d) it must be possible to gain access to the flat without using the part of the ground floor of the building that is authorised for business use (as defined in section 393C(2)),
>
> (e) the flat must not have more than 4 rooms,
>
> (f) the flat must not be a high value flat,

(g) the flat must not be (or have been) created or renovated as part of a scheme involving the creation or renovation of one or more high value flats, and

(h) the flat must not be let to a person connected with the person who incurred the expenditure on its conversion or renovation.

Discussion

64. Neither Mrs Cawardine nor Mr Ayeni made any submissions as to the procedure for claiming flat conversion allowances, or the requirements that need to be met for those allowances to be available. We considered asking the parties for further written submissions on these matters. However, since the position seems reasonably clear, we have decided not to do this.

65. Although Mr Ayeni genuinely wanted to claim flat conversion allowances in his letter of 20 December 2012, he has not made a claim in a tax return as required by s3 of CAA 2001. We have considered whether Mr Ayeni's letter could be treated as an amendment to his tax returns for 2007-08 or 2008-09. However, we do not consider that it could not least since it was not in the form of a tax return and did not contain a signed statement confirming its accuracy. Even if that letter were capable of being an amendment to Mr Ayeni's tax returns, as noted at [58], Mr Ayeni sent his letter after the deadline for amending his return for the tax years in question set out in s9ZA(2) of TMA 1970. He also sent his letter after HMRC had concluded their enquiry into the 2007-08 and 2008-09 tax years and so s9B of TMA 1970 could not apply.

66. Mr Ayeni has not, therefore, validly claimed flat conversion allowances and that is sufficient to dispose of this aspect of his appeal. Even if we had found that a valid claim was submitted, we would still have found that the allowances were not available since we did not consider that we had sufficient evidence to conclude either that the building in which the flats are located is a "qualifying building" or that the flats in question were "qualifying flats".

Late payment surcharges for 2006-07 and 2007-08 and late payment penalty for 2010-11

67. HMRC produced evidence in the form of schedules setting out Mr Ayeni's income tax liabilities for these tax years, the various payments that Mr Ayeni had made and the way in which those payments had been allocated to his tax liabilities. Mr Ayeni did not challenge that evidence. He did not suggest that he had paid more in income tax than HMRC's records suggested, that he had paid amounts on different dates from those that HMRC suggested or that HMRC had made a mistake in the way they allocated the payments received to his various tax liabilities. Nor did he suggest that there was an arithmetic error in the calculations that HMRC made. We have therefore accepted that HMRC's records were accurate in this respect and that the calculation of the penalties was accurate.

68. Mr Ayeni's sole argument on the surcharges and penalties was that they could not be imposed because, at the time they were issued (11 May 2010, 18 June 2010 and

10 April 2012 respectively), he had not agreed HMRC's calculation of his liability for the tax years in question. However, for the reasons set out below, we have concluded that this is not a reason why the surcharges and penalties could not be imposed.

69. The late payment surcharges (for 2006-07 and 2007-08) were imposed pursuant to s59C of TMA 1970. That section imposes a surcharge on late payment of income tax shown in a self-assessment return (under s59B of TMA 1970) and income tax due under s55 of TMA 1970. The reference to s55 of TMA 1970 is important in the context of this appeal as this provides that, even where a taxpayer is appealing against the conclusions set out in an HMRC closure notice, the tax in dispute remains due and payable nonetheless (see s55(2) of TMA 1970). A taxpayer has the right to make an application under s55(3) of TMA 1970 to postpone payment of tax pending the determination of the appeal. However, unless such an application is made and is successful, non-payment of the disputed tax continues to attract a late payment surcharge.

70. Therefore, even though Mr Ayeni is disputing the amount of his income tax liability, in order to prevent late payment of the disputed amount from attracting a surcharge, he should have applied to HMRC in the first instance to postpone payment of tax. Mr Ayeni did not say that he made such an application and there was no evidence in the bundle that suggested he had. He has not put forward evidence that enables us to conclude that he had a "reasonable excuse" for late payment. We therefore do not accept Mr Ayeni's argument that HMRC were not entitled to levy any late payment surcharge for 2006-07 and 2007-08. However, the amount of the surcharges levied will need to be recalculated to reflect the adjustments that we have decided have to be made to his tax liability for those years.

71. The late payment penalty (for 2010-11) was imposed pursuant to Schedule 56 of the Finance Act 2009 ("Schedule 56"). The effect of that legislation is similar to that set out at [70]. In particular, row 1 of the table set out in paragraph 1(5) of Schedule 56 makes it clear that late payment of an amount shown on a self-assessment return attracts a penalty and row 18 makes similar provision for late payment of amounts due under s55 of TMA 1970. HMRC have not issued closure notices or assessments for the 2010-11 tax year and the late payment penalty has been calculated by reference to amounts shown as due in Mr Ayeni's self-assessment returns.

72. Mr Ayeni said at the hearing that, at the time, he had a genuine belief that he had a loss available for carry forward for 2010-11 and this was why he had not paid his 2010-11 tax liability in full. However, Mr Ayeni's own figures which he had attached to his statement of case suggested that any loss that he thought he had (as a result of his belief that he was entitled to flat conversion allowances) would be used entirely against profits and income of the 2009-10 tax year. We do not, therefore, consider that Mr Ayeni's evidence in this respect can support a conclusion that he had a "reasonable excuse" for paying his 2010-11 tax liability late. Mr Ayeni did not argue that HMRC had reached a "flawed" conclusion on the question of whether a special reduction should be made to the amount of the penalty for the purposes of paragraph 15 of Schedule 56. Our overall conclusion, therefore, is that HMRC were entitled to charge the late payment penalty that they did.

Conclusion

73. Our overall conclusion therefore is:

(1) Mr Ayeni is entitled to a deduction against profits of his property business for 2006-07 of £2,545 in relation to certain property expenses (see [25] above).

(2) Mr Ayeni is entitled to deduction against profits of his accountancy business for a proportion of life assurance premiums of £4,603 in the tax year 2006-07 and £3,218 in the tax year 2007-08. The proportion that is deductible should be calculated as set out at [31] above.

(3) No adjustment need be made to Mr Ayeni's taxable profits for 2007-08 in respect of his argument that his entitlement to a deduction for loan interest has been understated by £2,020 (see [33] above).

(4) To the extent that Mr Ayeni and Mrs Cawardine did not reach an agreement on the deductibility of the £14,857 of expenses (so that we need to decide that issue), Mr Ayeni is entitled to a deduction against profits of his property business only for rates of £808 incurred in 2007-08 (see [38]) above.

(5) Mr Ayeni received additional taxable income of £6,259 (not £12,519) in his property business in 2008-09 (see [48] above). Mr Ayeni can set expenses of £5,290 against that income (see [52] above).

(6) Mr Ayeni had no entitlement to flat conversion allowances in 2007-08 or 2008-09 (see [66] above).

(7) The late payment penalties and late payment surcharges referred to in the table at [5] were due. However, they must be recalculated to reflect the adjustments to Mr Ayeni's tax liabilities as a result of this decision.

74. Mr Ayeni's liability to income tax and national insurance contributions must be recalculated to give effect to the conclusions we have reached as summarised above (and also to give effect to the reductions that HMRC had made prior to the hearing as set out in the table at [5]). However, except insofar as necessary to give effect to those adjustments, the appeal is dismissed.

75. 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.

JONATHAN RICHARDS
TRIBUNAL JUDGE

RELEASE DATE: 17 AUGUST 2016